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DIGITAL RIGHTS MANAGEMENT: IS THE MUSIC INDUSTRY ALIENATING THE
CONSUMER?

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Abstract <p>Digital rights management (DRM) has been a subject of debate within the music industry for as long as digital music has existed. Some companies still protect their digital releases with DRM while other companies have chosen to gradually abandon DRM. This thesis attempts to answer the question: Is the music industry alienating the consumer? Qualitative research methods were employed in order to identify answers to the research question, including an extensive review of industry journals and the implementation of industry interviews. Analysis of the research findings suggests that DRM does in fact alienate consumers, possibly leading to consumers moving away from using legal digital music retail and distribution models. Discussion is then developed he concerning whether the alienation resulting from the use of DRM is significant enough to overcome the positive effects of DRM on the business models it protects. After evaluating the pros and cons of the several existing DRM approaches and the opinions of industry professionals it seems that the business model that prevails will be a hybrid of several existing models.</p>		
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<p>Tiivistelmä</p> <p>Digitaalinen käyttöoikeuksien hallinta on aiheuttanut väittelyä musiikkiteollisuuden piirissä yhtä kauan kuin digitaalista musiikkia on ollut olemassa. Jotkut musiikkiyhtiöt jatkavat digitaalisten käyttöoikeuksien hallintaa, kun taas toiset yhtiöt ovat hiljalleen luopumassa tästä menettelytavasta. Tämä tutkielma vastaa kysymyksen: Vieraannuttaako digitaalinen käyttöoikeuksien hallinta kuluttajia laillisen musiikin parista?</p> <p>Tutkimuskysymystä tarkasteltiin kvalitatiivisen tutkimuksen avulla. Teemahaastattelujen sekä alan kirjallisuuden tutkimustulosten analyysin perusteella digitaalinen käyttöoikeuksien hallinta todella vieraannuttaa kuluttajia pois laillisen musiikin parista. Keskustelu siitä jatkuu, että onko tämä vieraantuminen mittakaavaltaan tarpeeksi vakavaa, jotta digitaalisten käyttöoikeuksien hallinnasta luovuttaisiin. Erilaisten digitaalisen musiikin jälleenmyyntimallien vertailun sekä musiikkialan ammattilaisten mielipiteiden vertailun perusteella näyttäisi siltä, että toimivin jälleenmyyntimalli tulevaisuudessa tulee olemaan hybridi, joka yhdistää parhaita puolia kaikista tällä hetkellä markkinoilla olevista toimintamalleista.</p>		
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TABLE OF CONTENTS

1	INTRODUCTION	5
2	LITERATURE REVIEW	6
2.1	Overview of intellectual property law	6
2.2	Intellectual property law and the music industry	6
2.3	What is DRM?	7
2.4	Digital rights management in the context of the music industry	7
2.5	The five different approaches to DRM	8
2.5.1	Copy protected pay-per-download	8
2.5.2	Seemingly DRM free pay-per-download	9
2.5.3	Subscription downloading and streaming	10
2.5.4	Super distribution	12
2.5.5	Completely DRM free MP3	14
3	RESEARCH OBJECTIVES	15
3.1	Research question	15
3.2	Research methods	15
4	FINDINGS	16
4.1	Interviews	16
4.1.1	Jani Jalonen – Warner Music Finland	16
4.1.2	Saara Manner – Sony Music Finland	17
4.1.3	Mikko Haapala – Universal Music Finland	18
4.2	Journal findings	19
4.2.1	Arguments and suggestions made by the music industry	20
4.2.2	What direction is the industry leaning towards based on the findings in industry journals	21
5	DISCUSSION	23
5.1	Analysis and conclusions	23
6	RECOMMENDATIONS	26
7	REFERENCES	28

1 INTRODUCTION

Digital rights management has been a controversial subject within the music industry for several years now and therefore a substantial amount of industry professionals have sounded their opinion on the subject in different magazines, conferences and other mediums. The focus of this thesis has been to look for a pattern emerging from these sources and to form an educated answer to the research question based on this data. Studies that focus on the effect of digital rights management on the music industry could not be found. Academic books written about DRM exist, but because the technical nature of this literature does not resonate specifically with the marketing side of the music industry, this literature does not play a substantial role in the research carried out in this thesis. The research conducted in this thesis has been done through qualitative means, focusing on thematic interviews with industry professionals and by reviewing carefully industry journals available to the public (Hirsjärvi & Remes, 1997). In order to find answers to the question presented in this thesis, an extensive amount of background research on the different retail models within the industry had to be conducted. This was accomplished by exploring different existing scenarios of selling and distributing digital music and by searching for and noting the opinions of industry professionals pertaining to the problems of the industry as regards DRM.

The findings from the thematic interviews and industry journals was then mapped out and analyzed. Similarities in the opinions and predictions of the professionals have been compared with each other. The resulting analysis served to develop new insights and perspectives concerning the primary research problem of the study. The thesis concludes with a chapter presenting proposed suggestions for the industry and suggestions for further research that the industry may choose to carry out.

2 LITERATURE REVIEW

2.1 Overview of intellectual property law

Intellectual property laws exist to protect the owners of copyrights, patents, trademarks, industrial design rights and trade secrets from wrongful infringement. The owner of the copyright, patent etc. is the only one who has the lawful right to exploit this protected property. The rights-owner may also give permission for someone else to exploit the protected technology or material, for example in exchange for a fixed sum of money or a percentage of the profits. This grant of rights is usually referred to as licensing. After a certain amount of time, the protected rights, be it copyright, patent or etc. may lose their protection and become part of the public domain. The time period of the protection differs between different copyrights, trademarks and patents.

