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A Rule of Reason Approach to the Antitrust Issues of the
Google Book Search Settlement

Kelvin Hiu Fai Kwok*

I. INTRODUCTION

This paper examines, from an antitrust perspective, the recent controversy of the Google Book Search (GBS) settlement in its broader context of copyright collective administration. It argues that courts should view competitive concerns of the settlement pertaining to exclusivity and pricing as ancillary restraints to an overall procompetitive copyright collective, and hence courts should analyze the settlement using the rule of reason instead of condemning it as per se illegal under antitrust law. In particular, I will examine closely the following five issues: (1) How does the GBS settlement relate to ASCAP and BMI blanket licensing in the music performance context and copyright collective arrangements in general? (2) Why should courts apply the rule of reason (as opposed to a per se illegal rule) to analyze anticompetitive features of the GBS settlement and other copyright collectives? (3) What is the proper antitrust baseline against which a rule of reason analysis is conducted? More precisely, should an antitrust court ask whether a collective scheme is overall efficiency-enhancing or should it look for a “less restrictive alternative” which is equally capable of achieving procompetitive goals, albeit in a less anticompetitive manner? (4) How should a court identify and weigh anticompetitive justifications and procompetitive objectives of an ancillary restraint? How can a “reverse” rule of reason be adopted to help courts and parties to identify efficiency modifications to an existing collective arrangement? (5) What would be the result if the rule-of-reason analysis is applied in the specific context of the GBS settlement in evaluating the competitive effects of allegedly anticompetitive restraints and proposed modifications?

The remainder of this paper is divided into four parts. Part II introduces the background and salient features of the GBS class action

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settlement, and discusses Judge Chin’s recent decision to reject the settlement agreement. Part III examines the relationship between the GBS settlement, copyright collective administration, and the antitrust rule of reason: specifically, it seeks to draw a comparison between the GBS settlement and the ASCAP and BMI blanket license in the music licensing industry, define the proper antitrust baseline for evaluating ancillary restraints to the GBS settlement as a copyright collective, and formalize a step-by-step process by which the antitrust rule of reason (or reverse thereof) should proceed. Part IV applies the rule of reason framework developed in the previous Part to analyze two central anticompetitive concerns of the GBS settlement: (1) Google's de facto exclusivity over orphan works and pricing mechanisms for consumer purchases and institutional subscriptions; and (2) certain efficiency-enhancing modifications proposed by Google or commentators which are yet to be implemented as part of the settlement agreement. Part V concludes.

II. BACKGROUND AND OVERVIEW OF THE GBS SETTLEMENT

In 2004, Google initiated the Google Books Library Project with the mission of digitizing millions of books from major research libraries and displaying the text in small “snippets” in response to online search enquiries. The goal of the GBS project was to promote wide access of books among global readers and researches as well as equalization of resources between libraries and academic institutions all around the world. Google also aimed to bring new life to the myriad of out-of-print books (including so-called “orphan works” whose copyright owners cannot be traced), which can only be found in the largest and most ancient libraries in the world. However, Google did not obtain permission from copyright owners before proceeding to scan the books, many of which were still in copyright. Google’s actions triggered a class action brought by authors and publishers for copyright infringement, with the rightsholders seeking injunctive relief and copyright damages. Google’s primary defense was that the display of only small sections of a book constituted “fair use” under

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4. Id.
5. Id.
6. Id. at 670–71.
§ 107 of the Copyright Act. Indeed, the reporting of search results itself was likely fair use since the quotations displayed were too fragmented to amount to substantial reproduction of a book. However, the focus of the rightsholders' argument was on the acts of scanning millions of copyrighted books in full and saving them onto Google's databases. These acts undeniably constituted "copying" under copyright law, and pleading fair use would be difficult for Google. In deciding whether a use is fair or not, courts are required to consider the four factors stipulated under § 107 of the Copyright Act, namely: "(1) the purpose and character of the use . . . ; (2) the nature of the copyrighted work; (3) the amount and substantiality of the portion used . . . ; and (4) the effect of the use upon the potential market for or value of the copyrighted work." The courts have traditionally placed more weight on the first factor (purpose and character of the use) and the fourth factor (market harm) in evaluating claims of fair use. Since Google's use was both commercial and non-transformative (verbatim copies of books being made), the Internet company would bear the burden of proving the absence of market harm. The burden would be difficult to discharge given that the court might consider that the digital library for web search amounted to a viable potential market for the rightsholders' works.

However, the case did not proceed to trial and the parties began settlement negotiations after engaging in document discovery. Google, the Authors Guild, and the Association of American Publishers eventually reached a settlement agreement in October 2008. The proposed settlement attracted hundreds of objections and the parties made modifications to the settlement agreement to address some of these concerns. An amended settlement agreement was filed by Google and the rightsholders in November 2009 pending approval by the court pursuant to Rule 23(e) of the Federal Rules of Civil Procedure. Judge Chin, sitting on the Southern District Court for New York, conducted a fairness hearing in February 2009 after receiving
comments from class members and amicus curiae supporting or objecting the settlement.\textsuperscript{16}

The following paragraph highlights the salient features of the amended settlement agreement, a complex document that spans 166 pages. The class is comprised of people who are United States copyright holders of one or more books as of January 5, 2009.\textsuperscript{17} The settlement, therefore, covers both commercially available works and commercially unavailable works (including orphan works). Google is authorized to continue scanning these books into digital form but must seek the express consent of rightsholders before displaying commercially available books as part of web search results, as books on sale individually (so-called consumer purchases), or as part of a blanket license (so-called institutional subscription).\textsuperscript{18} In other words, Google may display commercially unavailable works for the purposes of search or distribution without prior authorization, though their rightsholders can always opt out of the settlement (before the deadline of September 4, 2009) or later request removal of their books from the Book Rights Registry described below.\textsuperscript{19} But orphan work rightsholders have not opted out or come forward to claim their books, so Google's unqualified right to display and distribute orphan works in the absence of wholesale competition gives rise to the concern that Google will have a de facto monopoly over such works, an issue which will be addressed later in this paper.\textsuperscript{20} Google is also authorized to make "non-display" uses of all digitized books, which will be used to build a "Research Corpus" for similar, "non-consumptive" uses by certain qualified users;\textsuperscript{21} such alternative uses will be explored in detail towards the end of this paper.\textsuperscript{22} The pricing mechanisms of consumer purchases and institutional subscriptions have also raised antitrust concerns—their detailed description and analysis will also be deferred to a later stage of this paper.\textsuperscript{23} It is, however, important to note at this juncture that the settlement agreement plans to establish a Books Rights Registry which will (1) maintain a database of rightsholders in the class;\textsuperscript{24} (2) distribute royalties to rightsholders accord-

\textsuperscript{16} Id.
\textsuperscript{18} Id. §§ 1.31, 3.2, 3.3.
\textsuperscript{19} Id. §§ 1.124, 3.5(a)(i), 10.2(a).
\textsuperscript{20} See infra Part IV(A).
\textsuperscript{21} Amended Settlement Agreement, supra note 17, §§ 1.94, 7.2(d).
\textsuperscript{22} See infra Part IV(C).
\textsuperscript{23} See infra IV(B).
\textsuperscript{24} Amended Settlement Agreement, supra note 17, § 6.1(b).
ing to a default (and negotiable) revenue split of sixty-three percent to rightsholders and thirty-seven percent to Google; and (3) use “commercially reasonable efforts” to locate rightsholders in order to minimize the number of orphan works covered by the settlement. Google will collect royalties and the Registry will hold them for rightsholders of unclaimed works, who have ten years to come forward to collect them before any unclaimed funds go to literary-based charities. The amended settlement agreement will also create an Unclaimed Works Fiduciary (UWF), existing independent of the Registry, to represent the interests of orphan work rightsholders.

On March 22, 2011, Judge Chin issued a ruling rejecting the amended settlement agreement primarily based on the following grounds: (1) inadequate class representation; (2) the settlement agreement seeking to implement a “forward-looking business arrangement” which went beyond the scope of relief under Rule 23; (3) the agreement raising copyright concerns by taking copyright owners’ right to exclude; (4) the agreement raising antitrust concerns; and (5) the agreement raising international law or foreign copyright concerns. Regarding antitrust concerns, which played a large part in the Judge’s decision to reject the settlement and constitute the focus of the present paper, the Judge pointed to the possibility that the settlement agreement “would give Google a de facto monopoly over unclaimed works” and “Google’s ability to deny competitors the ability to search orphan books would further entrench Google’s market power in the online search market” in potential violation of § 2 of the Sherman Act. Strangely enough, the “Antitrust Concern” section was only two pages long, without any discussion of whether Google’s pricing schemes would fall foul of § 1 of the Sherman Act. Further-

25. Id. §§ 1.89, 1.90, 4.5(a)(i)–(ii), 6.1(d) (indicating that Google is required to pay over seventy percent of net revenues from sales and advertising to rightsholders, with a ten percent deduction to reflect Google’s operating costs, so the revenue split comes down to sixty-three percent to rightsholders, and thirty-seven percent to Google).
26. Id. § 6.1(c).
27. Id. § 6.3(a)(i).
28. Id. §§ 3.2(e)(i), 3.3, 3.10, 4.2(c)(i), 4.3, 4.5(b)(ii), 4.7, 6.2(b)(ii).
30. Id. (quoting Statement of Interest of the U.S. Dep’t of Justice at 2, No. 05-8136 (S.D.N.Y. Feb. 4, 2010) (ECF No. 922)).
32. Id. at 680–82.
33. Id.
34. Id. at 684–86.
35. Id. at 682–83 (citing United States v. Griffith, 334 U.S. 100 (1948) (indicating that monopoly leveraging can constitute an antitrust violation under § 2 of the Sherman Act)).
more, the Judge did not consider whether the exclusivity restraint (i.e. Google’s monopoly over orphan works) was reasonably necessary to further underlying efficiencies of the GBS project.37 Indeed, Judge Chin’s denial of the GBS settlement based on this antitrust concern is not much different than condemning the exclusivity arrangement as per se illegal monopolization under antitrust law. As will be argued in the Part that follows, the GBS settlement, similar to the ASCAP and BMI licensing scheme in the music industry, belongs to the general category of copyright collective administration, a form of productive joint venture activity, which should be accorded a rule of reason treatment. The mistake in the Judge’s reasoning lies in applying a per se illegality rule instead of a rule of reason standard in evaluating “ancillary restraints” to the GBS system. The following Part will also examine the proper manner in which the antitrust rule of reason should be applied to resolve antitrust concerns arising from the GBS settlement and copyright collectives of a similar type.

