

October 12, 2009

Open letter to Lord Mandelson: here is how to solve the Internet Music Problem - Legalize It!

Basel, Switzerland, October 12 2009

[Gerd Leonhard](#), Media Futurist

Open Letter to Lord Mandelson, First Secretary of State, Secretary of State for Business, Innovation & Skills (UK)

The Digital Music License (DML) – why and how a new public license for the legal consumption of music on the Internet would provide a solid alternative to the proposed '3 strikes' legislation

Update: Greek Translation [here](#)

Dear Lord Mandelson,

The [proposed "3 Strikes"](#) legislation is flawed in many more ways than I could hope to outline in this letter, and many of these issues have already been addressed in many other places. Therefore I shall provide only a quick summary of some of the key issues, and then move on to describe what a fruitful, realistic and decidedly more pragmatic alternative could look like.

Unauthorized use of music on the Internet is not a technical problem but a business issue. The reasons why the global 'free' sharing of music via the Internet (whether [streamed](#) or downloaded) is growing exponentially cannot be nullified by technological means. Rather, the digital music (r)evolution clearly poses a myriad of business and socio-cultural problems that require us to devise a new social contract that legalizes what people actually do, and then build new business models around it.

Anyone that has attempted to innovate within the music industry ([including me](#)) will attest to the fact that the largest hurdle for the monetization of music on the Internet during the past 15 years has been the astounding absence of new licensing schemes that actu-

ally fit the 'Internet Generation' i.e. the [digital natives](#), and the new ways of consumption that connected consumers are rapidly adopting. Bottom line: *the problem is not what consumers are doing - the problem is that the music industry has not blessed it with a license yet!*

Therefore, any attempt to solve these business issues with technological measures – such as the proposed [3-strikes legislation](#) – would, with utter certainty, be [very expensive](#), have serious social and political consequences and yet fail miserably to deliver tangible monetary results for the content industries or indeed the creators; just like Digital Rights Management (DRM) which was pushed very hard by the music industry for over a decade and has now finally been acknowledged as the [snake-oil it really always was](#). The only outcome of the proposed 3 Strikes legislation would be to further criminalize every single consumer that is interested in music, every fan and every potential customer.

So, again, let me be pragmatic: this idea means no money for the creators, no new revenues for the industry (but even more rejection by the consumer), and still no satisfaction for the music consumers. In my view, the most pressing objective must be to solve the very real problem of how music (and then, other digital content) can indeed generate *new* revenues via the Internet - for the old revenue streams are the past, beyond a shadow of a doubt - just look at what is happening to newspapers and print publishing! Technology will not and cannot solve problems posed by seriously outmoded business practices.

The bottom line: controlling the flow of digital files is 'Mission Impossible'. The challenging but nevertheless indisputable reality is that the very idea of reliably and consistently controlling the distribution of music files on the Internet is basically a technical impossibility as well as a social, political and cultural minefield. Today, the simple act of listening or streaming, watching or reading anything on a connected computer or a mobile Internet device is indeed the same as copying the content; one cannot be done without the other. The Internet is a giant copy machine, by definition, by design, and now... by culture. We may not like it, and we not appreciate it, but just like the railway was hated by the people that made horse-shoes and horse carriages we have no choice but to shift what we

do, adapt, and reinvent ourselves. As your own kids or any so-called digital native will tell you, access is now the same as a copy i.e. ownership - in technical terms and in terms of user behavior and mindset. Crucially, of course, not yet in terms of the existing laws and prevailing licensing practices. And therein lies the rub.

I would argue that we are in fact trying to build a new business on top of the decidedly pre-Internet principle of total and exclusive copyright – a stark dilemma that has proven to create endless friction but produce very few new revenues. The very idea of being able to control the flow of files in order to extract earlier or possibly higher payments from the users is fundamentally flawed, and we must therefore look for ways to [monetize it rather than to prevent it](#).

The value of music is no longer (just) in the copied file. We urgently need to understand and accept that the value of music is no longer (just) in the mere copies of the digital files. Our attention needs to shift from the old - and dying - business of 'selling the copy' to selling everything else i.e. the many other values *around that copy* (some people call that 'service' ;) but starting with providing very low-cost or flat-rated and bundled access, and then creating many new revenue generators on-top of the bundled, legalized access to music. Once legal and unlimited music distribution is build-into Internet access - when Access *is* Content - a revitalized music industry can focus on talent, curation and marketing, i.e. the attention-getting and the conversion of that attention into actual income. And yes, there is serious commercial value in the music industry once we regulate distribution (I call this Music 2.0 - if you care to read my free book on this... [here it is](#))

The DML: the alternative to the proposed '3 Strikes' legislation. 80 years ago, the answer to the challenge of a then-new and vastly popular technology called 'Radio' was to [legalize it](#) and provide new licensing schemes to remunerate the content creators. The same thing happened with CableTV and with the copy-machine, and the very same logic needs to be applied to music on the Internet. [A public, collective, standardized and open license for music on the Internet](#) needs to be either voluntarily created by the music industry, or mandated i.e. enforced by the government - and the sooner the better for everyone. The DML would - similar to the existing radio &

broadcasting licenses that are already in effect around the world - make music available on public, standardized terms and conditions, and therefore allow any and all businesses that want to use music to do so without the utterly crippling uncertainties that exist in the current marketplace.