Intellectual property laws also include moral rights, which are the rights of creators of copyrighted works. Moral rights are generally recognized in civil law jurisdictions. Article 6bis of the Berne Convention states:

Independently of the author's economic rights, and even after the transfer of the said rights, the author shall have the right to claim authorship of the work and to object to any distortion, mutilation or other modification of, or other derogatory action in relation to, the said work, which would be prejudicial to his honor or reputation. (The Berne Convention, 1886)

Intellectual property laws and the measures taken to enforce them vary widely from country to country and it is therefore difficult to give a very globally representative overview on intellectual property law. Many treaties have been made in an effort to harmonize IP laws internationally. These treaties include the 1994 World Trade Organization's (WTO) Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPs), the Rome Convention of the World Intellectual Property Organization (WIPO) in 1961, and the Berne Convention in 1886. The main reasons that have prevented a cohesive international system from forming have been disagreements over medical and software patents and the difference in the scale of enforcing intellectual property laws in different countries. In brief, intellectual property laws protect the owners of copyrights, patents and trademarks.

2.2 Intellectual property law and the music industry

The foundation of commercial exploitation of music lies in the protection given by copyrights and the effectiveness of national and international intellectual property laws. These laws exist to protect copyright holders from infringement. Intellectual property laws as such are quite simple and straight forward. The debate and discussion has generally risen from the different methods of enforcing the

laws and the different measures taken to ensure that infringement is not possible.

2.3 What is DRM?

According to the World Intellectual Property Organization, later referred to as WIPO, digital rights management includes two different things. It can include the (technical) enforcement of usage restrictions (digital management of rights), or the identification and description of intellectual property rights pertaining to works and to parties involved in their creation and administration (digital rights management). DRM may therefore refer to the technologies and/or processes that are applied to digital content to describe and identify it and/or to define, apply and enforce usage rules in a secure manner (WIPO, 2003).

2.4 Digital rights management in the context of the music industry

According to an analysis in Music Week magazine (2007) the increased use of music encoded using MPEG 1 Audio Layer 3, also commonly referred to as MP3, coincided with the startup of Napster in 1999. Napster provided the public a free peer-to-peer Website site that allowed people to exchange and download music with an ease that had never been possible with physical piracy. After suffering for a long time with the rising problem of peer-to-peer downloading, major record companies began their fight against digital piracy. In 2001 the UK's first copy-protected CD was released, Natalie Imbruglia's *White Lilies Island*. Many of these early copy-protected CDs were returned after the disc failed to play in certain CD and DVD players. Copy protection was effectively the first form of digital rights management used by the music industry. The reaction from the public to this kind of modified product was reported to be quite negative by the music retail industry in the United Kingdom. It was argued by consumers that a copy-protected record was actually a worse product than a CD without such protection. Many music industry experts claimed that this was exactly the opposite publicity than what the record industry expected and desired (Music Week, 2007).

It was not long after the first copy-protected release in 2001 when all the major record companies began including copy control software into their products. The industry soon realized that copy protection was not the ideal solution to piracy they were hoping it would be. Sony BMG was the first of the major record companies to face legal action because of their malfunctioning copy-protected CDs. In 2005 Texas attorney general Greg Abbott filed a civil lawsuit against the major label group. Abbott sought in excess of \$100,000 per violation of the state's *Consumer Protection Against Computer Spyware Act*, which came into effect earlier that year (Music Week, 2005). It was concluded that the copy protection software installed on audio CDs was considered to

be “spyware” and had to be removed from use (Music Week, 2005).

Piracy has been a problem for the music industry for decades, and by the end of the 1990s piracy had done so much damage to the industry that even the major record companies began reporting enormous financial losses due mainly to plummeting sales. At the same time marketing and A&R costs were rising or at least staying at current levels. It was commonly acknowledged within the industry that the main reason for this was illegal peer-to-peer downloading combined with traditional piracy in which the product was physically copied. As the new millennium turned and the amount of legal sales of downloads started to gain momentum because of companies like Apple Computer and its iTunes store, the music industry renewed their fight against illegal copying of music (IFPI, 2005). Digital rights management technology was introduced for MP3s. DRM application meant that once you bought an MP3 formatted song from iTunes, you had limited rights to copy and/or use that certain song.

Digital rights management is a very broad concept that has slightly different meanings in different industries and therefore this thesis will not be looking into all kinds of DRM. This thesis will concentrate on DRM in the music industry and especially in digitally downloadable music. DRM in this context is defined as code embedded into an MP3 file that is designed to protect the file from infringement of copyright as defined in intellectual property law.

2.5. The five different approaches to DRM and how they are applied to several business models of selling digital music

2.5.1 Copy protected pay-per-download

This traditional model of selling digital downloads is still the most widespread business model for selling digital music. Nokia’s Music Store, Apple’s iTunes and many other large digital music shops use the copy protected pay-per-download model as their main means of business. In this model the retailer sells a single MP3s or a bundle of MP3s at a fixed rate to the consumer and after the transaction the consumer owns the right to listen to the product with friends and family members for perpetuity. This transaction basically grants the customer the same rights that are passed on when one purchases a CD. The legality of copying this content varies depending on the local jurisdiction. This is the first point where this model gets into trouble. Even though most countries declare it illegal to share copyrighted content in either a profit seeking manner or in a manner that creates harm to the original copyright owner, in some countries making personal copies is considered within the limits of law.