III. Google Book Search, Copyright Collectives, and the Antitrust Rule of Reason

A. The Analogy Between the GBS Settlement and ASCAP/BMI Collective Licensing

As many commentators have noted, the GBS settlement bears interesting similarities with performing rights organizations, the most notable being ASCAP and BMI, in the music licensing industry.38 They all represent different forms of collective copyright administration, so-called copyright collectives, as a solution to the market failure problem of high transaction costs.39 Commercial entities that perform or play music in public, notable examples being shops, restaurants, bars, discos, television and radio stations, are required under copyright law to seek prior consent from copyright owners in respect of each and every performance.40 Since businesses are typically interested in performing multiple and different songs, absent collective licensing arrangements in place, this would entail an unimaginable

37. Id.
number of negotiations and individual licenses to be concluded between users and copyright holders. Collective or blanket licensing through performing rights organizations, such as ASCAP and BMI, came as a groundbreaking market solution. As the Supreme Court observed in *BMI,*

ASCAP and the blanket license developed together out of the practical situation in the marketplace: thousands of users, thousands of copyright owners, and millions of compositions. Most users want unplanned, rapid, and indemnified access to any and all of the repertoire of compositions, and the owners want a reliable method of collecting for the use of their copyrights. Individual sales transactions in this industry are quite expensive, as would be individual monitoring and enforcement[...]. The costs are prohibitive for licenses with individual radio stations, nightclubs, and restaurants, and it was in that milieu that the blanket license arose. A middleman with a blanket license was an obvious necessity if the thousands of individual negotiations, a virtual impossibility, were to be avoided.

Similarly in the context of books, it would be prohibitively costly for institutional subscribers to individually negotiate with numerous book rightsholders for blanket licenses, and for individual consumers to get hold of a printed or digital copy of a commercially unavailable book; not to mention the formidable task of tracking down orphan work rightsholders. The settlement therefore operates as a collective licensing scheme established by Google and the rightsholders. It has huge transaction-cost saving benefits in that Google acts on behalf of all rightsholders (just as ASCAP and BMI did in respect of music performing rights) in licensing digital books rights to multifarious users on either a blanket or a per-book basis. On the other hand, the GBS settlement leads to the creation of a new product, the institutional subscription service that aggregates a near-universal collection of books; this resembles the blanket licenses covering a wide range of musical works offered by ASCAP and BMI. In fact, lowering transaction costs and creating a new product constituted the procompetitive justifications which persuaded the Supreme Court to hold that the ASCAP and BMI arrangement was not per se illegal under antitrust law and should instead be tested under the “rule of reason.”

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43. See id. at 28–29. However, ASCAP and BMI each have their own exclusive songs since both of their agreements prohibit a rightsholder from licensing the same song through a rival blanket licensing intermediary.
this test, the anticompetitive and procompetitive effects of the arrangement shall be carefully assessed and weighed against each other before concluding whether the agreement runs afoul of antitrust law.\textsuperscript{45} More specifically, the offering of a blanket music license at a lump-sum price, similar to Google’s default price and royalty terms and de facto exclusivity over orphan works, should be viewed as ancillary restraints to a procompetitive joint venture—the copyright collective at issue. As will be further elaborated below, an antitrust rule of reason analysis would begin by asking whether such restraints have likely and significant anticompetitive effects and, if answered affirmatively, proceed to consider whether the restraints are necessary in promoting one of the procompetitive objectives of the collective arrangement in question.

It is worth noting that the Second Circuit in BMI found, upon remand and application of the rule of reason standard, that the ASCAP and BMI arrangement lacked anticompetitive effects because of non-exclusivity: (1) individual song users remained free to seek direct licenses from the rightsholders; and (2) the fact that users might prefer the blanket license over individual negotiation was irrelevant.\textsuperscript{46} Similarly, the GBS settlement does not bar purchases of books directly from rightsholders or other intermediaries such as Amazon, eBay, or physical bookstores, since every right Google has to digitize, display, or sell books under the settlement agreement is expressly non-exclusive.\textsuperscript{47} It can be argued, though, that Google has de facto exclusivity over the offering of orphan works (in any event—as will be examined below—this concern should be evaluated under the rule of reason instead of relied on as a per se ground for rejecting the settlement).\textsuperscript{48} In fact, as Professor Elhauge observed, there are several differences between the GBS settlement and the ASCAP and BMI arrangement which render the former less restrictive and hence less likely to constitute a rule of reason violation.\textsuperscript{49} First, ASCAP and BMI only offered blanket licenses but not individual songs; whereas Google is offering books both as part of its institutional subscription and on a standalone


\textsuperscript{47} Amended Settlement Agreement, supra note 17, §§ 2.4, 3.1(a).

\textsuperscript{48} See infra Part IV(A).

\textsuperscript{49} Elhauge, supra note 38, at 7.
basis, and hence provides consumers a choice that the plaintiff sought as a remedy in BMI.\textsuperscript{50} Secondly, while only ASCAP and BMI had the right to price the blanket license, the GBS settlement permits rightsholders to set their own prices for books sold through Google (or ask Google to set prices based on the Pricing Algorithm).\textsuperscript{51} Thirdly, although music rightsholders have the right to license directly to end users, they are prohibited under their ASCAP or BMI agreement from licensing the same song through a rival intermediary; in contrast, the GBS settlement allows book rightsholders not only to license directly, but also simultaneously distribute their books through Google and/or another intermediary.\textsuperscript{52} Fourthly, the procompetitiveness of the GBS settlement lies not only in grouping copyrights in one intermediary (as was the case of ASCAP and BMI), but also clarifying rights and digitizing books to make it easier for users to identify the materials they need.\textsuperscript{53} Finally, the requirements of competitive returns and broad access in the pricing of institutional subscription and consumer purchases provide a more reliable and objective benchmark than the reasonable-fee test for the ASCAP and BMI consent decrees in ensuring that prices remain competitive.\textsuperscript{54} We shall later examine the restraints relating to pricing and orphan work exclusivity more closely to determine their legality under an antitrust rule of reason.\textsuperscript{55}

There is also one subtle difference between the GBS arrangement—which arises from a class action settlement requiring ex ante court approval\textsuperscript{56}—and the blanket license agreement in BMI which (despite already subject to antitrust consent decrees) was challenged ex post as a violation of § 1 of the Sherman Act.\textsuperscript{57} When deciding whether to condemn a horizontal agreement or joint venture under the rule of reason, an antitrust court will weigh its anticompetitive effects against its procompetitive effects in deciding whether the arrangement is overall efficiency-enhancing or -reducing, and will possibly look into whether there is a less restrictive alternative that is capable of achieving the same procompetitive objectives.\textsuperscript{58} In contrast, when a court decides whether or not to approve a class action settlement under Rule 23(e), it is only bound by an open-ended stan-

\textsuperscript{50} Id. at 7, 60.
\textsuperscript{51} Id. at 7, 61–62.
\textsuperscript{52} Id. at 7, 62–63.
\textsuperscript{53} Id. at 59–60.
\textsuperscript{54} Elhauge, supra note 38, at 62.
\textsuperscript{55} See infra Parts IV(A)–(B).
\textsuperscript{57} Broad. Music, Inc. v. CBS, Inc., 441 U.S. 1, 6 (1979).
\textsuperscript{58} See infra Part III(B).
standard of ensuring that the settlement is "fair, adequate, and reasonable, and not a product of collusion."°

Over time, the courts have developed more concrete sets of considerations (for example, the Grinnell factors) in determining whether a settlement agreement is "fair, adequate, and reasonable," but which factors are more important in any particular case still turns on the facts and circumstances of each case and the experience of judges. In any event, courts will almost inevitably look at whether the settlement raises illegality concerns in different areas of law—as Judge Chin did in the GBS Judgment under the headings of "Copyright Concerns," "Antitrust Concerns," "Privacy Concerns," and "International Law Concerns." As mentioned above, he raised the antitrust concern that the settlement agreement would give Google de facto exclusivity over orphan works and thereby extend its monopoly in the online search market (though antitrust issues arising from Google's pricing schemes were not discussed anywhere in the judgment). What the Judge should have done regarding the exclusivity restraint (as with the pricing restraint that he should have discussed) is to subject it to a rule of reason analysis and evaluate whether its likely anticompetitive effects outweighed its procompetitive justifications. Indeed, the difference between ex ante approval of a class action settlement and ex post antitrust intervention of horizontal agreement may not be as significant as it first seems. First, although obvious and actual anticompetitive effects may serve as a substitute for formal market analysis, evidence of increasing prices and declining output alone is often inconclusive of cartel or monopolization effects. This is why market definition and analysis is frequently used as a surrogate for determining whether an agreement or conduct has likely and significant anticompetitive effects. Secondly, antitrust agencies (e.g. the Department of Justice (DOJ) and the Federal Trade Commission (FTC)) have actually developed voluntary procedures for ex ante assessment of non-merger activity, as the agencies used business review letters extensively in the context of patent pools and standard-setting organizations, an area closely related to copyright

60. See Google, Inc., 770 F. Supp. 2d at 674 (indicating the nine factors).
61. Id. at 674.
62. Id. at 680.
63. Id. at 673.
64. Id. at 673–74.
66. Id. at 682–83.
68. PHILIP E. AREEDA & HERBERT HOVENKAMP, ANTITRUST LAW: AN ANALYSIS OF ANTITRUST PRINCIPLES AND THEIR APPLICATION § 1503(a) (3d ed. 2006).
collectives. Such letters state an agency’s intention not to challenge business practices contemplated by the organization as of the date of the letter, though the agency may refuse to be bound by its letter. In sum, irrespective of whether a copyright-related horizontal arrangement or settlement agreement is tested under the antitrust rule of reason, a court should carefully assess market circumstances to ascertain its likely anticompetitive effects and weigh them against the claimed efficiencies of the agreement.

