Associazione Italiana Internet Providers

Directorate-General for Information Society and Media
Audiovisual and Media Policies Unit
avpolicy@ec.europa.eu

Contribution of *Associazione Italiana Internet Providers* (AIIP) to the Public Consultation

CREATIVE CONTENT ONLINE IN THE SINGLE MARKET

AIIP is a no-profit organization associating 53 companies (some listed on the Italian Stock Exchange) active in IP electronic communication services, new IP services and convergent Internet services[1].

INTRODUCTORY NOTE

AIIP appreciates the work performed by the Commission with the aim of assessing the necessary measures to: (i) maximize and foster the availability of creative contents for their on line distribution; (ii) remove any barriers to on-line distribution of the same and (iii) promote information and knowledge among users of on-line services.

Therefore, before answering to the questions, AIIP stresses that some issues raised by the Commission in the consultation document were then neglected (no question was raised on them) although relevant to achieve the above aims.

As a matter of fact, among the issues mentioned by the Commission as preventing the availability of creative content for on-line distribution there is that of "orphan rights", which account for more than 60% of all creative contents available, ad imply very high transaction costs.

As in the case of multi-territory licensing (on which specific questions were drafted at nos. 6-8), the issue of orphan rights implies a revision of the delicate relationship between the need to protect authors of creative contents and to grant third parties access thereto as well as an adequate fine-tuning of the balance between access to contents vs. extension of protection (both territorial and temporal) granted by copyright.

The most appreciated economic doctrine is seriously reconsidering the need for more protection in favour of access to contents, also by reducing the extension (e.g., duration) of copyright. As a matter of fact, excessive protection of copyright would generate misallocation of resources and externalities (e.g., W.M. LANDIS - R. POSNER, *The Economic Structure of Intellectual Property Law*, Harvard University Press 2003). However, the Commission stressed the concerns raised by "orphan rights" (which is due to excessive duration of copyright protection) but then lost the opportunity to start a public consultation also on these issues.

In addition AIIP wishes to stress that if on one side digital environment may dramatically increase the risks of unlawful copying (and fostering authors protection through DRM and TMP is therefore necessary to incentive creation), on the other side it increases the market power granted by copyright to their holders insofar as it permits effective segmentation of users by territory, priority of usage, etc.

Finally, another issue to be faced with by the Commission (although at a different table), in order to ensure competitive distribution of creative content online, is that of net neutrality (i.e, the carriers –or

[1] Among AIIP aims, sect. 1 of AIIP articles of association sets forth: "*encouraging the use of the Internet, of its applications in every form*; … *representing its members before authorities, organizations, institutions*". AIIP is member of Euroispa, the European ISP Association and ECTA, European Competitive Telecommunication Association. www.aiip.it

at least the dominant carrier- should not discriminate quality/price of content carried according to the "owner" of the content or the type of content to be distributed).

DIGITAL RIGHTS MANAGEMENT

1) Do you agree that fostering the adoption of interoperable DRM systems should support the development of online creative content services in the Internal Market? What are the main obstacles to fully interoperable DRM systems? Which commendable practices do you identify as regards DRM interoperability?

AIIP agrees that fully interoperable DRM systems are necessary to foster the development of online creative content services in a competitive environment as to content provision and their distribution.

However, this should not be achieved through *de facto* standards, based on the most spread proprietary protocols, but through a "concerted" definition of open standards, by all operators active in the market or, in the event of not reaching a market consensus, by open standards whose protocols are to be defined by the relevant regulation authorities (such as, e.g., ETSI) since DRM systems are "related resources" ancillary to electronic communications services (see Directive 2002/21/EC on a common framework for electronic communications and services, whereas no. 30 and art. 17).

Economic analysis suggests that the use of open interoperable standards may be the only tool to prevent the creation of domination positions and network externalities on a market featured by strong network effects such as the DRM systems market.

Indeed, the value of a physical or virtual network service, for each user of that network service, grows exponentially with the increase of the number of users connected to the network[2]: therefore, in case of a typical virtual network, such as software (and, consequently, DRM software system), the value of software grows exponentially with the increase of the number of users of such software[3].