The home-copying issues are fought on a certain moral ground, but the real practical problem

for the traditional legal download seems to be the problems with interoperability between different hardware and software providers. One example occurred when the band *Muse* began selling a download-only single titled *Map Of The Problematique*. A digital bundle of the release, which included a live version of the song recorded at the previous weekend's Wembley stadium show coupled with photos and a screen saver, was released through Muse's official site in DRM-protected Windows Media format only. The amount of complaints from fans on Muse message boards about the fact that the download didn't play on Apple computers or iPods was so large that the Muse website began selling the bundle in DRM-free format soon after, contrary to Warner Music's stance on DRM at that time (Music Week, 2007).

Some experts argue that even in this format's best case scenario, in which the interoperability problems were solved, the reality that the legal product that you purchase has little or nothing more to offer than the illegal counterpart still exists. The pros would basically only include the actual legality of the product and presumably being the more virus free option.

2.5.2 Seemingly DRM free pay-per-download

In the spring of 2007 EMI announced that they would supply an entire catalogue of DRM-free downloads. The agreement was initially limited to EMI and iTunes, but both sides stated that they were keen to extend the initiative further. Apple CEO Steve Jobs (2007) said that he expected 50% of iTunes' catalogue to be unprotected by the end of 2007, while EMI Group CEO Eric Nicoli (2007) suggested the decision to go DRM-free has been met with an overwhelmingly positive response from consumers, artists, retailers and staff (Music Week, 2007).

It was also reported that Apple had quietly installed safety measures with the launch of DRM-free EMI tracks by effectively introducing a new form of copy protection. The situation was that Steve Jobs' company, Apple Computer, had begun selling tracks by EMI artists in a new high-quality, DRM-free format through its newly-launched iTunes Plus service, but every track sold in this format was digitally embedded with the buyer's name and email address. This unannounced move meant that, while EMI was able to offer interoperable music files that work across multiple devices, it was also able to put up a strong disincentive to users who would consider uploading their purchased material onto peer-to-peer websites, since few customers were likely to want their names and email addresses available in the public domain (Music Week, 2007).

The approach that EMI and Apple took is interesting at the least. Calling this new product DRM free would still be overreaching a bit even though this approach takes away a lot of the restricting elements that are usually related to DRM.

Shortly after the move announced by EMI, Warner Music also embraced a limited DRM-free

service by signing up to new digital music site Lala.com. One of the few non-Apple sites to be iPod-compatible, Lala.com sells tracks without DRM, although music can only be downloaded to users' iPods and not their computers. Although much conversation has risen concerning the remaining flaws of these new so-called DRM free downloads, the general atmosphere within the industry and its consumers seems to be positive regarding the direction of these developments. Besides the obvious problems of this DRM solution having no way to copy-control the product, the other clear issue may be the pricing which is presented in this following example.

The standard iTunes AAC format at 128kbps encoding with copy-protection carried a price of 79p, \$0.99 in the US or e0.99 in mainland Europe. In addition, they also offered these new seemingly DRM free tracks at near-CD quality 256kbps encoding, and in AAC format, without copy protection, at a higher price of 99p (\$1.29/e1.29) per track. iTunes customers were able to upgrade their previous EMI track purchases to the premium versions at a cost of 20p per track. And in a bid to encourage package sales, the standard album price (typically pounds 7.99) would remain for the new premium tracks. This meant that it would be significantly cheaper to buy high-quality tracks in album bundles.

Even with the new approach to the MP3 retailing, the interoperability issues had not been resolved completely. Apple still offered tracks in its AAC format, rather than MP3, which limited interoperability. Many popular devices do not support the AAC format. While EMI's new DRM-free downloads could be converted into mp3 format, it is a time-consuming process. The bottom line was that that, while Apple allowed the customer to use iTunes' DRM-free music on other players; it did not go out of its way to make it particularly easy to do so (Music Week, 2007).

2.5.3 Subscription downloading and streaming

Spotify, Napster and Rhapsody employ the model in which the consumer has to pay a continuous subscription fee for unlimited access to the songs in their services database. These services allow the user to listen to samples and obtain downloads of sound recordings and related digital content. To access the service, the consumer must install or activate the online software application and then subscribe to the site as a user, and pay the monthly or annual fee set by the site or be willing to listen to advertisements between songs.

The user may play as many streams as they like and, depending on the chosen service, they can download the songs with certain restrictions while their subscription is current. The service they use will count the number of times that they stream each track for royalty accounting and analysis purposes. The royalties paid for the copyright holders will be dependent of the amount of tracks streamed and downloaded by the users. The user may save the download on to the hard drive of

their personal computer and play it back as many times as they want for so long as their subscription is current. The user may make an unlimited number of downloads while their subscription is current and may copy each download to up to two additional personal computers that they own (i.e. a total of 3 copies). If the user wishes to burn downloads to CDs or transfer them to compatible portable devices they will need to pay for them as purchased tracks. Under these terms it is forbidden to share the downloads with anyone else (Napster, 2008).

The terms and conditions of Napster (2008) define a purchased track as a track that the user may save to up to three of their personal computers and play back at any time, burn to a CD and/or transfer to a compatible portable device. Any security technology that is provided with a purchased track is an inseparable part of it. This means that trying to tamper with any DRM code embedded into the file is considered a violation of the terms and conditions signed by the customer (Napster, 2008 and Rhapsody, 2008).

