

Senate Commerce Committee Hearing -- Issues Related to MGM v. Grokster
Testimony of Marty Lafferty
CEO, Distributed Computing Industry Association (DCIA)

July 28, 2005

Dear Chairman Stevens and Ranking Member Inouye:

Thank you for holding this important and timely hearing on issues related to MGM v. Grokster and the appropriate balance between copyright protection and technology innovation. We greatly appreciate your leadership and that of your Commerce Committee colleagues. We are grateful for this opportunity to share the Distributed Computing Industry Association's (www.DCIA.info) perspective on this critical industry and consumer issue.

- **Long-Term Benefits of the Supreme Court Ruling**

The DCIA welcomed the Supreme Court's refusal to rework the Betamax decision, and remains optimistic that the grounds for secondary liability it defined will prove in the fullness of time to be fair and workable.

As the case works its way back through the lower courts, we anticipate clarification of the rules of engagement between content providers and technology suppliers in the digital realm generally, and with respect to peer-to-peer (P2P) file sharing in particular.

We are confident that the Court's decision in the MGM v. Grokster case will ultimately lead to the continued expansion of our industry.

We should clarify that our vision for that expansion does not center on filtering copyrighted works out of the P2P environment, but rather on deploying commercial and technical solutions, which the vast majority of rights holders will find attractive, for secure licensed and profitable redistribution of such works via file sharing.

Given the pace of broadband deployment and Internet-based software development, it is far preferable to focus on achieving the full potential of highly efficient P2P technologies for revenue generation – rather than on shortchanging that potential.

In the file-sharing environment that we are working to establish, rights holders will have the digital rights management (DRM) tools and support services to manage key aspects of every transaction – and to monetize them through such means as advertising support, sponsorships, cross promotion, packaging, subscriptions, and a la carte sales – whether their works are initially entered into redistribution by themselves or by others – including consumers.

We have already urged all affected parties to focus on deploying new business models for content distribution that are non-infringing and expand the marketplace for digital content, and not to pursue legislative intervention at this time, which would only be counter-productive. The private sector, with added clarity that will result from pending lower court outcomes, should manage the process from here, until we reach a later stage as described below.

The MGM v. Grokster ruling provides impetus for the P2P distribution channel to grow and flourish. P2P DRM technologies and micro-payment services have been proven with computer games, software, and independent music and films. Major labels and studios can avail themselves of these tools to develop marketplace solutions – starting today.

To quote Justice Breyer: *"The record reveals a significant future market for non-infringing uses of Grokster-type peer-to-peer software. Such software permits the exchange of any sort of digital file – whether that file does, or does not, contain copyrighted material..."*

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Such legitimate non-infringing uses are coming to include the swapping of: research information (the initial purpose of many peer-to-peer networks); public domain films (e.g., those owned by the Prelinger Archives); historical recordings and digital educational materials (e.g., those stored on the Internet Archive); digital photos (OurPictures, for example, is starting a P2P photo-swapping service); "shareware" and "freeware" (e.g., Linux and certain Windows software); secure licensed music and movie files (INTENT MediaWorks, for example, protects licensed content sent across P2P networks); news broadcasts past and present (the BBC Creative Archive lets users "rip, mix and share the BBC"); user-created audio and video files (including "podcasts" that may be distributed through P2P software); and all manner of free "open content" works collected by Creative Commons (one can search for Creative Commons material on StreamCast)...

I can find nothing in the record that suggests that this course of events will not continue to flow naturally as a consequence of the character of the software taken together with the foreseeable development of the Internet and of information technology. There may be other now-unforeseen non-infringing uses that develop for peer-to-peer software, just as the home-video rental industry (unmentioned in Sony) developed for the VCR."

We hope the Court's decision will lead to a shift away from conflict and toward commerce, and we encourage everyone to come to the table and develop new business partnerships. The MPAA and RIAA and their powerful members control ninety percent (90%) of popular entertainment content distribution and can now move forward to license responsible P2P companies using this highly efficient and extremely popular channel for the distribution of their copyrighted works to create new markets and revenue opportunities.

