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LATEST DEVELOPMENTS IN THE NAPSTER SAGA

(Update on Article: Napster and Gnutella : Is distributed file swapping software legal in Australia—Refer to page 9 November 2000 Issue)

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The injunction granted against Napster by judge Marilyn Platel late last year was stayed until the hearing of an appeal. Napster was unsuccessful in the appeal. While upholding the substance of her decision in favour of the RIAA, the Appeals Court has directed judge Platel to rewrite the injunction. Will she shut down Napster or allow it to operate on a new fee-paying basis? Meanwhile, she has appointed a former federal judge, Eugene Lynch, to mediate between the parties.

In the meantime Napster has released further details concerning its agreement with the German music giant Bertelsmann. The deal reflects Napster's vision of a legal file-swapping system. Napster has offered the other record labels a sum US\$ 1 billion over 5 years to run the legal oper-

ation along the lines that it proposes (\$150 million per annum for the majors and \$50 million for the independents). However, the offer doesn't really cover past infringement, and amounts to a proposed new business model for the next five years which the labels are 'invited' to sign up to. In that sense it is arguably not a real settlement of the outstanding legal action. The labels, even if attracted to the New Napster model, are not likely to accept writing off past infringements entirely.

In any case, the labels (in particular AOL Time Warner, Universal Vivendi and Sony) have not been keen to settle and are said to prefer shutting Napster down entirely rather than coming to some agreement whereby Napster continues with its file-swapping service but on a royalty basis. If they do not come to the table and Napster is forced to continue only with content from the labels it has agreements with (apart from Bertelsmann, no majors), it is unlikely to succeed in the long term.

The new 'legal' Napster would charge subscription fees for downloading files. The fees would be scaled, eg a service with limited monthly downloads would cost US\$2.95 to \$4.95 per month, while an unlimited download service would cost between US\$6 and \$10. However, some file-swapping would remain free. For instance, downloading and listening to a sound-file once or twice or for a certain period may be free, but downloading it for storage, making further copies, burning the file onto CD or transferring it to a digital player would require payment. New Napster would use a proprietary form of digital-rights management and security software to limit what subscribers can do with downloaded files. It would look and operate much like the present system, but would depend for continued operation on a new

version of the software that users would have to download to continue using Napster. That software would make certain secondary or further uses of music files impossible without obtaining a decoding key.

The big question is 'can Napster make it work?'. In other words, can they build the software and change their systems to set up a payment - based exchange that is secure and efficient? Bertelsmann seems confident that software engineers can come up with the required copy-protection technology for transferred files. If so, the new paying service would be launched in July. The economics of the paying service look good, as long as the subscriber base remains high enough; but it does not have to be anywhere near the 64million present-day users of the system.

The beauty of the New Napster model is that it allows the highly efficient system, whereby the web itself serves as a giant store and distributor, to continue, saving costs in terms of distribution, promotion, site-building etc. The alternative the labels want seems to envisage label-centered distribution; whatever form it may actually take, they want to control digital distribution based on their own plans. The New Napster model would depend critically for its success on sufficient numbers of present users switching to the paying system; the file-swapping model requires a critical mass of users to function. If it works, other big operators may launch similar services in cooperation with the labels.

In early March Judge Platel will hear argument and decide on the final form of the injunction if the parties do not settle by then. Whatever happens, the future of the on-line music business, and maybe of the music business as a whole, is being written right now. A decentralised, file-swapping service has proved very popular, although admittedly in a non-paying environment. A centralized system controlled from above by the big labels may prove to be less so. The betting is that Bertelsmann will soon have some company in the Napster nest.