The most recent model of streaming and subscription services is the model presented by Spotify, MySpace Music and Last.fm. This service gathers its revenue from advertising. Usually these types of services do not require a fee for their subscription. Senior writer Antony Bruno (2008) from *Billboard* magazine forecasts that the model MySpace Music is using will prevail over any other monthly fee subscription services for the obvious reason that MySpace Music is the sole service that not only combines all of the ad-supported free streaming and DRM free download capabilities of these earlier services, but also adds related products like concert tickets and merchandise (Antony Bruno, *In With The New*, *Billboard*, 2008).

As innovative as this model of selling digital music has said to be, it nevertheless presents several problems and inconveniences. The use of a purchased track as presented in the Napster model is a very restricted format from the end user's point of view. It is even more regulated than the original pay-per-download format. The technological aspects of streaming should also be taken into account. The quality of a stream is in fact quite a bit lower than compared to a download, not to mention to a CD as well. Also, the fact that the user has to install the service provider's own software on their computer and cannot listen to the stream in most portable devices will most certainly be a disincentive for some consumers.

The Spotify and MySpace Music models of giving the music away for free to the customer and generating the revenue from advertising seems to be the most intriguing model from the customer's point of view. The music industry on the other hand has serious issues to solve concerning sharing the revenue generated by MySpace Music. Most MySpace web pages have additional content such as blogs, video or pictures on them. How does one accurately define what part of the content is

deserving of what portion of the advertisement revenue?

The revenues of the MySpace Music model are also very closely linked to the popularity of the general site, which means that if the popularity of the MySpace Music site were to collapse, the ad money would fade away but the product on the website would still be free for the public to download. This is a serious consideration for the record companies. It would easily make a monopoly out of MySpace because no new web site using this same model would be allowed to put the same catalogue of free music up for the public to download as MySpace Music can at the moment.

2.5.4 Super distribution

In this approach a consumer pays a subscription fee and is allowed to download mp3s and given the necessary permission to listen to this music on any device he or she owns for 12 months from the date of download (as often as he or she would like to do so); he or she may also pass a copy of the music to up to ten friends without charge but they can only listen to it a restricted amount of times without obtaining a license of their own. However, to reward the consumer as a distributor of the protected files, they will be awarded, either financially or in kind, by the rights holder who benefits from the distribution to friends (WIPO, 2003). Services using this technology are not very wide spread yet, but for example in Europe, Orange (UK) and Telenor (Norway) customers can send preview clips of their favorite songs to friends via text message in their super distribution business model (Billboard, 2006). Some fears have been presented with the potential volume of the super distribution model. Montermob CEO Martin Higginson (2005) warned that super distribution, or sending music files via Bluetooth to phones or other devices posed a bigger problem than internet file-sharing. "In 2010, 2.4 billion people will be able to download music to their phones, the potential is enormous, but we must offer it at the right price," Higginson said (Music Week, 2005).

The sheer technical complexity of this model may prove to be too much of a constricting element for the super distribution model for several years to come. The model can only reach its full potential if it offers the possibility to share complete mp3 files via Bluetooth. The technology to do this is spreading as we speak, nevertheless not a large enough proportion of the music consumers have cellular phones with the required broadband technology. Another challenge for this model is figuring out how the revenue is shared if the consumer gets a cut. Will the final price for downloads have to be substantially higher than in the competing model because of one more party splitting the pie?

One thing is for sure: the super distribution model has the largest amount of DRM protection of

the models presented to date. Functioning DRM is the life line of this model because of the importance of being able to restrict illegal Bluetooth sharing opposed to legal sharing of either samples or full songs with limited listening rights. The fear that Higginson presented earlier should not be ignored. The results of illegal file sharing with the ease and convenience of a properly functioning super distribution system could spell disaster for the music industry very quickly.

2.5.5 Completely DRM free MP3

The format that has no DRM embedded in it is the traditional mp3 that has been widely spread through peer-to-peer types of networks and web sites like the original illegal Napster. The pros of being totally DRM free are quite obvious. There are no interoperability problems with classic MP3s. If one downloads an MP3 it will work just the same on an iPod as it will on a Microsoft-based player. It can be copied just like any other computer file without any restrictions or technical complications. The problem with this model is the fact that pirating this product is very easy. The same qualities that make it convenient to use are the same ones that make it easy to spread illegally.

A legal problem has arisen from the handling of DRM free MP3s. Even though one can now copy legal downloads from a computer to an iPod and vice versa, it is still stated in some local laws that this kind of activity is illegal. Government officials in the UK have stated that the government should draw up a new exemption permitting private copying on MP3 players and other household gadgets. At the moment the system seems to work in a way that the industry prefers to turn a blind eye to private copying and sees it as an acceptable loophole in copyright law. Government officials do not believe it is satisfactory that consumers should be advised by the industry that they can ignore certain parts of the existing law and not others. Basically the law makers believe that without a clear law this establishes a lack of respect for the copyright. The chief of the International Federation of the Phonographic Industry (IFPI) John Kennedy concedes that introducing a law to cover this is a "difficult dilemma," and could exercise lawyers for years. "We as an industry don't have a problem copying on to iPods," he says (2007). David Stopps (2007), head of copyright and contracts at the Music Managers Forum (MMF), is also disappointed that the law officials do not embrace the concept of home copying levies, "On the one hand, the committee says that copying within the domestic home should be legalized, but on the other it says there should be no compensation for this to authors, performer, record companies and publishers," (Music Week, 2007).

Amazon has made a great run for its money by undertaking the selling of DRM free MP3s. In less than a year, it has carved out a digital music market share in the United States of around 8%, according to various analyst estimates (Music Week, 2008).