P2P file-sharing technologies are part of the larger movement to an increasingly distributed computing environment. As the Court affirmed, this kind of technological progress is inevitable – embracing it to harness its capabilities will prove to be much more gainful than resisting or trying to stop it.

While it is regrettable that the earliest outcome of the Supreme Court's ruling likely will be additional backwards-looking litigation – and even more unfortunate because parties on both sides over time have implemented changes in business practices paving the way for them to work together – we can now also engage in more constructive activities without the uncertainty as to what the Court's decision will be.

Specifically, the DCIA has embarked on three areas of activity comprising development of: 1) a comprehensive best practices regime based on analysis of the Supreme Court opinion and concurrences; 2) a promotional program highlighting licensed content P2P distribution, appropriate software usage, and protection of children online; and 3) a technology solution initiative that emphasizes a combination of "offensive" tactics (e.g., placement of DRM-protected and other licensed files at top of search results) with "defensive" tactics (e.g., conversion of unauthorized files into licensed quality-controlled versions) that have long-term viability.

While some either cynically or naively propose forcing a migration to provisional closed P2P systems and/or continuing to use lawsuits and smear campaigns to express their opposition to real industry progress, it is right at this moment that we demonstrate our commitment to more positive alternatives.

Trying to drive global Internet users to abandon an ever-increasing abundance of open and interoperable software applications, which facilitate the instantaneous transfer of files with greater and greater efficiency, ignores marketplace realities, and particularly the effects of an ongoing evolution to low-cost open-source program development.

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It makes much more sense to put resources into projects concentrating on the third area of activity outlined above, which are distinguished by an emphasis on equipping individual files to carry the means of their protection and monetization with them as they are transported over public networks.

DCIA Members have relevant experience that can be applied in this initiative along with their expertise and capabilities to benefit not only legitimate business interests, but also consumers.

It is clear that certain of our industry's opponents are trying to leverage the courts and Congress to perpetuate entrenched but no longer optimal business models, temporarily curtail or slow down technological advances, and maintain hegemony of now outdated processes for content exploitation.

Our opponents blame others for their own failures to exercise responsible stewardship in protecting copyrights during a more than two-decades-long conversion to digital content origination and distribution. They seek to compel third parties to pay for solutions to problems arising from their own neglect, and buttress their campaign with intimidation. Instead, we need to come together to complete the tasks that must be done for all affected parties to move ahead.

It is important that those who oppose the growth of the distributed computing industry realize that our determination to continue developing P2P technologies for legitimate purposes is greater than their determination to restrain, obstruct, or suppress these efforts.

- **Short-Term Concerns About the Ruling**

The divisiveness of what has become a protracted conflict between major entertainment conglomerates and current-generation P2P software distributors has unfortunately been exacerbated by the Supreme Court's decision – indeed the immediate result of the high Court's ruling will be renewed litigation among these parties in the lower courts. More disturbingly, consumer lawsuits by music and movie industry interests are also continuing unabated. None of the entertainment industry's prospective new sanctioned P2P applications has yet to launch, and reportedly, P2P copyright infringement levels continue steadily to increase.

To make matters worse, the business models and technology solutions put forth by the DCIA's now more than fifty (50) Member companies and other qualified independent entities, to provide copyright protection while also promoting continued technology innovation, have not yet received the major entertainment sector support or the media attention that they merit. This despite the fact that they are squarely grounded in marketplace realities rather than wishful thinking, are focused on commercial development that will benefit all affected parties rather than just certain entrenched interests, and are gaining traction as clearly demonstrated by their promising initial consumer acceptance.