Revenue shares and flat rates - not fixed license fees per song.

The objective of the DML is to create a new, vast, and constantly replenishing '[pool of money](#)' for music, i.e. to grow the revenue potential along with the growing number of users, as well as via the many new kinds of usages that will be spawned by the DML.

In my opinion, the most crucial component of the DML is this: the license fee needs to be calculated on a revenue-sharing basis rather than on a per-unit i.e. per song fee, whether streamed or downloaded. The [current practice of a fixed per-track fee](#) (usually amounting to about 1 cent U.S. per song, for the use of the master recording) for a stream and around 70 cents (U.S.) for a download has proven to be economically detrimental and utterly unrealistic for the market participants (such as Omnifone, Spotify, Rhapsody, Napster, We7 and Yahoo). Why is this? Because of the still-very-nascent stage of the digital music ecosystem, the fact that large-scale advertising revenues for new forms of media are always 2-3-5 years behind, and given that a very large number of users - potentially all UK consumers - are likely to listen to quite a bit of music in this way.

In its formative stage, this new market does not and will not bear license fees that are fixed in this manner and that are totally unrelated to actual incoming revenue streams. Instead, the DML would need to be calculated on a flat-rate or percentage-of-revenue basis, possibly combined with a minimum 'floor' that could prevent unfair and unintended use of 'free' music as a loss-leader (if needed).

Initial DML's reserved for ISPs, telecoms and operators. Since there are many different kinds of businesses that would benefit from having legalized music available (e.g. telecoms, operators, search engines, social networks and communities, blogs, web portals, on-line magazines etc) but their business objectives and parameters are so vastly different, I would propose to initially make the DML only available to [ISPs, mobile network operators and telecommuni-](#)

[cations providers](#). This would have several important advantages: 1) once ISPs and operators are able i.e. licensed to offer music bundles and flat rates, they will have every incentive and reason to monitor (i.e. count not control!) which songs are used on their network, 2) they have very large user bases which will provide for a critical scale of payments to be obtained immediately (thus significantly lessening the *perceived* threat of revenue loss in the physical music market), 3) they have strong potential for the integration of [next-generation, user-friendly advertising](#) integration 4) and they already have build-in billing and payment mechanisms.

A flat fee license per_user, generated in a multitude of ways. When licensing ISPs, mobile operators and other telecommunications companies it will be crucial to offer flat-rate licenses rather than to pursue revenue shares which are not going to be an acceptable way of generating music revenues from this process, at least initially. Rather, I believe that a fixed, flat-rate license fee per user, per week or month, would be the most suitable way *provided that suitable 3rd parties (see below) will also engage to contribute to the funding of each user's license fee*. We must not simply declare the license fee payments to be the ISP's problem - because it isn't, and because the solution is in the creation of a new Ecosystem, a new business logic, and not in creating tax-like burdens for individual industries.

[Economic experts](#) have already done a lot of work on the flat rate model. Far from being an economist myself, I would add that a payment of 1 GBP (in the UK) or 1 Euro (in Germany, France etc) per week per user seems to be economically feasible; however the exact price point will of course need to be negotiated with all involved parties, and possibly be adapted on a yearly basis until the market is more fully developed and each party's ultimate value position can be determined. In any case -and this is crucial - the DML must clearly be so utterly affordable that every single ISP, operator and telecommunications company would immediately apply for a license.

In terms of the actual use of the music and the subsequent accounting for remuneration purposes, I propose that it should not make a difference if a song is downloaded or streamed (i.e. played on-demand while online), and - similar to CableTV - it should not

make a difference if a user would use music 24 hours a day, every single day, or just download 3 songs every now and then. All music usage would need be counted, anonymized and reported, and artists would get paid fully proportional to the actual use of music i.e. according to their popularity (see below for details).

A calculation example: a pool of 2.6 Billion GBP per year for music, in the UK. As an example, a DSL provider and mobile network operator with 20 Million UK users would need to generate funds to pay for a DML of GBP 80 Million per month, i.e. 960 Million GBP per year.

Assuming, for mere calculation purposes, an average of 50 Million eligible UK residents i.e. a large percentage of the entire UK population (~ 61 Million) generating 1 GBP per week, the revenues for the music industry would amount to a very substantial 50 Million GBP per week i.e. 2.6 Billion GBP per year, which represents almost twice the UK's recorded music revenues in 2008 (1.36 Billion GBP). Any argument of 'cannibalization' of existing revenue streams such as CDs or iTunes would pale against this figure. And yes, iTunes would do just fine with and on-top of the flat-rate: remember they don't sell music, they sell iPods and iPhones!