B. The Proper Antitrust Baseline and Rule of Reason Standard

A natural question arises: precisely how should a court apply the antitrust rule of reason? Specifically, how should it “weigh” anticompetitive effects of a horizontal agreement against procompetitive justifications when any quantitative cost-benefit analysis would be practically unachievable? The answer to this question turns on the proper antitrust baseline for qualitatively assessing the anticompetitive and procompetitive effects of an agreement. This has in fact been the subject of rigorous debate between Professors Einer Elhauge and Randal Picker in their articles concerning the GBS settlement. Professor Elhauge prefers to look at whether or not an agreement is overall output-increasing or efficiency-enhancing; if the answer is positive, it should be regarded as procompetitive and the antitrust inquiry is over. He therefore argues that “[a]ny claimed anticompetitive effects must be measured from the but-for baseline of what would happen without the settlement,” which means “there would . . . be no market in unclaimed or commercially unavailable books, and thus no firm offering them or a near-universal library.” In Elhauge’s view, society would be better off even with Google charging monopoly prices for commercially unavailable books and its institutional subscriptions and no rival being able to overcome entry barriers to offer digital books in a similar manner, as having a monopolistically-priced new product is always better than no product at all. In sum, a rule of reason analysis under antitrust law should determine “whether the settlement improves consumer welfare from the but-for world, not

72. Elhauge, supra note 38, at 2.
73. Id. at 17.
74. Id. at 20.
75. Id. at 17, 19.
whether it maximizes consumer welfare to the fullest extent conceivable."\textsuperscript{76}

In contrast, Professor Picker argues that it is wrong to solely focus on output expansion resulting from the creation of a new product.\textsuperscript{77} In deciding whether to use antitrust to block price-fixing of a new product, "[t]he relevant comparison isn't the before- and after- worlds as to the cartel but rather the worlds with and without the antitrust remedy."\textsuperscript{78} In particular, antitrust intervention is appropriate if it is expected to direct the innovation towards a competitively priced new product as opposed to outright abandonment of the innovative pro-

ject.\textsuperscript{79} As he further observes:

If price-fixing in the new market was the only way to bring it into being, antitrust authorities should accept the price-fixing as the necessary price of creating the innovation in the first place. But this requires actual judgments: Fully-competitive [new products] would be a better outcome if we can get there and sidestep killing off the innovation.\textsuperscript{80}

In other words, only if price-fixing or other ancillary restraints are marginal for the sustainability of the new product venture will society be better off by permitting the horizontal agreement under a rule of reason analysis. Therefore, the key issue in the GBS case would be whether there are separable anticompetitive features of the overall procompetitive settlement that should be removed pursuant to the antitrust laws.

Interestingly, the two distinct antitrust baselines advocated by Elhauge and Picker are reflected in the evolving antitrust jurispru-
dence on the proper approach of applying the rule of reason analysis. Professor Elhauge's approach, which focuses on the overall competitive effects of an agreement, is representative of the traditional rule of reason standard that the courts have applied for most of the previous century. In \textit{Chicago Board of Trade},\textsuperscript{81} one of earliest Supreme Court decisions applying the rule of reason, Justice Brandeis observed that "[t]he true test of legality is whether the restraint imposed . . . promotes competition or whether it is such as may suppress or even destroy competition."\textsuperscript{82} The Court's emphasis on net efficiency effects

\begin{itemize}
\item \textsuperscript{76} Id. at 20.
\item \textsuperscript{77} Picker, supra note 71, at 3.
\item \textsuperscript{78} Id. at 4.
\item \textsuperscript{79} Id.
\item \textsuperscript{80} Id.
\item \textsuperscript{81} Chi. Bd. of Trade v. United States, 246 U.S. 231 (1918).
\item \textsuperscript{82} Id. at 238.
\end{itemize}
has largely continued through to the \textit{BMI} case in the late 1970s, where
the Second Circuit, on remand, held,

A rule of reason analysis requires a determination of whether an
agreement is on balance an unreasonable restraint of trade, that is,
whether its anti-competitive effects outweigh its pro-competitive ef-
facts . . . . In this case, however, . . . the balancing of pro- and anti-
com-mptive effects need not be undertaken because Judge Lasker's
findings of fact demonstrate that the blanket license has no an-
ticompetitive effect at all.\textsuperscript{83}

More precisely, the blanket license lacks anticompetitiveness because
of its non-exclusive nature, rendering it unnecessary for the court to
proceed to the balancing stage where the procompetitive justifications
of transaction-cost savings and new product creation become relevant.

Over time, however, the courts have developed a more nuanced ap-
proach of applying the rule of reason analysis, which reflects Professor
Picker's rationale of unbundling anticompetitive effects from an over-
all procompetitive transaction.\textsuperscript{84} This so-called "less restrictive alter-
native" (LRA) inquiry asks whether a particular restraint is
reasonably necessary in promoting a procompetitive objective of the
agreement, or more specifically, whether there exists an LRA which is
just as or even more effective in achieving the claimed efficiencies.\textsuperscript{85}
In \textit{NCAA v. Board of Regents},\textsuperscript{86} a Supreme Court decision which
shortly followed \textit{BMI}, the Court applied the LRA analysis and con-
cluded that the NCAA's procompetitive justifications were merely
pretext and the real purpose of the NCAA's plan for televising college
football games was to restrict output and raise prices.\textsuperscript{87} Although the
Court agreed that the television plan had procompetitive objectives of
maintaining competitive balance between the teams and preserving
the amateur nature of college football as a unique product,\textsuperscript{88} it pro-
ceded to identify alternative rules and restraints which were just as
effective in achieving the claimed benefits.\textsuperscript{89} The maintenance of
competitive balance, restrictions on recruiting, number of coaches and
players per team, alumni donations, and other revenue resources were

\textsuperscript{83} CBS, Inc. v. Am. Soc'y of Composers, Authors and Publishers, 620 F.2d 930, 934 (2d Cir.
1980).
\textsuperscript{84} Picker, \textit{supra} note 71.
\textsuperscript{85} See, e.g., \textit{Areeda} \& \textit{Hovenkamp}, \textit{supra} note 68, §§ 1505, 1913; Gabriel A. Feldman, \textit{The
561, 577-86 (2009).
\textsuperscript{87} \textit{Id.} at 120.
\textsuperscript{88} \textit{Id.} at 102.
\textsuperscript{89} \textit{Id.} at 119.
considered as equally effective restraints. With regard to preserving the nature of college football, the NCAA could have employed the LRAs of limiting payment to players and prescribing eligibility requirements. The Court therefore found NCAA's television plan to be an illegal agreement under a § 1 rule of reason analysis. Later in Clorox Co. v. Sterling Winthrop, Inc., a case concerning the antitrust legality of Lysol trademark agreements, the Second Circuit formalized the LRA approach in the form of a three-part-analytical framework:

First, the “plaintiff bears the initial burden of showing that the challenged action has had an actual adverse effect on competition as a whole in the relevant market. . . .” Then, “if the plaintiff succeeds, the burden shifts to the defendant to establish the ‘pro-competitive “redeeming virtues”’ of the action. Should the defendant carry this burden, the plaintiff must then show the same pro-competitive effect could be achieved through an alternative means that is less restrictive of competition.”

The general framework set out in the “Antitrust Guidelines for the Licensing of Intellectual Property” (jointly issued by the DOJ and FTC) adopts largely the same approach but provides additional insights on how the LRA analysis should be conducted. Regarding the analysis of anticompetitive effects (i.e. the first part of the Clorox test), the Guidelines emphasized the importance of distinguishing between horizontal and vertical restraints in an intellectual property (IP) licensing agreement. For horizontal agreements, the anticompetitive concern lies in the facilitation of coordinated pricing, monopolization, or restriction of technological development. The concern for vertical restraints is that they may foreclose access to important inputs or facilitate horizontal coordination at the market level of either the licensor or licensee. Whether anticompetitive effects are significant and likely will depend on various factors, including degree of concentration, difficulty of entry, supply and demand elasticity, and duration of the restraint. Only if a restraint is likely to have anticompetitive effects will the antitrust agencies proceed to “consider whether the

90. Id.
91. Bd. of Regents, 468 U.S. at 119.
92. Id. at 117–20.
94. Id. at 56 (quoting Capital Imaging Assocs., P.C. v. Mohawk Valley Med. Assocs., 996 F.2d 537, 543 (2d Cir. 1993) (quoting Bhan v. NME Hosps., Inc., 929 F.2d 1404, 1413 (9th Cir. 1991))).
95. IP LICENSING GUIDELINES, supra note 45.
96. Id. § 4.1.1.
97. Id.
98. Id.
99. Id.
restraint is reasonably necessary to achieve procompetitive efficiencies," at which point it is relevant to consider "the existence of practical and significantly less restrictive alternatives[.]" Even if a restraint is reasonably necessary in that there is no identifiable LRA, the agencies are still required to "balance the procompetitive efficiencies and the anticompetitive effects to determine the probable net effect on competition in each relevant market." There is still some legal uncertainty as to whether "less restrictive" entails that the alternative achieves a greater level, the same level, or nearly the same level of procompetitive efficiencies with a lesser anticompetitive impact. What is certain, however, is that courts and agencies are not requiring antitrust defendants to adopt the least restrictive alternative that may substantially interfere with procompetitive objectives without adding much to competition at the margin. Nor are courts expected to engage in a marginal analysis weighing the incremental efficiencies of the restraint (vis-à-vis the next best alternative) against incremental social costs in terms of higher prices and lower output. A marginal cost-benefit analysis may well be the theoretically ideal way of resolving conflicts at the antitrust and IP intersection, but as Professor Kaplow noted, courts simply lack sufficient information to calculate an incremental welfare to loss ratio for every licensing restraint, let alone compare such a ratio to the welfare to loss ratio for the last year of optimal IP duration (which is itself impossible to determine). Kaplow advocated in his seminal antitrust and patent article a qualitative application of the marginal analysis by having antitrust courts consider three factors in determining whether to condemn or approve a patentee practice: (1) the extent to which the patentee reward is pure transfer; (2) the portion of the reward accruing to the patentee; and (3) the degree to which the reward serves as an incentive. However, it is doubtful whether these factors are appli-

100. IP LICENSING GUIDELINES, supra note 45, § 4.2.
101. Id.
102. See Feldman, supra note 85, at 604-05.
103. AREEDA & HOVENKAMP, supra note 68, § 1505(a).
105. Id. at 1835 (stating for example, discriminatory royalties resulting in a transfer of welfare from licensees to licensors without much deadweight loss, thus having a high ratio).
106. Id. at 1835-37 (stating for example, where a licensing agreement is a disguised cartel or is granted by an assignee of a patent, most of the reward is accrued to someone other than the original patentee who has little incentive to innovate, resulting in a low ratio).
107. Id. at 1837-39 (indicating that unless an ex post reward can be reasonably estimated ex ante because, for instance, the patentee is an experienced inventor and appreciates the value of restrictive licensing practices, the reward is unlikely to have substantial effect on inventive activity).
cable beyond the context of IP licensing. It is also difficult to gener-
alyze factors to be considered in a marginal analysis of other antitrust
and IP issues such as copyright collectives and IP-related settlement
agreements. Such an undertaking would require a large sample of en-
forcement practices and court decisions from antitrust authorities.108

Returning to the fundamental question posed at the beginning of
this Part: which type of the rule of reason analysis should be pre-
ferred—the Elhauge overall-efficiency approach or the Picker LRA
analysis? It is worth noting that the LRA analysis is a “maximizing”
test, which selects “the most efficient method for accomplishing the
procompetitive benefits of a restraint.”109 While the overall-efficiency
approach is a “satisficing” test, which only ensures that an agreement
is satisfactorily or sufficiently efficiency-enhancing, in that “the mar-
et is better off with the restraint than without it.”110 All things being
equal, it is obvious that a maximizing inquiry is preferred to a satisfic-
ing one; there is therefore no reason to favor the overall-efficiency
approach over the LRA analysis unless the latter is somehow practi-
cally unachievable.

