

# Napster offers record companies a new commercial arrangement

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The Internet music swap service Napster and its 50 million-plus users face a new court injunction that may effectively close down the service as it presently exists. Whatever the eventual fate of Napster, however, the naked economic interests that lie behind the invocations of artistic copyright and intellectual property on the part of the music industry giants are increasingly clear.

A February 12 ruling by a three-judge panel said that Napster technology enabling millions of users to trade pirated music over the Internet represented a mass violation of record label copyrights. The case was sent back to Judge Marilyn Hall Patel, asking her to more narrowly focus her original injunction that ordered Napster to prevent the trading of copyrighted material, while respecting the technological limitations Napster faces in policing its service.

Patel is anxious that some form of agreement is reached between Napster and the major record labels. Within days of the ruling Patel said, "I think they [Napster and the recording companies] should all work out something." In an implicit criticism of the record companies, she said, "There's no such thing as a free lunch, but sometimes lunch is more expensive than it should be."

It has since emerged that the judge had ordered the two sides to meet even before the 9th US Circuit Court of Appeals made its ruling. According to Russell Frackman, an attorney representing the recording companies, Patel appointed retired federal judge Eugene Lynch as mediator. Frackman said he attended a meeting with lawyers from Napster and other plaintiffs at which Lynch explored potential mediation.

Frackman said, "It was always our position with Judge Lynch [that] the only thing that could be mediated were damages for past infringements and the form of injunctive relief going forward. Any business resolution that Napster might be interested in would have to be discussed... with individual record companies."

Napster has already acknowledged the court ruling means it cannot continue allowing the unlimited free exchange of music between users, and the company has formed an alliance with the German media giant Bertelsmann AG to develop a subscription-based service. Napster officials have now outlined a strategy they hope will provide the possibility of a deal with

all the major labels. The company said it is willing to pay the recording industry \$1 billion over five years to end the lawsuit. This breaks down to \$150 million per year paid in licensing fees to the major record companies and \$50 million per year in fees to independent labels and artists.

Napster's plan is to create a multi-tiered subscription based service. CEO Hank Barry has indicated that a basic service that limits the number of file transfers would cost between \$2.95 and \$4.95 per month, with unlimited access costing between \$5.95 and \$9.95.

Speaking for Bertelsmann, chief executive officer Thomas Middelhoff said, "I believe it is time for the music industry and Napster to create a win-win strategy for users, artists and the labels." But the initial response of the recording giants has been to turn the offer down flat.

Some of the world's largest record labels, including Universal Music and Warner Music, issued statements expressing dissatisfaction with the offer, and Sony Music Entertainment said that \$1 billion was inadequate. "It's obvious to anyone that follows the music business that the numbers Napster proposed on Tuesday do not make sense for a \$40 billion industry," Sony said.

What will determine any final agreement is not only the amount of money offered by Napster but also if, and how quickly, the major labels can develop their own online music services. It cannot be ruled out that they will follow the path taken by Bertelsmann and decide that it is better to use the technology developed by Napster—not to mention its 50 million-strong user base—rather than attempting to reinvent the wheel.

## **Napster II would curtail the free exchange of music**

Despite the company's claim to be safeguarding the "Napster Community", the details of the planned changes to the service would severely restrict users' access and ability to exchange music online.

Judging by the response in several Internet discussion groups, and the results of numerous surveys, a majority of Napster users would not object to paying a small subscription fee for access to the service as it presently exists. But though the planned changes would be almost invisible to the user, what has been dubbed "Napster II" will be very different to its predecessor.

Firstly, users will have to download a new version of Napster programme, since current versions and, probably, open-source Napster clones will also not work with the new system. Once installed, the new software will appear to work as before—a search engine will bring up a list of users' song files from a central index kept at the Napster headquarters. Users will still be able to download the song files from any other user's computer. It is upon downloading the file that the changes to the Napster system would become apparent.

As a song is requested from another user's hard drive, the Napster software will encrypt the raw MP3 file on the fly, then send the scrambled result to the person who requested it. Each Napster user will have a unique software "key" that unlocks the encrypted file and permits the song to be played. Having downloaded a song, however, the user will not be able to email it to anyone else and will be prevented from downloading it to a portable MP3 player or burning it to CD unless he or she has paid the appropriate subscription fee.

The new model is even more restrictive than the way CDs or cassette tapes are presently distributed, since there is nothing built into a CD or tape that physically prevents it from being copied.

#### **Legal problems far from settled**

The proposed model may yet prove attractive to the recording giants, because it addresses the issues central to their dispute with Napster.

Contrary to the public statements of concern over the rights of the artist, what has troubled the media moguls since the emergence of Napster is the threat posed to their profits should they lose control over distribution channels in the era of the Internet and mass communications. The ability of an individual to make a cassette recording, or even burn a copy of a CD, and exchange it with friends is hardly likely to make much impression on the revenues of Universal or Sony. In the case of Napster, and the technology on which it is based, however, the utilisation of the Internet as a means by which millions of people worldwide can exchange music will have an impact.

Though studies show that Napster users generally buy more music than others, and that sales of CDs continue to increase, this could change with the emergence of affordable new portable devices for playing MP3 files and faster Internet connections. At the very least, the emergence of Napster has fuelled the demand to end the extortionate mark-up on music CD prices that exists at present.

If the major labels do not participate in the new system, and a court injunction is issued ordering Napster to block access to their material, Napster users would be limited to content provided by Bertelsmann and the smaller labels TVT and eDel with whom Napster has agreements, as well as independent artists seeking a broader audience for their work. In this event it is doubtful that Napster would maintain its user base and could lose out to alternative systems that have emerged, such as Gnutella or Freenet.

Republican Senator for Utah, Orrin Hatch, voiced concerns about this in the US Senate on February 14. Announcing plans to hold a Senate hearing to examine the impact of the February 12 ruling, the head of the Senate Judiciary Committee warned that it could cause more problems for the record industry if Napster is forced to shut down. "My feeling about this 9th Circuit decision is a gnawing concern that this victory for the labels may prove short-sighted," Hatch said. "I fear that this consumer demand will be built by Napster clones like Freenet or Gnutella, and such a development would further undermine copyright online."

In addition to the legal problems, very real technical difficulties confront Napster in implementing its new model.

Firstly, the extra step of encrypting the files could well slow down the system considerably, making it annoying, if not completely unusable.

Even if the new system can be deployed without a noticeable degradation of service, it may not succeed in its goal of preventing the broader distribution of copyrighted music. Digital-rights software of this type is notoriously vulnerable to malicious programmers. Furthermore, every time a computer plays a song, the music will exist somewhere in a decrypted form and it would be possible to capture the data and convert it back into an unencrypted MP3 file. The Toronto-based company High Criteria is already selling a program via the Internet for \$11.95 that can do this.

The reaction of the recording giants to the emergence of Napster is indicative of the conflict between private property and the new technologies spawned by the emergence of the Internet.

Napster is only the most well known application of a technology known as Peer-to-Peer or P2P networking. Its great advantage over previous systems is the ability to make use of the processing power and storage capacity of the millions of computers, including home PCs, connected to the Internet at any one time. In doing this, P2P comes close to realising the full potential of the World Wide Web as envisioned by its inventors—the ability to make every computer a broadcaster as well as a receiver of information.

Such a development inevitably comes up against the restraints of the profit system and meets with the opposition of big business. Today the main concern of the giant media conglomerates is to prevent any new technology diminishing their massive profits from the distribution of music. But with the wider availability of high-speed connections—at least in the advanced countries—they are already taking measures to prevent the free distribution of film and video over the Internet.



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