How to fund a DML of 1 GBP per week per user. The key question is, of course, how exactly the ISPs and telecoms would raise the money to pay for the quite significant cost of the DML, every week, per user. This is a crucial issue since, a gain, under no circumstances should the ISPs, operators or telecoms be made solely responsible for the financial solution of this problem; it is absolutely crucial to position the DML as a business solution that will unlock strong new revenue opportunities and will be more than cost-neutral in a fairly short time. In my view, the job of building the financial support mechanisms i.e. the ecosystem that the DML will require should be handled by a mutually respected, knowledgeable and neutral advisory board whose mission would be to 'collate' this new ecosystem and to get device makers, advertisers, premium-service providers and other interested parties aboard as quickly as possible.

Advertising is only one of the many ways to fund the DML. Of course, as in television and radio, advertising is one of the key fac-

tors that will subsidize the DML fees. The concept of advertising-supported content is not new but what will be drastically different, going forward, is the [type of advertising](#) that we will see on digital networks in the very near future. Concepts such as advertising becoming content, itself (such as in mobile phone applications) and [social advertising](#) will blossom once permission for the legal use of music is given, creating much higher advertising revenues than we are currently seeing online.

The global advertising spend currently amounts to roughly \$ 670 Billion USD, per year. The UK advertising & marketing spend is forecast at approx 25 Billion GBP in 2010 (eMarketer), with - by 2012 - an estimated 25% i.e. 6.25 Billion GBP going to [digital and mobile advertising](#). Yet, digital and mobile advertising would only be one piece of this new puzzle: handset makers could pay subsidies to get preferred i.e. 'presented by' access to users (basically a [network-centric variation](#) of the existing 'Nokia comes with Music' concept), social networks could contribute subsidies to legally integrate ISP-hosted music into their own networks via the DMLs that operators and ISPs would already have; search engines and portals could do the same. Imagine if Google could sit on-top of this new system of fully legalized, feels-like-free music - this is similar to how [Google has already made legal music](#) (streaming and downloading) '[feels like free](#)' in China.

After an initial set-up period, it would be crucial that an ISP or operator that makes use of the DML would be able to fully recover the DML costs through a multitude of new revenue streams, such as next-generation advertising, the sale of mobile applications based on the unlimited availability of music (such as social music and play list applications), subsidies by CE companies i.e. handset and device makers, data-mining and cross-selling (with careful consideration to consumers' data protection and privacy, of course) and various forms of up-selling of other product and services (including music-related premiums) such as the games industry has been offering for the past decade, already, or even by re-packaging some of the license costs to their users.

The DML is NOT a tax. Any indication that the DML essentially amounts to a tax or is yet another compulsory payment scheme levied onto the consumer (such as the existing TV & Radio li-

censes) or a particular industry needs to be avoided, at least in the UK market where such a proposal would probably be politically unwise. The DML is simply a new license that is made available to businesses that want to use digital music, with the funding being generated from the market participants, themselves.

Monitoring of usage and fair payment to content owners. Every song that is performed i.e. streamed or downloaded on the Internet would need to be tracked and accounted for, using already available software solutions such as Gracenote or Shazam. This data would need to be made anonymous using a mathematical formula that would protect each user's private data while still providing actuarial tracking of which song has been used how many times, on any given day, week or month.

Each artist and rights-holder would then receive a monthly payment that is proportional to the actuarial use of their music during each tracking period, e.g. if a given artist's music was used 1.3% of the time (e.g. in any given month), he or she or their representatives (record labels and publishers) would receive 1.3% of the total pool of money collected. All participating creators (e.g. writers, lyricists, composers, producers etc) would get their proportional payment from the same pool. I am advocating a 50-50 split between the composer and the performer (i.e. recording and publishing), at this time. Overlaps with existing rights schemes (such as public performance on the Internet, and so-called web-casting and Internet-radio) would need to be investigated and addressed, as well.

Existing examples: similar models to the proposed DML are already in place, or are being investigated in:

- 1) China, where [Google is providing free and fully legal streams](#) and downloads of music via their Top100.cn property, in return for a share of advertising revenues (and in full collaboration with all major labels)
- 2) [Denmark, where the ISP and mobile network operator TDC](#) has already made music 'free' to all of their subscribers, in return for paying a flat fee per year to the music rights organizations
- 3) The U.S., where Warner Music Group, via [Jim Griffin and the his Choruss project](#), is rolling out a flat ra

te music license for universities and colleges 4) Korea, where [SK Telecom's MelOn](#) service has been providing flat rate music access to most the population ([11 Million subscribers at ~\\$ 5 USD](#) per month) for a few years, already 5) [Canada](#), where the Canadian songwriters are lobbying the government for a new flat for digital music 6) [The Isle of Man Music Flat Rate](#) project, headed by Ron Berry.

I look forward to discussing this with you.

Best regards

[Gerd Leonhard](#)

Please note: this short letter cannot possibly answer every question that may arise if this proposal is further investigated or realized. Rather, I intend to make the case for why the DML would solve the pressing problem of legalizing and at the same time monetizing the many new ways that consumers use music on the Internet. Please keep in mind that most of the suggestions outlined above are still quite basic; prior to making any precise recommendations in regards to possible implementations a lot more research and input from all involved parties is required. Also, while my suggestions should be applied to digital music only, at this time, I do foresee similar developments within other digital content sectors such as motion pictures, TV and books - albeit within a wider timeframe (i.e. 3-5 years).