De facto standards (i.e, those based on the most spread proprietary protocols) by their own nature may lead to anticompetitive dynamics and raise barriers to entry (having features similar to a natural monopoly) since they would prevent to the competitors access to the DRM copyrighted by its owner.

Consumers just purchase products and show their preferences for technologies embedded into products. In the absence of full interoperability between DRM systems, the DRM system of an operator with significant market shares will be preferred by content owners, by content providers and by service providers, to that of a smaller competitor (even if better or more innovative), since only the former will allow to "communicate" with more users. Therefore, who controls technology may also change the structure of the market (access market, from AIIP point of view).

[2] Supposing that the marginal profit of each user from communicating to another user is "1", the total marginal profit of "n" users belonging to the same network, deriving from the connection of an additional user, is not "*n*1*" but "*n*(n-1)*". See M. L. KATZ - C. SHAPIRO, *Network Externalities, Competition and Compatibility*, 75 Am. Econ. Rev. 1985, 424; S. J. N. ECONOMIDES, *The Economics of Networks*, [1996] Int'l. J. Ind. Org. 673 and *Notes on Network Economics*, in www.stern.nyu.edu/networks; R. W. CRANDALL – J. W. SIDACK, *Competition and Regulatory Policies for Interactive Broadband* Networks, in South.Cal.L.R., 68, 1995, 1213; M. A. LEMLEY -D. MCGOWAN, *Legal Implications of Network Economic Effects*, 86 Cal. L. Rev. 479, 1998; R. MASON, *Network Externalities and the Coase conjecture*, in 44 Eur. Econ. Rev., 2000, 1981; R.A. POSNER, *Antitrust in the New Economy*, http://papers.ssrn.com/sol3/papers.cfm?abstract_id=249316;. A. VALLI, *Profili legali e regolamentari della convergenza di tecnologie e servizi nelle comunicazioni elettroniche: l'impatto della nuova disciplina europea*, [2002] 3 Dir. Comm. Int. 539

[3] See European Commission decision *Microsoft* of March 24, 2004, COMP/C-3/37792, §§ 420 and 437

Proprietary standards in a market featured by (direct and indirect[4]) network effects -such DRM systems- would prevent competition and, therefore, create market inefficiency.

As a matter of fact, experience has demonstrated that the owner of the protocol of the largest PC client operating system was not motivated to disclose the interfaces thereof to producers of work group server operating software but rather tried to limit interoperability between Windows PC and work group servers operating systems to acquire a dominant position also on the market for work group server operating systems[5].

Therefore, the likely risks of allowing proprietary protocols in the DRM systems are clear and only open standards, (by providing full interoperability) prevent the creation of market power and network externalities as well as of any limit to end-users freedom to access available contents in different locations, on all digital platforms and through different devices.

AIIP agrees with the Commission that "*DRM interoperability means that they can choose different devices and still use them with different 'download-to-own' services; for content producers or content aggregators interoperability means they are not locked into one distribution channel that forms a gatekeeper to the marketplace, for device and ICT developers, interoperability means that their products can be used with different content services" and support that the official adoption of such definition for DRM interoperability*" (Creative Content Online Communication, page 7).

AIIP suggest that the Commission regulated that DRM systems should therefore be open, interoperable and user friendly.

In this respect, as stated by Directive 2002/21/CE, technical solutions should be reached by industry standardisation groups and the European Commission financial contribution to R&D projects. Of course, in the absence of reaching an agreement on a standard by the market in a reasonable period of time (i.e., 18 months), open standards protocols should be defined by the relevant regulation authorities (e.g. ETSI).

2) Do you agree that consumer information with regard to interoperability and personal data protection features of DRM systems should be improved? What could be, in your opinion, the most appropriate means and procedures to improve consumers' information in respect of DRM systems? Which commendable practices would you identify as regards labelling of digital products and services?

AIIP appreciates that the Commission working document mentioned the risk of abuse of consumers personal data. In fact, we believe that consumers personal data has to be protected more than the digital content itself.