3 RESEARCH OBJECTIVES

3.1. Research question

This thesis seeks to address the question: Is digital rights management alienating music consumers from the legal purchase of music by restricting the consumers through the imposition of digital rights management?

This research will consider the advantages and disadvantages of DRM embedded releases versus DRM free releases and use these findings as criteria in comparing the feasibility of the different approaches. Exploring these existing scenarios hopefully provide some insight as to whether consumers will accept and learn to use the currently available forms of digital music retail or become alienated by the DRM imposition, and subsequently use less frequently or completely stop using legal music downloads.

The suggestions and opinions of key industry professionals and people with in-depth working knowledge of the business and the issue of DRM will be researched. This information will be accessed through industry journal articles and face-to-face industry interviews as well as interviews published by different medias like websites, magazines etc. If the findings suggest that DRM is alienating the customer from using legal music downloads, suggestions will be made about the future options that the industry has to win back its consumers. These suggestions will be made on the basis of the expert opinions in journals and the one-to-one interviews with industry experts. In the following section an overview will be given of different concepts closely related to the subject of this thesis, starting with an overview on copyrights and intellectual property law.

3.2 Research methods

This thesis applies different forms of qualitative research. Respected industry journals have been researched to find opinions of music industry professionals. The three face-to-face interviews that were carried out were done by using a semi-structured theme interview model where the interview questions have been given to the interview subjects in advance (Hirsjärvi & Remes, 1997). Very little academic literature has been found pertaining to the effect of the use of digital rights management in the music industry. This is why the research in this thesis is heavily weighted on journal findings and interview findings. One of the key factors to understanding the effects of DRM on the music consumer is a comprehensive understanding of the several different operating models of the digital music retail industry. These perspectives can be found in the background research of this thesis.

4 FINDINGS

4.1 Interviews

Three Finnish music industry professionals from three different record companies were interviewed for this project. The answers of the industry professionals will be presented in this chapter to the extent that they are relevant to the research question of this thesis and the contextual framework surrounding the research question. The following six questions were asked from each of the professionals.

1. Is the use of digital rights management alienating the consumer from purchasing legal music?
2. What is the best digital retail format, Pay-per-download, subscription or other? Please explicate your answer.
3. Are you in favour of copy-protection on CDs? If yes/no, please elaborate why?
4. Do you believe that selling DRM-free music can exist as a profitable business model? If not, why not? If yes, please elaborate why?
5. What are the biggest pros and cons in the different digital music retail formats at the moment?
6. What is going to be the business model that will prevail in the future and will it be DRM based? Why?

4.1.1 Jani Jalonen – Warner Music Finland

Mr. Jani Jalonen works as a new business developer for Warner Music Finland. Jalonen feels that DRM does to some extent alienate music consumers from the legal product of the music industry. He elaborates on the subject by saying that in the first couple of years of the current decade, the DRM used on CD albums had a very negative effect on the consumers' experience with the product and that the copy-protection they used actually caused the record companies more harm than it ever did good. He also goes on saying that throughout the history of digital music the biggest road block in the way of expanding the business has been the interoperability problems between different formats and types of DRM technologies, "When buying and using the products are difficult, the consumer will not use them". Jalonen feels that the best model for selling digital music so far has been Apple Computer's iTunes. He goes on to state that iTunes has been superior compared to its

competitors in the field of product development.

Jalonen thinks that subscription services like Spotify have great potential although these models also face a lot of challenges like problems with reporting playlists and revenue distribution. Spotify distributes their advertising revenues as a chunk of money and it is quite a lot of work for the record companies to divide that bulk of money to the artists in a fair manner. Another challenge for subscription models according to Jalonen is the difficulty of acquiring premium customers who pay a fixed amount for their music on a monthly basis. “Once you give something for free, it's hard to start charging money for it afterwards“ Jalonen said.

The interviewee believes that the digital market will keep growing significantly but he does not believe that it will make up for the overall losses of the industry, mainly because of the change in the overall structure of the music industry. He also goes on to say that nobody knows whether selling records – digital or physical - will even be the main source of income for music companies in the future.

Jalonen seems to be quite confident on one issue. He says that DRM will not be used widely in the future of selling music, “The fast paced advancement of technology will make it impossible to try to control music on the digital playing field”.

4.1.2 Saara Manner – Sony Music Finland

Ms. Saara Manner works as a brand manager in digital and brand partnerships at Sony Music. Manner feels that DRM is in fact alienating the consumer from the legal services of the music industry. She says that the only digital music store that has successfully been able to embed DRM into their product is iTunes. This has happened because of the widespread success of the iPod. iTunes and iPods have been a great match, but no other company has had the same kind of widespread platform to sell their music to. All the local DRM embedded music stores have failed because of interoperability problems. “If your product doesn't work on an iPod no one is going to buy it” says Manner.

Manner said that in her opinion the best model of selling digital music has not been found yet. The main focus at the moment is to get people that are using illegal models to shift to using the legal equivalents. The best ways to do this are the different subscription models that are funded with advertising money. One of the current problems of this model for the user is the fact that one cannot

access the music database of the site from their portable devices because the model uses streaming technology. Because of this there will be a demand for pay-per-download services at least as long as technology advances enough to enable streaming for portable devices like mobile phones and MP3 players. She also goes on to say that Sony Music is going to remove DRM from all of its pay-per-download music products before the end of 2009.

Manner concludes her interview by saying that the music industry is paying the price for moving too slowly into the digital world and closing their eyes from the problems for too long. She says that “the generation of people that have learned to use illegal models of acquiring digital music will not be easy to get to use the legal models”. She elaborates that “the key to luring this demographic is via subscription models like Spotify”. Manner also states that Spotify also has the most potential of all the existing models because they can generate good incomes through deals with Internet providers and mobile service providers.