The DCIA firmly believes that P2P copyright infringement can not only be dramatically reduced, but that P2P has the potential to serve as a more robust and efficient distribution channel than its predecessors for a greater diversity of content offered in a larger variety of ways. But to do so will require leading entertainment companies, P2P software distributors, and technology solutions providers to collaborate rather than litigate or retreat from participating in fear of litigation. Service-and-support firms need to be allowed to demonstrate that they can provide adequate safeguards through such techniques as P2P DRM and micro-payment solutions, and entertainment content rights holders need to license their works for P2P distribution. Beyond that, P2P can also become an advanced communications medium and collaboration platform.

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Fully addressing the P2P copyright infringement problem for the long-run will require a coordinated, multi-faceted approach that includes content and technology sector collaboration, cross-industry self-regulation, and targeted enforcement. But first, appropriate activities for companies and consumers alike to use P2P in authorized ways for redistribution of copyrighted works need to be established. Users need clearly to be shown appropriate ways to utilize P2P to access and share popular entertainment content. It should be deemed unacceptable, for example, that not a single major label track is yet available in a licensed format in today's P2P environment.

Our view is that it is essential for any proposed solution's viability that it be agnostic in terms of working with current and foreseeable P2P applications, including open source clients and swarming transfer protocols. To be fully effective, it should address both the intentional authorized introduction by rights holders and their agents of secured files of copyrighted works – and their continued protection as they are redistributed from user-to-user no matter what software program(s) are being used; as well as the unauthorized introduction of unsecured files of such works by third parties including end-users – and their continued prevention from being redistributed in unauthorized form.

Not to oversimplify this matter, but it seems to us that two fundamental tasks with respect to securely redistributing copyrighted works via P2P can be defined as:

A) To apply P2P DRM to a file (permitting rights-holder[s] to set price, usage terms, etc.), then create multiple variations of the secured licensed version of the file (supporting robust viral redistribution), and finally seed these initial authorized copies into the file-sharing environment in such a way that they will appear at the top of search results on major P2P software programs (using algorithms unique to each protocol) and other search engines; and

B) To support a system that essentially mirrors the decentralized architecture of P2P applications, extended to include torrent technologies which break files into smaller pieces, that blocks redistribution of unauthorized files of registered copyrighted works (without comprising consumer privacy or interfering with redistribution of other files), that reconstitutes usable quality-controlled portions of copyrighted-works files into licensed versions (to optimize the efficiency of a distributed computing environment), and that provides detailed specific measurement data regarding P2P traffic.

To date, DCIA Members have developed and deployed solutions needed for task 'A' for major P2P software programs including BearShare, eDonkey, Grokster, Kazaa, Morpheus, TrustyFiles, etc. as well as some search engines and websites, despite being hampered by a very limited amount of test content. Examples of companies actively engaged in this – and their solutions, include Altnet – TopSearch; INTENT MediaWorks – myPeer; Shared Media Licensing – Weed; Trymedia Systems – ActiveMark; and Unity Tunes – Unified DRIV. P2P DRM, e-commerce, payment services, and related solutions providers now include an impressive roster of highly qualified firms such as Clickshare, Digital Containers, Digital Rivers, Javien, KlikVU, P2P Cash, Predixis, Relatable, RightsLine, Softwrap, SVC Financial, and Telcordia.

Their models work well mechanically and these companies are poised for enormous growth as the P2P channel matures. In terms of sales volume, which is obviously the more important issue, it is too early to draw conclusions, however, and results-to-date are skewed by not yet having licenses for major label or studio content and not yet having 'B' deployed. New solutions providers are now proposing credible approaches to accomplish 'B', which augur especially well for P2P's future. With these in place, delivery of licensed digital media content, such as through methodologies developed by Unity Tunes, will evolve into a secure user-friendly model for super-distribution by means of most P2P networks. More than anything, the private sector needs time and

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encouragement for 'B' to be adopted and implemented, and for 'A' to be fully developed with the participation of major entertainment rights holders.

