

The Open Music Model

A New Business Model for the Digital Distribution of Music Maximizing Value for Consumers and the Recording Industry

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Introduction

It is clear from the upheaval in the recording industry that the traditional distribution model does not meet the needs of either the industry or its consumers. Many consumers – apparently over 60 million in the United States alone, according to some of the recording industry’s estimates – find that downloading music from free exchanges, primarily *Kazaa*, is the most convenient way to access and store music. The leading commercial solutions, Apple’s *iTunes Music Store* and *BuyMusic.com*, have both experienced stalled sales and failed to spark an interest in the dollar-per-track model that was hailed as the industry’s salvation merely a few months ago. Now the Recording Industry Association of America has launched its infamous campaign of suing individual consumers, based solely on the owner of the IP address used to make files available on free exchanges. So far, all the cases have been settled on the basis of the individual’s financial resources rather than the extent of their violation, and none were tried in court. These lawsuits must necessarily be a temporary phenomenon. They may in fact drive users from the Kazaa platform, but then they will simply adopt file sharing systems which suppress IP-based identification. Whether the RIAA would even be able to win their legal argument is questionable, but the simple technological circumvention of the only weapon in their arsenal renders that point moot.

This article provides a solution. The proposed model may be challenging for some, and is built around the idea that new music (as opposed to deep catalog tracks) will be the primary reason for most people in the future to pay for music, and that music in the future will be thought of more as a service than as discrete goods. It is based on consumer research conducted just over one year ago at the Massachusetts Institute of Technology (<http://shumans.com/p2p-business-models.pdf>) which shows why it could succeed where other solutions have failed. That thesis correctly predicted the failure of all the new commercial solutions in the past year. The Open Music Model is based on the “open clearinghouse networks” idea presented in that work, which should be referenced for the detailed analysis of these issues. The fundamental premise of the new model is:

A peer-to-peer system with a flat monthly fee of \$5 for unlimited downloads, and proportional compensation for content owners.

In addition, it would have the following five “open” characteristics:

1. **Open File Sharing:** users must be free to share files on their hard drives with each other.
2. **Open File Formats:** content must be distributed in MP3 and other formats with NO digital rights management protection.
3. **Open Membership:** content owners must be able to freely register to receive compensation.
4. **Open Payment:** users must be able to access the system using either credit cards or access cards purchasable anonymously in cash from retail stores.
5. **Open Competition:** there must be multiple such systems which can tie into each other’s file sharing databases. It must not be a monopoly through legal design.

The reasoning for these characteristics is based on what surveyed users said they desired in an online system, but has logical justifications as well, detailed below.

Why \$5 per month?

The \$5 monthly fee for unlimited downloads model is based upon survey data which indicated that over 84% of existing file sharers would pay more than \$10 per month for a system which provided access to a complete library of music recordings, rather than just a subset of licensed titles as currently offered by all commercial systems. The \$5 price point is deliberately one half of what the research indicates is a sustainable fee. The reasoning is that if demand turns out to be weaker than anticipated, the system should still be commercially viable. Reducing the price for the sake of this model also recognizes that a powerful network effect exists for file sharing systems and that the primary competitors are distributing the product for free. The greater the number of users, the more powerful such a system would be. Going forward, the monthly fee might be revenue maximizing between \$30 and \$120 per year.

Why unlimited downloads?

The a-la-carte download model made famous by Apple iTunes Music store generated initial excitement, but failed to show any growth or create a loyal user base. Those systems had some good ideas – exemplified primarily in their simplicity of use – but their relatively small amount of content relative to free exchanges, and the expense associated with building up a library of several thousand MP3's – as many users are now accustomed to doing – proved uncompetitive. Systems which offered a capped number of downloads encourage hoarding. Allowing for unlimited downloads acknowledges the ease with which users can already copy several thousand tracks from a friend for free, and allows consumers to shift their thinking from owning discrete tracks to accessing the recording industry's goods as a service – similar to how cable television is sold. Consider that a single blue laser DVD will be able to store more music than most individuals buy in their lifetimes – for example, the top 100 songs of the past fifty years. It is unrealistic to think that individuals copying such a single disc for their friends could be prevented. Therefore, the industry must adopt a model which is cognizant of the future and understands that with greater societal interest in music, there are ever greater opportunities to make money from it. Providing a system which meets users needs, rather than pretending those needs don't exist or arguing that they shouldn't exist, is the only sustainable model.