Indeed, critics of the LRA analysis have noted its potential adverse
effects of increasing decision-error costs and chilling procompetitive
behavior.111 However, these negative effects can be effectively miti-
gated such that applying a properly structured LRA analysis will be
more social-welfare-enhancing than a crude overall-efficiency ap-
proach. If the concern about false negatives is due to judges’ lack of
expertise in understanding industrial market structures and behav-
ior,112 the courts can seek guidance from a judicially-appointed eco-
nomic expert and the antitrust agency (the DOJ or the FTC) which
specializes in enforcement in the industry concerned. Besides, the an-
titrust courts are not expected to engage in an open-ended “search for
a theoretically least restrictive alternative”;113 instead, courts are
asked to realistically consider the merits of LRA claims by an antitrust
plaintiff (who bears the burden of proving an LRA) against “the prac-
tical prospective business situation faced by the parties.”114

108. See Kelvin Kwok, A New Approach to Resolving Refusal to License Intellectual Property
Rights Disputes, 34 World Competition L. & Econ. Rev. 261 (2011) (indicating an attempt to
generalize factors to consider in the qualitative balancing of allocative efficiency losses and qual-
itive efficiency gains due to a monopolist refusing to license intellectual property rights).
110. Id. at 590.
111. See, e.g., id. at 599–610.
113. IP Licensing Guidelines, supra note 45, § 4.2.
114. Id. § 4.2.
A more legitimate concern is that the LRA analysis may result in over-deterrence of procompetitive conduct due to ex ante uncertainty and opaqueness of the legal standard. This can be partially mitigated by conducting the LRA inquiry from an ex ante rather than ex post basis. In the GBS context, this entails asking whether Google would still be willing to move forward with the GBS project if particular restraints (e.g. orphan work exclusivity, pricing and royalty terms) were removed or substituted with an LRA at the point in time when no investment has yet been made, rather than the time of the court’s decision-making when Google has already incurred huge sunk costs in the project and will still find it profitable to continue with it even with the court’s antitrust intervention. The purpose of adopting an ex ante perspective is to ensure that Google, or similarly situated competitors, will not in the long run abandon innovative but risky research and development activities which overall enhance social welfare on the account of the courts’ previous LRA interventions. On the other hand, although irrelevant to approval of class action settlements as in the present case, chilling of beneficial conduct may be attributable to the prospect of treble damages in antitrust court cases, which automatically follows from an antitrust plaintiff successfully establishing an LRA.

A possible solution to this problem is to introduce a legislative exception for mandatory trebling specifically for copyright collectives (or more generally for co-operative joint ventures involved in the development and commercialization of IP rights). Congress has taken this approach to protect the interests of standard-setting organizations: it passed in 2004 the Standard Development Organization Advancement Act which created antitrust exceptions to qualifying standards groups, including a limitation to single damages liability, guaranteed rule of reason treatment, and a safe harbor for organizations with members holding less than twenty percent collective market share. Nevertheless, it may be felt that any amount of damages resulting from a LRA inquiry would create sufficient ex ante uncertainty and risk to deter net procompetitive conduct; but if damages were to be completely eliminated, it would be doubtful whether private parties will still have an incentive to bring antitrust suits at all. An alternative solution to this damages dilemma is therefore to eliminate private suits altogether and to permit only government agencies (i.e. DOJ or FTC) to initiate equity proceedings seeking to implement

115. Feldman, supra note 85, at 609-10.
the LRA as part of a court or agency order without any criminal sanctions or civil penalties attached.\textsuperscript{118}

Since varying the antitrust remedy and taking an ex ante perspective should be effective measures against the threat of deterring procompetitive behavior, there seems to be reason to favor the maximizing LRA inquiry over the satisficing overall efficiency test as the normative antitrust standard for evaluating copyright collectives under the antitrust rule of reason. The following Part will present a general, step-by-step framework that courts should follow in evaluating antitrust concerns of copyright collectives under the LRA rule of reason analysis. It is applicable in both a court case in which the legality of ancillary restraints is challenged ex post under the relevant antitrust statutes and also the unique situation of the GBS dispute where a court comes to decide ex ante whether to approve a class action settlement agreement having antitrust implications.

C. Application of the Rule of Reason to the GBS Settlement and Copyright Collectives: An Analytical Framework

An antitrust analysis should begin by asking whether the restraint at issue is ancillary to the copyright collective, in that it is "expected to contribute to an efficiency-enhancing integration of economic activity."\textsuperscript{119} The collective licensing arrangement can lead to efficiencies in both the productive sense (e.g., savings in transaction costs) and the qualitative dimension (e.g., creation of a new product, often blanket licensing arrangements). Ancillary restraints should be accorded a rule of reason treatment, meaning courts should not immediately condemn the restraint under the antitrust statutes or reject a class action settlement upon finding an anticompetitive restraint. In other words, courts should reserve per se illegality only for plainly anticompetitive restraints such as naked price-fixing, output restriction, or market division among parties (in either a horizontal or vertical relationship) who are not collaborating in any procompetitive joint venture activity.\textsuperscript{120} This was definitely not the case for music licensing by BMI and ASCAP\textsuperscript{121} or digital books distribution by Google in the GBS settle-

\textsuperscript{118} See Kelvin H. Kwok, A Proposal to Resolving Conflicts at the Intersection of Antitrust Law and Securities Regulation (unpublished working paper) (on file with author) (indicating a similar suggestion in the context of antitrust and securities conflicts).

\textsuperscript{119} IP LICENSING GUIDELINES, supra note 45, § 3.4.

\textsuperscript{120} Id. § 3.4.

so the restraints in both instances should be tested under the rule of reason.

A rule of reason treatment of ancillary restraints should commence with an antitrust plaintiff (or amicus curiae opposing a class action settlement) demonstrating that a restraint has likely and significant anticompetitive effects. It is important to present an anticompetitive theory in order to identify evidence necessary for courts to judge probabilities and magnitudes. This feeds into the examination of market circumstances surrounding the copyright collective in question, which forms the fulcrum of the anticompetitive inquiry. Although the precise market conditions to focus on vary from one type of restraint to another, it is possible to generalize several factors that are generally applicable in most cases. For example, how much market power does the restraint confer? How concentrated in the relevant market? Is entry difficult? How about the behavior and shares of existing rivals? How elastic is supply and demand in the relevant markets? Does the restraint tend to restrict or expand output? Is there direct evidence of anticompetitive effects in terms of higher prices or lower output?

If anticompetitive effects are established, the burden is shifted to the antitrust defendant (or the settlement parties—Google and the book rightsholders in the GBS case) to demonstrate that the restraint is reasonably necessary for a procompetitive objective, which is part and parcel of the copyright collective. The defendant or settlement parties will establish a prima facie case of necessity by pointing out the procompetitive purpose of the challenged restraint and showing economically how this could lead to redeeming efficiencies. This is the point at which the LRA analysis enters the picture. It falls to the antitrust plaintiff (or opposing party to a settlement) to show that there is a practical LRA that could have achieved (or can likely achieve) the same level (or nearly the same degree) of claimed efficiencies with less competitive harm. The court should carefully consider the LRA against the "practical prospective business situation faced by the parties" and obtain guidance from a judicially appointed economic expert or amicus curiae who has informed knowledge of actual market conditions. To preserve innovation incentives and hence long-term qualitative efficiency, the courts should conduct the LRA inquiry from an ex ante perspective, asking whether the joint venture parties (here,

123. Areeda & Hovenkamp, supra note 68, § 1503(a).
124. Id. § 1503(b).
125. IP Licensing Guidelines, supra note 45, § 4.2.
Google and the rightsholders) would still have commenced the innovative project, assuming the absence of any form of sunk investment, had the restraint been substituted with the plausible LRA. If a practical ex ante LRA can be identified, the court should issue an injunction or consent decree implementing that LRA in the case of an antitrust action, or rejecting the proposed class settlement but recommending that the parties amend their agreement to reflect the LRA for a likely future approval. As is suggested above, Congress should introduce a legislative exception to waive mandatory trebling of antitrust damages in the context of copyright collectives, or to go further by allowing only the government (not private parties) to bring an equity suit to enjoin the restraint in question and have it substituted with a practical LRA.

If substituting anticompetitive restraints with LRAs which are equally effective in attaining certain procompetitive objectives works in favor of economic efficiency, in a similar logic, adding procompetitive features to the collective licensing arrangement should make the copyright joint venture even more procompetitive and hence be encouraged. A “procompetitive” feature is one that is overall efficiency-enhancing: it results in productive or qualitative efficiency (for instance, further transaction cost savings or additional product offerings), which is likely to outweigh any potential negative impact on allocative efficiency. It is true that courts do not have the authority to mandate parties to implement add-on features to make their transaction more procompetitive (and it would be going too far to enact legislation conferring on courts such a power), but there is nothing to prevent courts from affirmatively recommending certain pro-competitive modifications that the parties should consider in its judgment (whether resulting from antitrust litigation or class action settlement approval). It may be unrealistic to expect the courts to expend much energy “brainstorming” and designing possible procompetitive modifications for the parties’ (and society’s) benefit; but the parties themselves surely have the incentive to undertake this form of “reversed” rule of reason analysis to figure out whether certain procompetitive features can be added to the copyright collective (which enhances producer surplus), and whether courts are likely to uphold these modifications should they later be challenged in an antitrust action (which depends on whether the modifications are social-welfare-enhancing as well). Besides, a business letter review program can be set up to enable copyright collective members to benefit from ex ante screening of proposed modifications by antitrust agencies before their actual implementation.
The remainder of this paper is devoted to an in depth rule of reason analysis of two central anticompetitive concerns in the GBS settlement. First is Google's de facto exclusivity over orphan works and its pricing mechanisms for consumer purchases and institutional subscription, which largely follows the framework proposed above. Second, it also demonstrates how the "reverse" rule of reason can be applied to analyze the desirability or procompetitiveness of certain modifications proposed by Google or commentators which are yet to be implemented as part of the GBS settlement.