4.1.3 Mikko Haapala – Universal Music Finland

Mr. Mikko Haapala is Universal Music Finland’s digital manager for Finland and the Baltic region. Haapala begins by stating that he does not feel that DRM is alienating the music consumer from the legal product of the industry. “The people who are complaining about DRM are a small but loud minority of music lovers. The core part of the market does not have a problem with DRM as long as it does not interfere with their day to day music listening experience” says Haapala.

He believes that Nokia's Comes With Music service that will be launched soon will have a large impact within the Finnish music industry mainly because of the large penetration that Nokia has in the Finnish market. He added that iTunes and subscription models will continue growing although the key to the monetary value of subscription models will be decided by the amount of monthly paying premium users they are able to attract. Haapala also says that CD copy protection was a good example of how DRM should not be implemented. He goes on to elaborate, “It was an experiment that failed and CD copy protection will not come back.”

Haapala believes that the growth of digital music will explode as soon as the present main problems concerning the current models are solved. He does not believe that the digital music market will ever grow so much that it will reach the same volume that physical sales generated in the golden days of the CD. The reason for this is the simple fact that the market place has changed in structure and that there are so many other competitors competing for the same disposable income

of the consumer. “Nowadays teenagers have to decide whether they want to spend their money on video games, movies or other things. The bottom line is that owning music records is no longer the same kind of priority that it used to be in youngsters' lives,” says Haapala.

He assesses that the biggest problem that different digital music retail models have at the moment continues to be the difficulty of payment online. The older generations are still afraid to give their credit card information to third parties online and the youngsters often don't have a credit card at all. The interviewee states that the key to solving this problem is to get the mobile phone operators to co-operate with music companies. The possibility of paying for music with one's mobile phone is crucial to expanding the market. “Unfortunately the price that mobile operators are charging for this service is still too high for this payment model to be widely implemented.” said Haapala.

Interestingly, Haapala also mentions that one of the main problems in the Finnish music industry is the high value added tax (VAT) enforced on music. All other cultural products have a VAT of eight percent, but for some reason music is taxed at 22 percent. This is something that is lobbied by the industry from year to year but no progress has been made yet. Haapala seems confident while stating that, “We will see a change in this tax policy soon.”

Haapala says that Spotify and iTunes are the best models at the moment and he feels that these models will continue to be the predominant ones in the future. He adds that Spotify and other subscription models will not survive on advertisement income alone. “They have to be able to generate subscription income as well” Haapala said. Haapala concludes the interview by saying that “Because subscription models are going to keep on growing in the market place, DRM is a tool that has to be used in order to make them work.”

4.2 Journal findings

The following segment will contain ideas and thoughts of music industry professionals from people in the music industry that could not be interviewed face-to-face. All of these statements and ideas have been found by means of extensive study of the top industry journals such as *Music Week* magazine and *Billboard* magazine.

4.2.1 Arguments and suggestions made by the music industry

There is very active opposition toward different forms of DRM in the music industry even though most major players in the industry are applying some form of digital rights management.

Consumers are complaining that when you buy a legal copy, it is inferior to an illegal copy because of the limitations set for the consumer. Entertainment Retailers Association (ERA) director general Kim Bayley said in Music Week,: "We are getting the message that people are confused by DRM" (2007) ERA, which is positioning itself as the consumers' friend on the matter, took the issue further by putting it on the agenda at the ERA/BPI (British Phonographic Industry) joint meeting that took place in December 2007.

ERA also wants to turn attention to the immense problem of compatibility between different merchants' products like iTunes and Zune that is causing frustration among the consumers. As an example, the problem with legal downloads is that if the user downloads an illegal mp3 he or she could play it on any MP3 player or media player but if the user bought one from iTunes it would only work on iPods and iTunes software and vice versa with Microsoft's Zune music store. The retail organization publicly set out its case in a letter to the *Financial Times* in which it urged record companies to adopt MP3 as the universal download standard, suggesting that consumers were perplexed by the proliferation of different DRM systems and end up giving up on legal downloads. Bailey (2007) also says about the industry: "We have to trust people. In the CD world we trust people. CDs are DRM free. It should be the same in the digital world." The point is well understood by many more liberal industry professionals even though many say that Bailey should know better than to say that CDs are DRM free, because some companies are still implementing copy protection software on their CDs, which effectively is just one form of digital rights management. Such a view, however, may run in to opposition at the BPI? While the organisation is broadly DRM neutral, reflecting the differing views of its member record companies, chief executive Geoff Taylor (2007) says the following about ERA: "ERA is missing the point in blaming record labels for the lack of interoperability," he says. "Its target should be online retailers with proprietary DRMs who refuse to license their technology or let it inter-operate with other systems" (Music Week, 2007).

Deputy-director of technology for IFPI (International Federation of the Phonographic Industry) Dr. Richard Gooch takes a very different stand on DRM in his article in *Billboard* magazine. He portrays that DRM is driving new flexible music services for consumers in the digital market. He also states that DRM has proved to be the framework that has allowed today's thriving legal digital music scene to flourish, making more music available to the public than ever before in more formats and distribution channels. It is DRM that gives consumers different options and helps

different kinds of services compete (Billboard, 2006).

EMI Group CEO Mr. Eric Nicoli (2007) said to Music Week Magazine that it was important to educate customers about the value of music, rather than presume guilt and restrict their ability to transfer music. "This is still an industry in its infancy," he added (Music Week, 2007).