[4] Indirect network effects occur when the value of a network service to a uses increases as the number and variety of complementary products increase (See *Microsoft* decision, §§449 and 450 and fn. 536). In this case, an indirect network effect would be realized by the spreading of applications programs created to interoperate with the DRM system having the largest customer base (e.g. e-commerce payment systems linked to the DRM system).

[5] See Commission decision *Microsoft*. See also Commission proceeding for IBM abuse of dominant position (case IV/29.479, opened in December 1980), informally closed with the IBM commitment to disclose, in good time, information on interfaces necessary for competitors' hardware and software systems to interoperate with IBM System/370.

The first issue affecting consumer's protection, that should be resolved by the Commission, is to guarantee that no "*watermarks*" could be embedded inside the digital content, in order to trace personal information of the users. This is clearly an unacceptable way to capture data or consumer's choices, against privacy rights.

On the other hands, copyright holders and content distributors have to inform users of on line services in advance of any such activity.

Moreover, the need to ensure priority of protection to privacy rather than to copyright, in the present European regulation frame, has been recently stated clearly by the European Court of Justice in its judgement on case C-275/06, *Promusicae.*

3) Do you agree that reducing the complexity and enhancing the legibility of End-User Licence Agreements (EULAs) would support the development of online creative content services in the Internal Market? Which recommendable practices do you identify as regards EULAs? Do you identify any particular issue related to EULAs that needs to be addressed?

The terms and conditions of EULAs, in the interest itself of content providers and content owners should be simplified. Most of the EULAs bear technical conditions, since such contract models derive from software licenses made for those users who acquire professional applications.

As a consequence, acceptance of the terms of use of digital contents is regarded as a mere process necessary to have access to the on-line services. It is evident that the arrangement of "*clear and lean*" contractual terms, beyond being "*customer friendly*", would introduce major legal certainty with respect to the fruition of highly innovative digital services.

4) Do you agree that alternative dispute resolution mechanisms in relation to the application and administration of DRM systems would enhance consumers' confidence in new products and services? Which commendable practices do you identify in that respect?

AIIP agrees with the Commission analysis and suggest that "*ADR*" clauses are inserted in the terms of use of the digital content services. The above, also to exclude the practice of abusive conditions, such as the forum selection clauses outside the place of residence of the consumers.

However, one should remember that any such clause could not be imposed in no way to consumers which should be free to decide whether to accept it or not.

5) Do you agree that ensuring a non-discriminatory access (for instance for SMEs) to DRM solutions is needed to preserve and foster competition on the market for digital content distribution?

Yes. As a matter of fact, this is the natural consequence to the reasoning developed under answer 1, above, in order to prevent the leverage of "network effects" or the creation of walled gardens to the detriment of competitors.

However, in the event that DRM solutions are owned by vertically integrated operators dominant on the upstream or downstream of the chain, access to DRM should not only be granted on non-discriminatory conditions, but also on "cost oriented" basis to avoid any monopoly mark ups.

In addition, another argument should be considered. It is clear that DRM will increase market power (which is also expressed by power to price discriminate) of copyright owners.

To avoid excessive market power of copyright holders, DRM systems must not place undue restrictions on the use of content. This implies that end-users should be able to make private copies and forward content from one device to another.

If content right holders would be free to price discriminate according to different user categories, user locations, equipment, etc., they could create a sort of "one-off" distribution system, where end-users would not be free to choose between an licence to view the content unlimitedly or just once. This not only would affect consumers rights, but would undermine convergence of electronic communications (which is one of the ain aims to be achieved, according to Framework Directive 2002/21/CE).

MULTI-TERRITORY RIGHTS LICENSING

As clarified above, it is once more necessary to reconsider the balance between interests of copyright owners and the opposite interests of third parties to access to contents, so to ensure efficiency and to prevent externalities and transaction costs. As anticipated, this may render necessary an amendment of copyright law, as it would be necessary in order to ensure "one stop shopping" for multi-territory licensing.

6) Do you agree that the issue of multi-territory rights licensing must be addressed by means of a Recommendation of the European Parliament and the Council?