Why Open File Sharing?

Users say that ease of use and database size are among the most important characteristics to them. Open file sharing ensures the greatest likelihood of a search for any given song coming back with a positive match, which addresses both factors. Systems which only offer explicitly licensed content eventually drive users back to free exchanges to find content that closed catalog systems lack. The goal of a commercial solution should be to make non-commercial file sharing obsolete for most people, and its main advantage should be convenience. A commercial system would be able to freely offer content authentication (searching for a track returns that track listed only once, and where possible, a verified or “authorized” version of it) and would therefore immediately be far more convenient for any user. In addition, links to related merchandise (concert tickets, artists' web sites, giveaways, etc.) would create a far superior overall shopping experience. This superiority to free exchanges is critical considering that deep catalog music is one of the primary areas where the recording industry is particularly uncompetitive. *When it becomes technologically possible for all users to store every song ever recorded on their individual hard drives (only a few years away), where users go to obtain new music will determine where the industry can obtain its revenues.*

Why Open File Formats?

The goal of digital rights management is to prevent one user from giving their content to another. Nearly all DRM providers acknowledge that, in the case of audio tracks (and other commoditized sensory information goods), absolute prevention of replication is technologically impossible. In addition, when one looks at the above cited example of a single disc in the future being able to hold most of the music – in a DRM-free format – that anyone would ever want to purchase through other means, DRM becomes irrelevant for previously released tracks. For new tracks, which users obtain incrementally, the difficulty in copying from a friend or finding a single working copy of the track on a free exchange is generally minimal. Finally, DRM protected tracks are simply inconvenient to use relative to their unprotected MP3 counterparts, and user-hostile technologies are always at a natural disadvantage in being adopted.

Why Open Membership?

The owners of content must be compensated for their work. The number of unique users downloading a given single would be easily tracked by the system, and content owners could be commensurately compensated. The system would allow for any content owner to follow a simple procedure to prove ownership of a given track and claim all compensation associated with it.

Why Open Payment?

Credit card payments offer access to a certain segment of society, but teenagers without credit and individuals without bank accounts still purchase CDs for cash in stores. Teenagers are, of course, one of the primary markets for new music. Currently, the only way they can obtain music online is through free exchanges. In addition to allowing these groups access, subscriptions purchasable with cash could provide anonymous access – similar to buying a CD with cash in a retail store – to those who desired it.

Why Open Competition?

Several commercial exchanges would offer access to the same file sharing network, similar to how there are many Gnutella and FastTrack (Kazaa) clients. They would offer different front-end interfaces, pricing models, and other features, with the same content. This would create competing overall shopping experiences, much the same way different retail stores offer the same CDs for sale. Open competition would also ensure maximum innovation and benefit to consumers (not to mention that any monopoly system would likely be deemed legally in violation of antitrust statutes).

Conclusion: Is this Legal? How much money can be made from this?

Whether this proposal is legally viable is unknown, and there are certainly hundreds of arguments on either side. Unfortunately, most of the major issues relating to file sharing have yet to be tested in any court of law, let alone by the US Supreme Court. Its realization depends upon the cooperation between industry groups and a possible reform of the copyright system. But it does fairly compensate content owners for their intellectual property, so the legal maneuvering required may not be as difficult as the industry consensus building and education required.

However, the financial prospects are compelling. 84% of existing file sharers say they would pay \$10 per month for such a system, without even seeing how much more powerful it would be than any free exchange they've used. At the current estimate of 60 million file sharers, at \$5 per month, this would mean over **\$3 billion** per year – approximately 30% of the industry's current US revenues from pre-recorded music. In reality, the 60 million figure is probably high, but competing systems priced between \$5 to \$10 would be able to generate more revenue for the industry overall. In addition, online distribution is far more profitable than traditional means.

The recording industry clearly has a great deal to gain, and even more to lose. Unless such a commercial system is embraced very soon, its hostile tactics against its own consumers will lead to the development of hackerware-supported systems which offer far more functionality than the free exchanges of today, making switching to a commercial system less attractive than it would be at this moment in time.

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