This comment is in great contrast to the comments that Warner CEO Edgar Bronfman (2007) gave soon after the statement of Nicoli. Bronfman stated to Music Week Magazine that, "The notion that music does not deserve the same protection as software, film, video games or other intellectual property, simply because there is an unprotected legacy product in the physical world, is completely without logic or merit" (Music Week, 2007).

Warner soon jumped from being a slow shifter to making a deal with MySpace Music for a free streaming service that is funded with ad money. They argued that by finding a way to monetize the manner in which consumers are already interacting with music rather than trying to force them into a business model convenient to the industry, they can finally tap a vein of hope for their struggling fortunes. Warner Music Group chairman, CEO Edgar Bronfman Jr. (2008) perhaps said it best in his statement distributed with the MySpace Music press release: "This venture may provide a defining blueprint for this next important stage in the evolution of social media, benefiting consumers, artists and music companies alike."

This model could have serious implications for the digital industry as we know it. First, it might mark the end of the digital warehouse model like iTunes and Amazon. Both will remain important contributors to the industry's revenue for the next several years, but that model is fading away and we are unlikely to see new, similar services come to light. Second, subscription services like Napster and Rhapsody are even more vulnerable. They should have worked to integrate their service more deeply with an existing social network, as Rhapsody is trying to do with MOG, before those social networks develop their own solution like MySpace Music has. It also seems like these older subscription models need to immediately find a way to eliminate the monthly fee in their service or it will find itself competing with another free opponent, this one being legal (Billboard, 2008).

4.2.2 What direction is the industry leaning towards based on the findings in industry journals?

Shortly after the decision by EMI to begin offering the seemingly DRM free pay-per-download format on iTunes (as presented in the background research earlier in this thesis), the other majors made the same decision, the last one being Sony-BMG in January 2008. All of the majors adhered

to roughly the same pricing system as EMI in which the new format was slightly more expensive as the original DRM equipped format (Billboard, 2008).

The older advocates of the subscription model, Napster and Rhapsody, are facing serious times with the launch of Nokia's Comes With Music service and MySpace Music. The Comes With Music service proposes to include the price of a one-year unlimited music subscription service in the cost of the mobile phone that supports it. As of now, all major labels except EMI are onboard. Many questions remain about how the idea will be implemented at launch, which is expected in October 2008 in the UK. How much extra will the device cost? How much will labels get? How free is the consumer to use the content they acquire? Nevertheless the main issue here is the model, not the execution. Labels are shifting strategy and focusing on getting a cut of the overall cost of either devices or services that use their content, rather than just the cost of the music itself (Billboard, 2008).

MySpace Music, the second big time player to enter the digital music retail business is also launching its new venture soon. MySpace Music is a joint venture with the major labels and the original Newscorp affiliate MySpace. The majors in the joint venture have agreed with MySpace that they will profit not only from a cut of the ad and sales revenue, but also in the underlying revenue the venture receives, even from content contributed by other of the MySpace Music services content.

Mr. Charles Caldas (2008), CEO of indie music licensing group Merlin, criticized this arrangement, arguing that it allows major labels to profit from the use of indie music at MySpace Music without giving independent record companies the ability to profit from the venture as equity partners. "Without an equitable participation by independents, that creates a situation that is both unhealthy and dangerous," Caldas says, acknowledging that Merlin is nonetheless in licensing talks with MySpace Music (Billboard, 2008).

By contrast, Orchard CEO Greg Scholl (2008) downplayed the immediate importance of securing an equity stake in MySpace Music. The opportunity to create an ancillary revenue stream and ignite growth in the sector is, on balance, more important to our clients than holding out for an equity stake of uncertain future value that will likely never come to pass Scholl says. "We will continue to press our case for equity or profit sharing for the independent sector, but in the meantime, we will ensure our clients prosper from the value MySpace Music creates." Scholl goes on to say (Billboard, 2008).

5 DISCUSSION

5.1 Analysis and conclusions

In the three face-to-face interviews carried out for this thesis there were a lot of similar thoughts that emerged from the interviewees. Surprisingly, one of the three interviewees felt, that DRM does not alienate music consumers and two of the interviewees believed that some degree of alienation has happened and will keep happening if DRM is enforced. One of the three interviewees was convinced that consumers are not alienated from using the legal products of the music industry and the other two felt that DRM has alienated the music consumers to some extent. Jalonen from Warner Music, was most opposed to DRM of the three interviewees, and he believed that DRM will not be a part of the future of digital music retail. Interestingly, he did not go on to elaborate on how certain subscription models can function without the use of DRM. Manner and Haapala believe that subscription models need DRM to function. Manner was convinced that the pay-per-download model will not have DRM in it in the future. All three of the interviewees agreed that the digital music industry will keep growing as problems with interoperability and payment methods are solved but at the same time all of the three were skeptical on whether the music industry in its current format will ever reach the same volume as in its best years in the mid-nineties.

The opinions of the interviewees seemed to reflect the findings from the review of music industry journals. The majority of the opinions of music industry professionals seem to be leaning on the side of a DRM free music environment although most of the professionals also go on to say that certain models like the subscription model need DRM to function.

The opinion of Universal Music's Mikko Haapala seems to be the most controversial and opposite to most of the opinions found in journals and other interviews. He fails to elaborate on his opinions concerning confusion among consumers that Kim Bayley (2007) from ERA so clearly portrays in his interview with Music Week. Haapala also goes on to ignore the interoperability problems by stating that everything is fine as long as the DRM works with the hardware and the DRM does not clash with the user experience of the customer. As was presented in the background research chapter of this thesis, these interoperability problems still exist and are only now after many years beginning to be solved.