In terms of business models and technology support to realize them, DCIA Members are committed to providing the best solutions possible, and engaging on every level to find new and better commercial and technical means to secure and promote licensed content so that it will be possible for every P2P transaction to be monetized with terms and conditions established by rights holders, whether the subject content is initially entered into redistribution by rights holders or by consumers.

The distributed computing industry is actively exploring innovative business models for monetizing copyrighted works in the file-sharing marketplace through advertising support, sponsorships, cross promotion, packaging, subscriptions, and a la carte sales. The industry is building better DRM and payment solutions every day, and is investing in research and development to open the door to greater innovation. We acknowledge the need for solutions that are more user-friendly, transparent, and supportive of fair-use provisions expected by consumers. But most of all what has been missing has been major label and studio involvement as content licensors.

While DCIA Members and others have made significant advances in commercially developing P2P, we also recognize there is still much work to be done beyond attracting the major labels and studios. But these efforts are not the only answers. Effective and complementary self-regulation efforts by the content and technology industries are crucial.

- **Industry Self-Regulatory Efforts**

Specifically, we advocate the establishment of independently coordinated authorities around the globe to help establish P2P file-sharing best practices, and then to serve as an ongoing resource for industry participant certification and dispute resolution. In short, these authorities should provide mechanisms for registering copyrighted works, supporting inter-operability of DRM and payment service solutions, plus monitoring and reporting progress to participants in reducing instances of copyright infringement as a percentage of the universe of P2P transactions. Of course, any technology approved for adoption should be based on open standards and developed with broad input from the affected industries.

As a preliminary step towards achieving this objective, interested parties are now invited to join the MGM v. Grokster Response Working Group (MGRWG), which the DCIA established within weeks of the Supreme Court ruling.

We are especially interested in recruiting additional content rights holders, peer-to-peer (P2P) software distributors, and delivery solutions providers.

The principal goal of MGRWG is to recommend a set of best practices for the distribution of P2P software with the object of promoting its use in ways that do not infringe copyright through affirmative steps taken to foster non-infringement.

Our purposes are to enhance and not diminish benefits in security, cost, and efficiency of P2P software for storing and transmitting electronic files, and to encourage further commercial development of beneficial distributed computing technologies. We intend for end-users to be able to prominently employ ad hoc P2P networks for sharing copyrighted music and video files – with proper authorization.

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The proposed structure for defining these best practices, subject to full discussion by MGRWG, will have four parts: 1) Advertising Guidelines; 2) Protection Mechanisms; 3) Business Models; and 4) Tracking Studies.

Questions to be answered by MGRWG include:

- What kinds of consumer communications are recommended to promote non-infringing usage of P2P software;
- What types of P2P digital rights management (DRM) solutions are recommended so that each transaction of a copyrighted work's P2P redistribution can take place on terms-and-conditions determined by its rights holder(s);
- What revenue sharing opportunities are recommended for content rights holders to fully exploit the possibilities of P2P for licensed content redistribution (e.g., advertising support, sponsorships, cross promotion, packaging, subscriptions, a la carte sales, etc.) plus what kinds of disclosures, if any, are recommended for non-copyrighted-content related P2P revenue generation (e.g., behavioral marketing, VoIP services, paid search, travel applications, collaborative research, blogging, etc.); and
- What industry-wide measurements using such methods as test-cell extrapolation are recommended to track growth trends of authorized copyrighted works transactions as a percentage of all P2P transactions, as well as other key metrics.

Copyright holders should expect that a balance will be struck between their legitimate demands for effective – not merely symbolic – protection of their statutory monopoly, and the rights of P2P software distributors and others to freely engage in substantially unrelated areas of commerce.

Users should be able to continue to search for, retrieve, and store files without involvement of P2P application providers, who should not be expected to monitor or control use of their software with respect to actual knowledge of specific content transactions. Involvement of other members of the distribution chain, however, should provide the requisite controls to enable secure P2P dissemination of registered works globally.