IV. A RULE OF REASON ANALYSIS OF THE GBS SETTLEMENT

A. De Facto Exclusivity over Orphan Works

First, it important to note that Google does not have legal exclusivity over any kind of work—commercially available, commercially unavailable, or orphan works. Commercially available books are by default excluded from the GBS system under the amended settlement agreement. As for commercially unavailable books under active ownership, their rightsholders can always opt out of class action or come forward at a later time to request that their books be excluded. Book rightsholders are free to license their book rights to any company—not only Google but also its competitors. Why, then, is the settlement so controversial? A common concern among commentators is that Google will have de facto exclusivity over orphan works under the settlement. Although there is an apparent right to opt out of the class action or to claim one's book at a later stage, orphan work rightsholders, by definition, have not opted or come forward and their whereabouts simply cannot be traced. So although Google seems to have nonexclusive rights to display and sell orphan works, these rights may, in reality, turn out to be exclusive in nature.

But what about Google's competitors, can they not enter the market to compete with Google in offering book searches and distribution? There are two methods of competitive entry in theory. First, a new entrant can contact the rightsholders individually (or use the Authors Guild of America and the Association of American Publishers as contact points) and reach an agreement in respect of each book.

126. Amended Settlement Agreement, supra note 17, § 3.2.
127. Id.
This method entails high transaction costs (e.g. ascertaining the books in copyright, identifying their rightsholders, and negotiating license agreements with them); and it is impossible to obtain licenses for orphan works. Secondly, a new entrant can imitate the actions of Google: scan millions of books without permission, wait for a class action by the rightsholders, and either litigate the case (and argue fair use) or attempt to strike a settlement deal with the rightsholders. This method has the downside of high litigation costs and risk-bearing costs (note that statutory damages for willful copyright infringement can reach $150,000 per book,\textsuperscript{129} not to mention the severe criminal penalties).\textsuperscript{130} As Google's competitors may lack the ability, money, or willingness to undertake either of the two routes, Google may well end up being the sole proprietor of orphan works.

Nevertheless, one should notice that when Google decided to enter the digital book market a few years ago, it faced many of the same options. Both avenues were equally costly, if not more, for Google. The Internet company decided not to go down the route of obtaining permission, which probably would have taken a preclusive amount of time before every book was digitized. Instead, it elected to digitize books on a vast scale, risking catastrophic damages should rightsholders bring a successful action for copyright infringement. This risk, in this respect, emanated from the legal uncertainty surrounding the applicability of copyright law's fair use defense. It was in no way certain then, as it is now, that rightsholders would agree to a settlement and grant Google the permission to distribute books on their behalf (and as a side effect, orphan works as well). Therefore, as some commentators have argued, courts should not punish Google for its entrepreneurship provided that it does not seek to raise rivals' costs, either directly or indirectly through reaching the class settlement agreement.\textsuperscript{131} Specifically, the key question is whether the class settlement has the effect of erecting artificial entry barriers that would bar potential entry, as distinct from the question whether entry is difficult because natural entry barriers have no causal link with settlement itself.\textsuperscript{132}

The settlement parties voluntarily removed one example of an artificial entry barrier, the most-favored-nation (MFN) clause in the origi-

\textsuperscript{129} Copyright Act, 17 U.S.C. § 504(c)(2) (2006).
\textsuperscript{130} Id. § 506.
\textsuperscript{131} See, e.g., Elhauge, supra note 38, at 16.
\textsuperscript{132} Id.
nal settlement agreement. The MFN clause required that if the Registry licensed a significant portion of unclaimed works to a third party intermediary within ten years of the settlement’s effective date, it had to offer Google the same or better terms as the third party is entitled to. MFN clauses have the effect of discouraging entry, and hence future competition, in the market. First, any benefit that a licensor grants to a subsequent licensee will have to accrue to the first actor (here Google) also, which means doubling the cost of granting subsequent licenses. Secondly, the second actor will find it difficult to gain competitive advantage over the first one since they will always be entitled to the same licensing terms. It is important to note, however, that courts generally consider MFN clauses legal under antitrust laws. As the Seventh Circuit observed in Marshfield Clinic, “[MFN] clauses are standard devices by which buyers try to bargain for low prices, by getting the seller to agree to treat them as favorably as any of their other customers . . . [which] is the sort of conduct that antitrust laws seek to encourage.” It is indeed possible that removing the MFN clause will discourage Google from reaching a settlement with the rightsholders (this turned out not to be the case ex post as the MFN clause was eventually removed from the settlement agreement) or even undertaking the GBS project in the first place. Whether such a clause should be retained or removed under a rule-of-reason analysis will turn on the court’s judgment as to whether it is a necessary ancillary restraint to the GBS scheme from an ex ante perspective. In any event, the issue is less important now given that Google has already agreed to eliminate the MFN clause from the settlement agreement.

Let us now revisit the two routes of entry and evaluate whether the GBS settlement has raised the cost of entry for each. Regarding the first option—obtaining licensing and permission to digitize—one might argue that the settlement gives Google an advantage over its competitors in obtaining “permission” to exploit orphan works. Licensing costs are basically zero for Google to exploit any of these unclaimed works pursuant to the settlement agreement, and infinity for a new entrant that does not wish to break the law by offering orphan

134. Id.
135. Picker, supra note 128, at 401.
137. Marshfield Clinic, 65 F.3d at 1415.
works without permission. So in relative terms, Google’s potential rival will be facing higher costs than Google in respect of the licensing of orphan works. However, this is only true in the ex post sense. From an ex ante perspective, comparing the licensing options available to Google before its entry and to its competitors in light of the GBS settlement, Google and its competitors are in fact facing the same impossibility of offering orphan works if they insist on obtaining consent beforehand. Therefore, the settlement agreement does not raise entry costs for Google’s competitors insofar as the licensing and permission route of entry is concerned.

With regard to the second entry mode—copyright litigation and settlement—the relevant question is whether the GBS settlement makes it more difficult for a subsequent intermediary to strike a separate settlement deal with the rightsholders. Some commentators have argued that, despite the removal of the MFN clause, rightsholders still face disincentives to offer licenses (over orphan works and other books) to a new entrant. Specifically, Professor Picker has argued,

If we think that the collection of rights represented in the lawsuit really is unique, then we should not think that the Authors Guild would wish to license them to a second online search provider. The rights represent a monopoly and licensing use to two or more providers will result in competition between those providers and will almost certainly make the returns to the rights provider much lower.138

This observation seems incorrect. While competition on the selling side would push prices down, competition on the buying side would actually push prices up. In the context of the GBS settlement, it would mean that the sixty-three percent to thirty-seven percent royalty split would possibly be adjusted to a higher ratio in light of competition between Google and the new entrant for a rightsholder’s license. The Supreme Court correctly observed in Leegin that “[t]he difference between the price a manufacturer charges retailers and the price retailers charge consumers represents part of the manufacturer’s cost of distribution, which . . . the manufacturer usually desires to minimize.”139 One way to reduce the distribution makeup is precisely to introduce more retailers at the wholesale level. In the present case, it would mean having the rightsholders license their rights to another book intermediary, which is rational and to their benefit. It is true that Google and this new intermediary may compete with each other (as sellers) by offering discounts off the “List Price” set by each right-

138. Picker, supra note 128, at 403.
sholder (note: this list price actually represents a maximum retail price: see the analysis in the next Part); but since both intermediaries are offering these discounts at their own costs (i.e. the sixty-three percent to thirty-seven percent royalty split is applied to the List Price by default, not the final retail price), such retail price competition does not harm the rightsholders at all. If anything, it actually benefits individual rightsholders because a lower retail price translates into higher sales volume and in turn higher revenue for rightsholders (which is volume times sixty-seven percent of the list price, unaffected by the offering of discounts by intermediaries). The above analysis suggests that an argument based on the unwillingness of rightsholders to license another intermediary is untenable. One exception is perhaps a situation where rightsholders are colluding to exercise market power through Google to set monopoly retail prices for their books and splitting monopoly profits among themselves. But the next Part will demonstrate that the Pricing Algorithm adopted in the amended settlement agreement does not allow Google to set monopoly prices on behalf of rightsholders collectively to facilitate a book cartel; nor do industry conditions in a differentiated book market suggest that any form of collusion between rightsholders would be sustainable.

Despite the dismissal of the disincentives to license argument, there remains concern that, if a new entrant comes along and triggers another class settlement agreement, it will face stronger opposition (vis-à-vis the first settlement) on the grounds of collusiveness or abuse of the judicial process which will result in its failure to satisfy the test of “fair, adequate, and reasonable, and not a product of collusion” for the purposes of judicial approval under Rule 23(e). As Professor Grimmelmann observed:

The Authors Guild lawsuit was genuinely adversarial when filed, the parties did significant pretrial work, and litigation remains a real possibility if the settlement falls through. But since a structured ... settlement [initiated by another entrant] would be the goal ab initio, it would be difficult to negotiate one without calling into question the adequacy of the class representation or the existence of an Article III case or controversy. Unless [the second] settlement differed from Google's in some material points, it might be hard to say it was actually negotiated at arms' length.

Nor is it practicable for the new intermediary to rely on trial and the fair use defense as a fallback in the event that settlement fails. Since

140. Amended Settlement Agreement, supra note 17, § 4.5(b)(i).
there is a clear intention on the entrant’s part to deliberately infringe copyright in the hope of an eventual settlement, the courts will likely impute a “bad element” into the entrant’s infringement, which weighs against a finding of fair use and enhances the likelihood of finding willful infringement, and consequently enhanced statutory damages.

It is therefore likely that a new entrant cannot simply follow Google’s footsteps, without at least incurring higher costs, by triggering a class action and hoping for a class action settlement. The fact that rivals face higher entry costs provides justification for altering the Settlement Agreement to facilitate entry and prevent Google from acquiring a de facto monopoly over orphan works. One way to achieve this is to confer power on either the Registry or the UWF to grant a collective license over orphan works to any intermediary that wishes to enter the book digitization market. At present, neither the Registry nor the UWF has this power. There has been some confusion among commentators as to the effect of § 6.2(b)(i) of the Settlement Agreement, which authorizes “the Registry, . . . to the extent permitted by law, [to] license Rightsholders’ U.S. copyrights to third parties (in the case of unclaimed Books and Inserts, the [UWF] may license to third parties . . . to the extent permitted by law).” This clause is best understood as a description of what the Registry or UWF is permitted to do under the current law; it is not a power-conferring provision which authorizes the Registry or UWF to transfer a copyright license on behalf of a rightsholder.