Although it would be important to introduce the possibility of getting a multi-territory licence on a "one stop shopping" basis, the aim to settle the issue of harmonization of multi-territory rights licensing may not be achieved by a mere recommendation of the European Parliament and Council.

As a matter of fact, a Recommendation of the European Parliament and the Council would not contain compulsory rules and therefore may result into a non efficient mean to address the issue of multi-territory rights licensing.

Although the process of adopting an "*ad hoc*" directive might be time consuming we believe it would more appropriate as to promptly define the matter at stake.

7) What is in your view the most efficient way of fostering multi-territory rights licensing in the area of audiovisual works? Do you agree that a model of online licences based on the distinction between a primary and a secondary multi-territory market can facilitate EU-wide or multi-territory licensing for the creative content you deal with?

AIIP believes that the multi-territory rights licensing may be appropriate to meet the demands of new services by consumers, in line with the ubiquity of such on-line services.

However, the distinction between a primary and a secondary multi-territory market, where the online distribution would be the secondary market and would only be possible after two years time since its first exploitation on a given territory, would relinquish to a minor role any on line distribution of new creative content.

8) Do you agree that business models based on the idea of selling less of more, as illustrated by the so-called "Long tail" theory, benefit from multi-territory rights licences for back-catalogue works (for instance works more than two years old)?

AIIP agrees that business models based on the "Long Tail" theory may benefit from multi-territory rights licenses, not only for back-catalogue works, but also for niche audio-visual new work created by small and medium producers, who have difficult access to wide distribution.

For this reason, the online distribution through multi-territory licences should be allowed earlier than after two years time since its first exploitation on a given territory.

LEGAL OFFERS AND PIRACY

9) How can increased, effective stakeholder cooperation improve respect of copyright in the online environment?

With respect to this question, AIIP agrees with the analysis in the Commission Staff Working Paper accompanying the Communication of January 3, 2008 (pages 28 and 29).

10) Do you consider the Memorandum of Understanding, recently adopted in France, as an example to followed?

AIIP believes that the "Olivennes" MoU is a good start but it is not totally satisfactory for the issue that it intends to regulate.

As a matter of fact, according to AIIP some principles of the "Olivennes" MoU may be agreed upon as reasonable. Among those, the need of a regular judgement for infractions in order to apply the relative sanctions. Moreover it prevents the temptation of the right-owner to make justice by themselves with embedded technical measure adopted to trace traffic or content.

However the French agreement has several critical aspects which should be overcome if all interest should be adequately preserved (e.g., first of all, the public interest to access the Internet and the constitutional right to communicate with the world).

So AIIP is seriously concerned about the 'medieval' sanction to cut the Internet access to the subscriber infringing the copyright who, incidentally, could be different by the real infringer (especially if the access is made through wireless shared connections or from public places like schools or offices).

11) Do you consider that applying filtering measures would be an effective way to prevent online copyright infringements?

AIIP is a fierce opponent of filtering measures for the following reasons.

As a matter of fact, filtering by "blacklisting" on the basis of IP address certain sites which would infringe copyrighted contents may be performed, would certainly have no prejudice for end users (such as it may happen when the problem is caused by one or more specific sites, as in the AAMS Italian case, in order to prevent internet access to sites where sport bids are carried out which – according to the Italian government- would infringe the franchises on public gambling).

However, this may not prove to be an effective solution where copyright is infringed by peer to peer systems and programs without running a central server that can be identified, but which only rely upon peripheral nodes.

In this case, filtering might be performed through traffic shaping and algorithms. However, since these filtering systems would be intrusive of users privacy, any such activity should be subject to prior communication by all Providers to their users.

In addition, since such an activity would be expensive, it should first be clarified who should bear the cost of content protection.

As a matter of fact, any imposition of similar externality on ISPs without rewarding them would infringe art. 295 of the Treaty

In this regard, AIIP suggest that content owners and content providers, in whose interest such an activity ids carried out, contribute to financing the cost of such an activity.

However, AIIP prefers a "prevention" approach to the matter, based on persuasion and education of on line services users not to infringe copyright, rather than an *ex post* approach only based on sanctioning copyright infringements.

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