Decentralized P2P software applications should not be expected to reveal which files are being copied and when, but rather related technology solutions should be supported for affiliated third parties to equip individual files to accomplish this as they are redistributed across public networks using P2P protocols. Filtering copyrighted material out of P2P users' downloads or otherwise impeding redistribution by such methods as blocking usage should not be advocated as impositions on P2P software suppliers. Advanced alternatives will more effectively accomplish the underlying goals that previously have led some to suggest these approaches.

Distributors of P2P programs should be able to clearly voice the objective that recipients use their applications to download licensed copyrighted works, and take steps to encourage them to do so, because the file-sharing environment supports secure redistribution. These and other P2P content-reselling entities should be able to competitively market their offerings to prospective users.

P2P distributors should be able to advertise and instruct consumers on how to engage in authorized usage of their software to download and redistribute licensed copyrighted works and to recommend and directly encourage such usage. They should be able to overtly and aggressively take steps to respond to consumer demand for online access to copyrighted material through highly efficient and very popular P2P software.

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As with other DCIA-sponsored working groups, participation in MGRWG is voluntary and open to DCIA Members and qualified non-members. Confidentiality of MGRWG participation will be maintained unless express written authorization for disclosure is given by an individual company in advance. Once the work product, in this case, an outline of best practices, is completed and publicized by MGRWG, adoption and compliance with its recommendations, whether in full or in part, will be a separate voluntary action to be independently decided upon by MGRWG participants (and others) individually.

As the step beyond MGRWG, the DCIA would be willing to serve as coordinator of a multi-industry group constituted with broad relevant multi-industry representation, working in consultation with the Federal Trade Commission (FTC) to help codify best practices.

But in order for self-regulation, business model exploration, and technology development efforts to be successful, ultimately they may well need to be supported by strong federal legislation to prohibit unacceptable practices and empower consumers without threatening the vitality of legitimate P2P usage.

- **Ultimate Role for the Federal Government**

It is our view that business and technical solutions should be encouraged in the private sector, and that a request for any necessary enabling legislation should come only as a last resort and only based on a consensus among affected parties, in this case primarily content rights holders and P2P software providers, but also closely related telecommunications and technology firms, once traction for a particular solution(s) has clearly been established.

Global decentralization of the Internet has reached the point that it would be virtually impossible to stop the proliferation of P2P file-sharing technology or prevent its continuing evolution to higher levels of efficiency.

The channel has already been proven to be a highly efficient medium for marketing copyrighted works. The availability of licensed copyrighted material is assured by the software, which automatically makes copies of works available to millions of other users, who each in turn are required to acquire a license under rights-holder stipulated terms, including usage and price.

The key issue that has perpetuated copyright infringement by means of P2P software continues to be a collusive refusal-to-deal by a handful of large, multi-national, very profitable entertainment rights aggregators, who by their own admission control more than ninety percent (90%) of pop-culture content.

If this continues, what may ultimately be called for is an injunction against "intentional withholding of licensed content from a distribution channel that happens not to be fully controlled by major rights holders."

Copyright infringement is the natural and inevitable by-product of the failure to take necessary steps to protect content from unauthorized duplication and distribution in the digital realm, and then to refuse to license it to willing distributors with proven solutions to problems certain rights holders essentially have created for themselves.

This argument carries through to the fact that these large entertainment copyright aggregators knowingly continue to distribute unprotected CDs and DVDs by the millions, with their only tactics to respond to the massive adoption by consumers of file-sharing technologies being to sue hundreds of users per month for alleged acts of infringement and to sue small P2P software distributors. They themselves are the ones in fact driving consumers to become distributors of

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infringing copies by not licensing a single music track or video under their control for authorized distribution by means of currently distributed P2P software, as well as failing to take reasonable technical precautions to prevent the free and facile replication and redistribution of their works.