Having the Registry or the UWF act as a clearinghouse for all willing entrants can be seen as an LRA to the present settlement under which Google will likely have de facto exclusivity over orphan works. It is “less restrictive” because such a scheme would greatly reduce rivals’ costs and facilitate their entry into the book digitization market to compete with Google in offering orphan works and other books. It would also reduce deadweight loss because enhanced competition at the retail level (between Google and the new entrant) will bring down retail prices and induce greater demand for books. But is such an improvement to allocative efficiency purchased at a cost to productive efficiency or qualitative efficiency in the long run? One could imagine

145. Amended Settlement Agreement, supra note 17, § 6.2(b)(i).
146. Grimmelmann, supra note 142, at 3; Picker, supra note 128, at 402; cf. Elhauge, supra note 38, at 12–13.
a productive efficiency argument being made based on the natural monopoly characteristics of the digital book market. The natural monopoly describes a market characterized by substantial economies of scale or scope such that it operates most cost-efficiently with a single firm serving the whole market (and under price regulation if overall efficiency is to be maximized). The GBS project enjoys economies of scale due to the high fixed costs of scanning books and negotiating a class action settlement, in contrast to the low marginal costs of making available an additional digital book copy or institutional subscription license. Considerable economies of scope are potentially captured by Google’s combination of orphan works and non-orphan works, web searches and online purchases of books, and individual users and institutional users in its consumer base. However, while administration of book licensing or distribution is highly inefficient if conducted by individual rightsholders, it does not follow that that having a single intermediary (i.e. Google) is necessarily more efficient than using several licensing intermediaries. It all depends on the tradeoff between allocative efficiency (derived from price competition between two or more licensing intermediaries) and productive efficiency (due to economies of scale or scope enjoyed by a large operation like Google, as discussed above). As Professor Katz observed in the context of music performance rights licensing, “the existence of multiple publishers [of records, CDs, and sheet music] of varying sizes suggests that the minimum efficient scale for copyright administration . . . can probably be achieved at scales that fall well short of a monopoly.”

The same argument can be made for the licensing and distribution of digital books: the market is likely to operate most efficiently, considering both productive and allocative efficiency absent price regulation, with more than a single intermediary, and the number of intermediaries should be comparable to the number of major book publishers and bookstores out there. Considering the tradeoff of allocative efficiency and productive inefficiency alone, market entry is justified, and courts should allow it, so long as gains from enhanced intermediary competition outweigh forgone efficiencies in a more concentrated distribution network.

But it is also important to consider the tradeoff between short-term improvements to allocative efficiency and long-term implications for qualitative efficiency. The prospect that any entrant can easily enter the market and “free-ride” on Google’s entry efforts may well create

147. Ji, supra note 38, at 272–73.
148. Id. at 273.
149. Katz, supra note 41, at 554.
disincentives on the part of Google, and its competitors, to undertake similar risky ventures in the future. Even Professor Picker, one major critic of the GBS settlement agreement, stipulated that if a restraint is a *sine qua non* for bringing about the innovation in the first place, the antitrust response should be to permit the restraint rather than to strike it down. Some might argue that the relevant “innovation” here should be limited to developing a universal book search service, but not a full access and distribution service, and that when Google started the GBS project, it only envisioned “people everywhere being able to search through all of the world’s books to find the ones they’re looking for.” There are two responses to this argument. First, Google’s intention was at best ambiguous: shortly after announcing the commencement of the GBS project in 2004, it invited publishers in 2006 to collaborate with it in developing a sales model for full access to books online within the GBS system. Secondly, even if Google’s original idea was to develop a universal book search system only, it cannot be certain that Google would have moved forward with scanning millions of books and risking to be sued had it known ex ante that antitrust law would intervene to allow a competitor to readily gain access to a broad orphan works license. Further, without Google first developing a book search system, the offering of full access to books (whether through consumer purchases or institutional subscriptions) could hardly become a reality. If antitrust law required a private company to facilitate rivals’ entry should it succeed in creating a market, it would likely perversely dissuade the company from acting in the first place, and this is true not only for Google but any company on the fence about whether to proceed on a risky endeavor. Where the trade-off between allocative efficiency and qualitative efficiency is uncertain, the general wisdom is to err on the allocative side rather than to assume the risk of forgoing new product creation in the long run with the ex post substitution of LRAs. This is especially true in the book digitalization context where no other firm has thus far been able to produce anything similar to the near universal access to books that the GBS settlement is seeking to provide. The closest company is perhaps Microsoft: the computer giant previously ran a “Live Book Search” project with the goal of assembling a library of 750,000 books (with public domain and licensed commercially available

152. *Id.*
153. Elhauge, supra note 38, at 18.
154. *Id.*
works), but abandoned it in 2008 due to the lack of a sustainable business model. The outcome of the foregoing analysis is that granting Google de facto exclusivity over orphan works is a necessary restraint in order to provide sufficient incentives for Google to have developed a universal book search and distribution network, and hence should be upheld as legitimate under the antitrust rule of reason. It would not be in society’s interests to authorize either the Registry or UWF to grant a collective orphan works license to a competitor of Google which is interested in becoming a digital books intermediary.

B. Price-fixing at wholesale and retail levels

Settlement critics have expressed concerns that there will be price fixing by rightsholders, facilitated by Google, at both the wholesale and retail levels. It is helpful to think of each rightsholder as a “wholesaler” of a book with Google acting as the “retailer,” with Google charging the “retail markup,” (the percentage of revenue accruing to Google through consumer purchases and institutional subscriptions) and the remaining sales proceeds returning to each rightsholder as the “wholesale price.” The pricing of “consumer purchases” and “institutional subscriptions” will be considered in turn.

1. Consumer purchases

It is important to understand how the pricing scheme works for individual purchases before delving into its allegedly anticompetitive aspects. As previously mentioned, commercially available books are by default excluded from the Google book search and distribution system. If a rightsholder elects to have his book included in Google’s distribution system, it can set the list price of the book (at any price, even zero) or ask Google to compute a price based on the Pricing Algorithm. There is also a hybrid mechanism whereby a rightsholder specifies the maximum and minimum prices within which Google can set the book price. In contrast, commercially unavailable books are by default included in the search and distribution system, and Google will price these books using the Pricing Algorithm, unless a rightsholder comes forward to set a price or ask for its exclusion from the system. Rightsholders of orphan works, by definition,

155. Id.
156. See, e.g., Picker, supra note 128, at 398.
157. Amended Settlement Agreement, supra note 17, § 3.2.
158. Id. § 4.2(b), (c)(i).
159. Id.
160. Id. §§ 3.2(b), 3.3(a), 4.2(b).
have not come forward, so there is no choice but to have Google price these books according to the Algorithm. The default revenue split between the rightsholder and Google is sixty-three percent to thirty-seven percent which can be varied upwards or downwards at the request of either party (each may also elect to walk away from the transaction). Although a rightsholder, or Google on his behalf based on the Algorithm, is setting the retail price, it is in effect setting the wholesale price only. This is because Google can always "provide discounts off the List Prices at its sole discretion" but also at its own cost (since the revenue split will still be based on the original List Price set by a rightsholder, unless otherwise agreed). The list price specified by the rightsholder (or under the Pricing Algorithm) therefore establishes a price ceiling that Google cannot go beyond. In other words, there is a vertical agreement to fix maximum retail prices.

Let us first consider the Pricing Algorithm. Some settlement critics are concerned that the Algorithm will be used by Google to facilitate cartelization of wholesale, retail prices, or both among rightsholders. For example, Professor Picker worried that "rightholders are collectively appointing Google as their agent to implement pricing rules for Consumer Purchases that do not seem to mimic ... pure decentralized competition," which would "drive[] down prices to costs and [would] not have the effect of maximizing revenues to individual competitors." This concern was indeed a legitimate one given how the parties drafted the pricing clause (§ 4.2(b)(i)(2)) in the original Settlement Agreement. Under the original clause, the Pricing Algorithm was "design[ed] to find the optimal such price for each Book and, accordingly, to maximize revenue for each Rightsholder." This effectively meant that Google should set a schedule of cartel prices for all books simultaneously that would maximize revenue (and hence profits, since the marginal cost of producing a digital book copy is zero) for all rightsholders collectively. Indeed, this was not different than an express cartel among rightsholders, with Google acting as the central decision-maker, to fix retail and wholesale prices with a view to earning monopoly profits for the industry (note: whether a book cartel is itself sustainable is a separate issue, which will be discussed shortly). Such simultaneous price setting

161. Id. § 2.1(a).
162. Amended Settlement Agreement, supra note 17, §§ 3.2., 4.5(b)(i).
163. Picker, supra note 128, at 398.
164. Id.
165. Settlement Agreement, supra note 133, § 4.2(b)(i)(2).
166. See Elhauge, supra note 38, at 37; Fraser, supra note 38, at 13.
would be complicated, requiring knowledge of the entire matrix of pricing elasticities of books, but it is very much within Google's capacity given its significant computing power and ability to run sophisticated pricing experiments.\textsuperscript{167} In response to this cartelization concern, therefore, the pricing clause has been modified as part of the Amended Settlement Agreement. Under § 4.2(b)(i)(2) of the present agreement, the Pricing Algorithm is now configured to "find the optimal price for each . . . Book in order to maximize revenues for the Rightsholder for each such Book and without regard to changes to the price of any other Book (but Google may use historical price data of other Books in designing the Pricing Algorithm)."\textsuperscript{168} Section 4.2(c)(ii)(2) goes on to provide that "[t]he Pricing Algorithm . . . will be designed to operate in a manner that simulates how an individual Book would be priced by a Rightsholder of that Book acting in a manner to optimize revenues in respect of such Book in a competitive market . . . assuming no change in the price of any other Book."\textsuperscript{169}

The present Pricing Algorithm is therefore seeking to simulate a Bertrand pricing game: each rightsholder will set a price for each book individually taking prices of other books as exogenous; competition between digital books will presumably drive prices down to marginal costs (essentially zero) plus a premium reflecting the differentiated nature of books.\textsuperscript{170} Professor Picker was mistaken in suggesting that competition always drives prices down to cost and that producers in a competitive environment do not maximize revenues and profits. The reality is that producers always aim to maximize profits by producing up to the point where marginal revenue (MR) meets marginal cost (MC), and this is true irrespective of whether the applicable competitive model is perfect competition, monopoly, or something in between (such as a differentiated, monopolistically competitive market for digital books in the present case). MR equaling MC is not a sufficient condition for P equaling MC; the fact that books are differentiated products suggests that every rightsholder has some degree of market power enabling him to price above MC. Absent coordination between rightsholders, this price will be lower than the cartel and monopoly price. In fact, the producer surplus that a rightsholder earns by pricing above MC (which approximates to zero for digital books, typical of digital copyrights) plays a significant role in incentivizing innovation (i.e. the authorship of books) in the first place. Although

\textsuperscript{167} Fraser, supra note 38, at 14.
\textsuperscript{168} Amended Settlement Agreement, supra note 17, § 4.2(b)(i)(2).
\textsuperscript{169} Id. § 4.2(c)(ii)(2).
\textsuperscript{170} Fraser, supra note 38, at 13.
the Pricing Algorithm does not bring prices down to MC, it does preclude any form of horizontal collusion: not only express cartel pricing, but also tacit collusion that is typical of oligopolistic markets, since Google is required to price any book “without regard to changes to” and “assuming no change in the price of any other Book.” As Professor Elhauge observed, antitrust law does not prevent a rights holder from responding intelligently to rival price changes or considering effects on rival prices, at least in the absence of “plus factors,” such as extremely improbable confidence, actions contrary to self-interest, and ruinous industry conditions. Since the Algorithm will only result in more competitive prices than individual price setting by rightsholders, which can be elected so long as the rights holder is not an orphan work owner, the court should characterize it as procompetitive, not anticompetitive.