It would seem like DRM is in fact alienating the consumers from purchasing legal digital music. Most of the debate on the subject seems to rise from whether the degree of this alienation is severe enough to actually have a lasting and profound effect on the industry. Some industry experts

like Haapala from Universal Music and Edgar Bronfman Jr. from Warner Music believe that music must be protected just like all other copyrighted products and people will understand that and accept the restrictions that follow. Other experts like Nicoli from EMI music and Jalonen from Warner Music Finland deem that the industry must abandon DRM before the consumer decides to completely abandon the music industry.

While the digital retail models are being tested by the markets it seems like we are facing a divided music industry, where most independent labels are opposed to copy protection, EMI has fully embraced - and Universal is experimenting with DRM-free downloads. Sony BMG is going from being supportive of DRM to slowly getting rid of DRM on their pay-per-download releases, and Warner has shifted from strongly opposing the dropping of copy protection to dropping it completely in their newest venture (Music Week, 2007).

Achieved industry analyst and senior writer for Billboard magazine Antony Bruno (2007) suggests that digital rights management technology has reached a fork in the road. One road represents the status quo, locking music with protective software that requires devices to have the corresponding key to play or even recognize the files, yet restricts users from transferring tracks to different devices. The other road represents a radical new future: unprotected music files that let users freely play their music on any device and distribute it online, but allow labels to identify, track and potentially monetize that activity. Which road gains the most traffic largely depends on how the industry reacts to the reactions and results of such pioneering acts as EMI's recent decision to sell unprotected digital music via iTunes and other services (Billboard, 2007).

It seems like even in the divided music industry a consensus has been reached that if DRM is to be used widely in the future of selling digital music, a solution to the current interoperability problem needs to be found. As long as music purchased from sources other than iTunes will not work with the iPod, the outlook of the DRM protected pay-per-download model is bleak. The consensus within the industry seems to be that DRM is in fact alienating the consumers from the legal product of the industry, at least to some extent. The debate seems to now dwell on whether this is a big enough problem for the industry to completely abandon DRM or to work on solving the problems of existing DRM. There are two schools of thought on the subject. On one hand there is the argument made by Haapala from Universal Music Finland who says that DRM is not the reason for declining sales and that the people protesting are merely a loud minority and that the main core of the market are not alienated by the use of DRM. On the other hand there is the EMI Groups approach which is heavily leaning towards completely getting rid of DRM in digital music.

What about on the other side of the crossroads, the one that Bruno is suggesting? Even if every record label were to abandon DRM and sell unprotected digital files, they'll still expect to make

money by doing so. In a world where music is unrestricted, the definition of DRM would have to change from a means of control to a means of monetization.

Some DRM experts, such as Bill Rosenblatt (2007) of GiantStep Media Technology Strategies, say there could even be a schism among the major labels where some follow the road first suggested and stick with DRM and others the road that abandons DRM. If this were to happen, the final winner of this format war would be decided by the market. The question is, will the consumer stick around to see the major companies fight for several more years putting aside the will of the actual core of the market – the customer (Billboard, 2007).

6 RECOMMENDATIONS

It seems there are three factors that need to be carefully taken into consideration by the music retailing industry while developing a successful sales model in order to satisfy the consumer rather than alienating them from the process with excessive red tape and consumer restrictions. These factors are convenience, content and price. Convenience includes aspects like an accessible and easy to use software platform, total interoperability with different music players and portable devices, and ease of payment. One of the main reasons why Amazon was able to grow their market share so rapidly was the 81 million people that already had their credit card information stored in the Amazon database from their previous purchases. Once again, content is key. A functioning digital retail model will not work unless it features a catalogue of songs that truly satisfies the average consumer. This would seem to require the catalogues of all the major labels and the larger independent labels at the least. The issue of price does not necessarily have to focus on how cheap or expensive the service is. More important is getting the consumer to feel as they are getting some return on their investment. The other important aspect is to have a consistent and logically understandable pricing system. It has already been proved that the public is willing to pay for digital music, which quite frankly is astonishing when considering how clumsy and restrictive the product is that they have received so far. Pulling together the thoughts put forward by the industry and the experiences that have been observed from the market, the model that will thrive and be the most successful will no doubt be one that brings together the best aspects of all these different digital retail models.

It seems that the future model will be a subscription service that applies factors from the pay-per-download model (with or without DRM) and even the super distribution model once mobile technology is widespread and efficient enough for it to work in the core of the consumer market. In this subscription service the basic subscription plan would perhaps not cost the consumer anything - the consumer would only have to submit his or her account information and be willing to accept some advertisements while using the service. The foundation of the funding for this model would come from advertisement money and from other premium services provided to the consumer for extra cost and would be divided to the participating companies according to tracking of what songs get played in what ratio.

In addition there would be a pay-per-download service that would offer interoperable music files that may or may not be embedded with fingerprinting DRM to be able to track the sold files, were they to be distributed in an illegal fashion. These pay-per-download files would cost the standard amount defined by iTunes and other market leaders. The incentive for purchasing them

would be the possibility to listen to the song on one's portable device, burn it to a CD, and of course the fact that the sound quality would be better compared to the streamed equivalent.

In the future this model should also attempt to tap into the huge potential of the super distribution model. The challenge with the super distribution model as earlier noted is the heavy amount of DRM that has to be embedded into the product to keep from it turning into a free-for-all file sharing medium.

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