It would seem, in these circumstances, that responsible behavior by the major rights holders would be to follow the example of more progressive independents and license their content for the P2P distribution channel, now that the success of such efforts has been demonstrated.

The true problem in the context of P2P software, where program developers and distributors and solutions providers have sought to negotiate with major rights holders, is that they have been met with a refusal to do business or to even engage in technical tests or market trials.

Despite this, these innovative software companies and solutions providers have succeeded in "competing with free" by licensing and successfully facilitating the marketing of lesser known, less popular entertainment content offered by an increasing number of small independents.

This condition has scrambled the venerable structure of copyright-based businesses. There is a growing need to bring the major rights holders to the table with such willing intermediaries, rather than allowing their litigation against consumers and small P2P developers to continue.

To achieve a more comprehensive solution, Congress may eventually want to consider legislative approaches.

Specifically, federal legislation should create incentives for P2P distribution channel participants to adopt best practices. One way to encourage companies to adopt best practices is to provide a "safe harbor" for those who are members of an FTC-approved self-regulatory organization. Under this approach, safe harbor participants would be entitled to avoid the burden of additional requirements, based upon their compliance with specific guidelines.

Thus, federal legislation should identify the basic components that industry guidelines must address, but permit the industry to take the lead in developing the specific guidelines within these parameters.

Here is an outline of what can tentatively be called The Peer-to-Peer Distribution of Copyrighted Works Development Act of 2006:

First Provision: Copyright owners and rights holders, who desire to monetize their copyrighted works by means of digital distribution over discovery and transport protocols, shall register digital files of such works, in a manner that permits their efficient identification during Internet transport, with the Copyright Office, which shall stipulate the technical specifications for such file identification, as may be reasonably updated from time-to-time.

Second Provision: Owners and operators of broadband ISP services and computer hardware and software manufacturers and distributors, shall cause to be deployed, within twelve (12) months of enactment of this bill into law, and to maintain, systems to accurately track the delivery of files identified in Provision I to individual consumers, in a way that will ensure timely billing for registered copyrighted works by means of distribution via transport protocols designed to discover and deliver digital assets.

Third Provision: Copyright holders in Provision I and technology and telecommunications providers in Provision II shall be entitled to establish pricing and revenue-sharing through private negotiations, to recover their costs for registering, tracking, billing, collecting, etc. and to earn a

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profit, provided that prices charged to consumers for copyrighted works through distribution via transport protocols are competitive with alternative distribution channels for such works.

Please do not interpret this proposal as a recommendation for compulsory licensing or a derivative of that type of regime. Rights holders would be able to voluntarily license their content or to withhold it, to set rates and to determine usage parameters, and otherwise to exert control over their copyrighted works, just as they do in other distribution channels.

As a strong proponent of the still nascent distributed computing industry, the DCIA is committed to using its resources to help address the P2P copyright infringement problem from every perspective: business models, technology solutions, self-regulation, legislation, and enforcement. We have started to see progress on all fronts, but much more work clearly needs to be done.

We pledge our support to your ongoing legislative efforts, and look forward to sharing our proposals and working with others towards viable solutions. The DCIA offers whatever assistance this Committee would need with respect to such efforts.

Respectfully,

Martin C. Lafferty
Chief Executive Officer
Distributed Computing Industry Association (DCIA)

Attachments: Testimony of Digital Containers and Scooter Scudieri

Cc: Senator John McCain
Senator Conrad Burns
Senator Trent Lott
Senator Kay Bailey Hutchison
Senator Olympia Snowe
Senator Gordon Smith
Senator John Ensign
Senator George Allen
Senator John Sununu
Senator Jim DeMint
Senator David Vitter
Senator John D. Rockefeller IV
Senator John F. Kerry
Senator Byron L. Dorgan
Senator Barbara Boxer
Senator Bill Nelson
Senator Maria Cantwell
Senator Frank Lautenberg
Senator E. Benjamin Nelson
Senator Mark Pryor