What of the argument that agreed-upon pricing formulas among competitors are always anticompetitive and should be condemned as per se illegal, as some precedents seem to suggest? Professors Areeda and Hovenkamp have provided some useful guidance for determining whether agreed-pricing formulas raise anticompetitive concerns:

The principal danger of agreed-upon pricing formulas is that they enable competing sellers to track one another’s pricing more readily. For example, if real estate brokers agree to use fees based on a percentage of sale service, any deviation from the “going” commission rate is readily detected. But if a broker uses some alternative formula, such as payment by the hour or by the transaction, then interseller pricing verification can be much more difficult.

Indeed, it is highly unlikely that a formula that is principle-based but not rule-based, conveying the basic idea that Google will charge consumers prices in a competitive Nash-Bertrand market, will have the effect of facilitating inter-seller verification. In fact, market conditions suggest that detection of cheating in a digital book market will be formidable difficult, as will be explained below. To the extent that legal precedents suggest that the use of pricing formulas are per se illegal, they are wrongly decided and should not be applied to condemn the

171. Amended Settlement Agreement, supra note 17, § 4.2(b)(i)(2).
172. Id. § 4.2(c)(ii)(2).
174. Elhauge, supra note 38, at 38.
176. AREEDA & HOVENKAMP, supra note 68, § 20.25(d).
Pricing Algorithm in the GBS settlement. Having said that, Google’s use of a set of pre-defined discrete “pricing bins” (i.e. books processed under the Pricing Algorithm will be given a price of either $1.99, $2.99, $3.99, and so forth until $14.99, $19.99 and $29.99)\textsuperscript{177} is questionable from an antitrust point of view. Professor Picker does not think that “this centralized . . . approach matches what would emerge from normal, decentralized competition.”\textsuperscript{178} Indeed, the pricing-bin approach seems to fall squarely within the Socony-Vacuum rule that it is price fixing if “the prices paid or charged are to be at a certain level or on ascending or descending scales.”\textsuperscript{179} A cursory search on Amazon.com would reveal that a large number of books are priced at the margin of $0.01, the lowest currency denomination in the U.S.\textsuperscript{180} As electronic forms of payment have become almost exclusive in online commerce, there seems to be no convincing argument based on transaction costs or Google’s productive efficiency that could justify the use of pricing bins in dollar intervals; they should therefore be abandoned for lack of a procompetitive justification.

Regardless of how the Pricing Algorithm operates, essential elements of successful collusion, the ability to reach a consensus, to detect and punish cheating, and to maintain supra-competitive prices,\textsuperscript{181} are apparently lacking in the digitized books market. Product differentiation is perhaps the most significant factor rendering unlikely any form of collusion among rightsholders.\textsuperscript{182} A prominent antitrust and IP treatise has observed that “individual books are extremely differentiated from one another in consumers' eyes and many titles are not even regarded as 'competing' with one another.”\textsuperscript{183} Any agreement between rightsholders would require some understood relationship between different books so that their rightsholders could agree upon the appropriate price differentials.\textsuperscript{184} However, given the significant degree of differentiation among books, “differences in consumer preference will make a consensus more difficult to attain and may give one participant significant advantage over others.”\textsuperscript{185} Other market conditions also diminish the chance of successful collusion between

\begin{itemize}
\item \textsuperscript{177} Amended Settlement Agreement, \textit{supra} note 17, § 4.2(c)(ii)(1).
\item \textsuperscript{178} Picker, \textit{supra} note 128, at 398.
\item \textsuperscript{179} \textit{Socony-Vacuum Oil Co.}, 310 U.S. at 222.
\item \textsuperscript{180} For example, Judge Posner's “The Crisis of Capitalist Democracy” and “How Judges Think” were priced at $17.13 and $12.89 respectively on May 2, 2011.
\item \textsuperscript{181} \textit{Aareeda & Kaplow, supra} note 173, at 204–05.
\item \textsuperscript{183} \textit{Id.} §30.4, at 30–16, 30–17.
\item \textsuperscript{184} \textit{Aareeda & Kaplow, supra} note 173, at 205.
\item \textsuperscript{185} \textit{Hovenkamp et al., supra} note 182, § 30.4, at 30–36.
\end{itemize}
rightsholders: (1) authors and publishers are numerous, rendering co-
coordination and detection difficult; (2) barriers to entry are low, since
anyone who can write has a chance of being published; (3) many right-
holders who are individual authors or academics value wider readers-
ship over profit-making and have incentives to cheat by lowering
prices of their books;\textsuperscript{186} and (4) there is no effective mechanism for
punishing any cheating identified inside or outside the settlement
agreement.\textsuperscript{187}

If there is no price fixing at the retail level, there will not be whole-
sale price fixing given the structure of the royalty division arrange-
ment between Google and rightsholders under the settlement
agreement. The default sixty-three percent to thirty-seven percent
revenue split between rightsholders and Google means that the
wholesale price is by default thirty-seven percent of the list price of
any book, which is the final retail price assuming no discounts from
Google. If the retail price ($P$) is competitive under Nash-Bertrand
market conditions, the competitive price at wholesale level would be
thirty-seven percent multiplied by the retail price; a competitive price
at the wholesale level. Although the wholesale price varies precisely
with the retail price in percentage terms, the revenue split itself does
not affect the incentives of any rightsholder (or Google on its behalf)
to set a competitive price to maximize revenues and profits for his
book absent collusion.\textsuperscript{188} Some might argue that a fixed royalty split
would lead to some form of wholesale price stability, but one should
note that the sixty-three percent to thirty-seven percent split is only
the default royalty split. Indeed, if the distribution makeup based on
the default split is inefficient in promoting sales for a commercially
available book, either Google or a rightsholder has the incentive and
the right to ask for an upward or downward adjustment in the split, or
to opt out of the transaction altogether.\textsuperscript{189}

Nevertheless, there seems to be no convincing justification for why
the settlement parties have not extended this renegotiation power to
cover commercially unavailable books.\textsuperscript{190} This is a particularly worry-
ing feature given that commercially unavailable books form the over-
whelming majority of books covered under the settlement.\textsuperscript{191}
Although it is impossible for orphan work authors to negotiate a reve-

\begin{itemize}
  \item \textsuperscript{186} Jerry A. Hausman & J. Gregory Sidak, \textit{Google and the Proper Antitrust Scrutiny of Or-
  \item \textsuperscript{187} Id. at 434.
  \item \textsuperscript{188} Elhauge, \textit{supra} note 38, at 39.
  \item \textsuperscript{189} See \textit{id.} at 40; Amended Settlement Agreement, \textit{supra} note 17, § 4.5(a)(iii).
  \item \textsuperscript{190} See Ji, \textit{supra} note 38, at 259.
  \item \textsuperscript{191} \textit{Id.}
\end{itemize}
nue split with Google, it is submitted that the scope of the renegotiation power should be expanded to cover commercially unavailable works with traceable rightsholders. It is true that allowing bargaining for out-of-print books would create negotiation costs, but such costs are high only in a bilateral monopoly situation where Google has substantial buyer power and a rightsholder has substantial seller power. But unless one is the author of a bestselling title or is a large publisher owning the copyright of many books, it is inconceivable that an ordinary rightsholder would have significant bargaining power vis-à-vis Google that would empower him to request for a substantial revenue share or outright exclusion of its book. In fact, it is reasonable to expect that many rightsholders would not exercise this renegotiation power, which means that Google, and hence society, would not have to incur high transaction costs due to negotiation with numerous parties. But this does not mean the majority of books would be sold at around the same wholesale price: significant price differentials would still remain at the wholesale level simply because of the highly differentiated nature of books.

There was previously a scheme of minimum resale price maintenance (RPM) under the settlement agreement. Section 4.5(b) of the original settlement agreement only allows Google to provide “temporary discounts” from list prices set by rightsholders, or set by Google based on the Pricing Algorithm; the relevant rightsholder and the Registry must approve any discounts for more than a temporary duration. However, the settlement parties removed the RPM scheme and they have only retained maximum retail price limitation (analyzed below) under the amended settlement. This was presumably a response to the DOJ’s criticism regarding “restrictions on retail price competition” in its amicus brief. It is indeed questionable whether the removal of RPM is necessary and desirable, especially in light of Leegin in which the Supreme Court held that courts should test any RPM scheme under the rule of reason instead of condemning it as per se illegal. The primary anticompetitive concern of RPM, its facilitation of either a manufacturer or retailer cartel, is apparently absent in the present case, since Google is the only retailer and any collusion among rightsholders at the wholesale level is highly unlikely for rea-

192. Settlement Agreement, supra note 133, § 4.5(b).
195. Id. at 892–93.
sons already explained above. On the contrary, a RPM scheme carries a strong procompetitive justification of incentivizing distribution services and preventing free riding.\textsuperscript{196} Rightsholders may wish to provide Google with a guaranteed distribution margin so as to incentivize the latter, as with other Internet or physical booksellers, to provide better promotional services or recommendation of books, which would induce their demand.\textsuperscript{197} The above analysis suggests that the original RPM scheme is procompetitive for it enhances interbrand competition without any sacrifice of intrabrand competition. The parties should therefore have retained the scheme in their settlement agreement to be later approved by the court after conducting a rule of reason analysis.

As for maximum resale price limitation, it should be seen as a solution to the classic problem of double marginalization. A producer, or any downstream firm, with some degree of market power, as in the case of monopolistic competition in a market of differentiated books, will set its wholesale price at some level above $MC$. This results in an output lower than that observed under conditions of perfect competition. A retailer who possesses market power at the retail level will then take this wholesale price as given and set a supracompetitive retail price at a level further above $MC$. This causes a further reduction in market output, which is undesirable for both the producer (due to fewer sales and hence lower profits) and the consumer (who either faces a higher price or is turned away despite his willingness to pay above $MC$ of the product). Maximum resale price limitation is therefore an effective solution to the problem: a rightsholder now specifies the maximum price at which Google can sell its digital rights in a particular book, thus limiting Google to a competitive markup.\textsuperscript{198}

Meanwhile, the potential competitive evils of maximum resale price fixing are apparently absent. For example, one anticompetitive possibility is that rightsholders set a wrong retail price, one that is unduly low, that would limit dealer services. Market forces, however, would swiftly correct this with Google negotiating for a higher royalty share (for example, a fifty percent split instead of sixty-three percent to thirty-seven percent) or insisting to drop the book for "non-editorial reasons" unless the rightsholder agrees to raise the retail price, and hence the retail markup, to an efficient level.\textsuperscript{199} Another potential concern is that a maximum resale price is in fact a minimum price in

\textsuperscript{196} \textit{Id.} at 890–91.
\textsuperscript{197} Elhauge, \textit{supra} note 38, at 34 n.58.
\textsuperscript{198} \textit{AREEDA & HOVENKAMP, supra} note 68, § 758(c).
\textsuperscript{199} \textit{Id.} § 1637(e).
disguise. However, such disguise would rarely be successful;\textsuperscript{200} and in any event, for reasons already mentioned, any RPM scheme would only be procompetitive in the present context and should be encouraged. Since the maximum resale price limitation operates procompetitively against double marginalization and does not raise anticompetitive concerns, it should remain in the settlement agreement (if not coupled with a restored RPM scheme) with the expectation that courts would approve the retail price cap under the antitrust rule of reason.

2. Institutional subscriptions

Apart from consumer purchases, Google will offer institutional subscriptions—essentially blanket licenses that cover all commercially unavailable books eligible for consumer purchase through Google and commercially available books that rightsholders elect to include the institutional subscription—to corporations, educational institutions, the government, and other institutions. Pricing of institutional subscriptions in accordance with the two objectives is set out in § 4.1(a)(i): "(1) the realization of revenue at market rates for each Book . . . and (2) the realization of broad access to the Books by the public, including institutions of higher education."\textsuperscript{201} As with consumer purchases, some settlement critics fear that the settlement will provide Google with a monopoly in collective licensing of books and accordingly the power to charge supracompetitive prices.\textsuperscript{202} This concern was doubted by Professor Elhauge, who argues that the objectives of charging “market rates” and ensuring “broad access . . . by the public” entail that “institutional subscriptions must be priced low enough to produce the sort of broad access that is consistent with the market output that would exist with competitive pricing.”\textsuperscript{203}

Leaving aside the issue of implementing the pricing objectives, does Google’s charging of monopoly prices for institutional subscriptions raise antitrust concerns at all? Two important factors suggest that the answer is negative. First, Google is seeking to offer a new product: a blanket license for digital access to a near-universal collection of books. This product is "new," for it is qualitatively distinguishable from individual books or its closest substitute—physical access to the

\textsuperscript{200} Id. § 1637(c).
\textsuperscript{201} Amended Settlement Agreement, supra note 17, § 4.1(a)(i).
\textsuperscript{203} Elhauge, supra note 38, at 53.
largest library in the world. The ability to access millions of volumes of books from any remote location without delays due to recall or interlibrary transfers is surely much more productive to academic research.\textsuperscript{204} Users can perform keyword searches on a universal database of books without necessarily knowing which ones are useful to them beforehand.\textsuperscript{205} As books continue to accumulate on this database, Google's books search system can grow into the book-equivalent of Westlaw (a database of court judgments and legislation) or HeinOnline (a database of legal journals). As noted earlier, Google's institutional subscription closely analogizes to ASCAP's or BMI's blanket license for music performing rights. The Supreme Court remarked in \textit{BMI} that the blanket license is a "different product" that should be "differentiate[d] . . . from individual use licenses," for "[i]t allows the licensee immediate use of covered compositions, without the delay of prior individual negotiations, and great flexibility in the choice of music material."\textsuperscript{206} That the blanket license is a new product that creates substantial qualitative efficiencies is the decisive reason behind the Supreme Court's ruling that courts should test the pricing of the blanket license under the rule of reason.\textsuperscript{207} On remand, the Second Circuit relied on copyright owners' "unimpaired independence" to grant individual licenses to users to uphold the blanket licensing scheme under a rule of reason analysis.\textsuperscript{208} As noted previously, the blanket license under the GBS settlement is in many ways less restrictive and more procompetitive than the ASCAP and BMI scheme, suggesting that Google's pricing of institutional subscriptions could hardly raise any antitrust problems.

Some might argue that despite the overall procompetitiveness of the blanket license as being a new product, it would not be an LRA to prevent Google from charging monopoly prices by imposing some form of price ceiling for Google's institutional subscription service. This leads us to the second point—the limits of antitrust in terms of price control. It is important to note that unlike E.U. competition law, U.S. antitrust law does not impose liability for a firm's charging of excessive or monopoly prices.\textsuperscript{209} The Supreme Court famously re-

\begin{itemize}
\item \textsuperscript{204} Hausman & Sidak, \textit{supra} note 186, at 419.
\item \textsuperscript{205} Ethauge, \textit{supra} note 38, at 52.
\item \textsuperscript{206} Broad. Music, Inc. v. CBS, Inc., 441 U.S. 1, 21–22 (1979).
\item \textsuperscript{207} \textit{Id.} at 23–24.
\item \textsuperscript{208} CBS, Inc. v. Am. Soc'y of Composers, Authors and Publishers, 620 F.2d 930, 936 (2d Cir. 1980).
\item \textsuperscript{209} See Case C-385/07 P, Der Grüne Punkt – Duales System Deutschland GmbH v. Comm'n, (2009), available at http://curia.europa.eu/en/content/juris/ (click the case number and then click on the “opinion" link), for a case in which the European Commission found excessive
\end{itemize}
marked in *Trinko* that "[t]he opportunity to charge monopoly prices—at least for a short period—is what attracts ‘business acumen’ in the first place; it induces risk taking that produces innovation and economic growth." Google’s charging of supracompetitive subscription fees can therefore be seen as “procompetitive” from an ex ante perspective as it serves as the prize rewarding Google for its innovation and entrepreneurship in undertaking the GBS project. In any event, to place an ex post ceiling on institutional subscription charges would amount to price regulation, something that antitrust authorities have painstakingly sought to avoid. Society would not improve if antitrust authorities simply substituted their valuation of a product or service for that of the transacting parties, here Google and the institutional subscribers. On the other hand, there could hardly be an objective measure of what constitutes an “excessive” or “monopoly” price. Under EU competition law, prices are considered “excessive” if they bear “no reasonable relation to the economic value of the product” and will constitute an abuse of dominance in violation of Article 102 of the TFEU. But isn’t the “economic value” of a product precisely how much a consumer values the product—his “willingness to pay” (WTP) as described by that product’s demand curve? If the EU authorities meant that a price is excessive if it is significantly higher (hence bearing “no reasonable relation”) to a consumer’s WTP, which consumer along a downward-sloping demand curve are they referring to? Even if they manage to pick the “right” consumer, how much below this consumer’s WTP should constitute a safe harbor for pricing? Given these conceptual difficulties of defining the boundaries for illegally high prices, it is indeed sound antitrust policy not to condemn the charging of excessive prices ex post. In any case, it is inconceivable that Google would start charging exorbitant subscription fees, since doing so would threaten the Internet giant with reputational sanctions (and consequently, loss of advertising revenue) and the risk of losing large institutional customers in the aftermath.

Apart from the two pricing objectives under § 4.1(a)(i), Google also plans to implement third-degree price discrimination for its institutional subscriptions. This is a kind of imperfect discrimination, aim-
ing to extract as much consumer surplus (that would be observed under perfectly competitive conditions) as possible by charging different customer groups different prices that approximate their different valuations of the product. Google plans to vary subscription fees according to the number of full time equivalents (FTEs) and the nature of the institution (i.e., corporate, higher education, school, government, or others). One critic pointed out that FTE pricing is "neither an accurate nor fair gauge of the true value of the product" and could possibly lead to public libraries and universities (with a large of patrons) being priced out of the market. He therefore recommended that Google price subscriptions based on actual usage patterns according to a simulations pricing model.

This criticism reflects a misunderstanding of the economics behind price discrimination. In fact, an FTE price, which is designed to track an institution's willingness and ability to pay, better reflects the "true value of the product" with respect to that institution than a price based on usage patterns (which does not capture the earning power aspect of willingness to pay). The same arguments against condemnation of excessive pricing noted above also apply here: to render illegal a pricing scheme that does not "fair[ly] gauge . . . the true value of the product" is bound to cause definitional problems and harm rather than good to economic efficiency.

In fact, third-degree price discrimination is usually procompetitive and courts should not condemn such conduct on antitrust grounds without a detailed analysis of its competitive effects. Since third-degree price discrimination is imperfect, there is no dispute in that market output will be lower than the perfectly competitive level. But perfectly competitive pricing and output will never be observed in situations where price discrimination is feasible. Persistent price discrimination requires some degree of market power, as where the market consists of differentiated products. This means even in the absence of price discrimination, the seller would be charging a price above MC, or a "monopoly price" in the broad sense. Whether third-degree price discrimination is pro- or anti-competitive will depend on

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214. Full time equivalents are figures representing the number of full time employees or students at an institution.


217. Id. at 203.

218. Id.

219. AREEDA & HOVENKAMP, supra note 68, § 721(c).
whether it enhances output compared to market conditions under nondiscriminatory monopoly pricing. If the discrimination is output reducing, it is anticompetitive for it results in incremental deadweight loss \textit{vis-à-vis} the nondiscriminatory monopoly situation (added to this is the social loss in rent-seeking behavior: the seller’s expenses in identifying and segregating different customer groups).\textsuperscript{220} Even then, antitrust intervention may not be justified if market correction is possible, that is, if new entrants can enter the market to serve customers priced out of the market because of discrimination and undercut the “monopolist” with respect to its existing sales. Economic theory therefore suggests that antitrust law should only intervene if price discrimination is accompanied by an exclusionary practice such as predatory pricing.\textsuperscript{221}

This economic thinking is reflected in the Robinson-Patman Act provisions relevant to price discrimination.\textsuperscript{222} To allege a primary line violation,\textsuperscript{223} the plaintiff is required to prove that the defendant is using high prices in one market to subsidize losses due to predatory pricing in another market.\textsuperscript{224} The Act therefore effectively subsumes primary-line price discrimination under antitrust law’s predatory pricing doctrine. Since the Supreme Court’s decision in \textit{Brooke Group},\textsuperscript{225} just as in a case of predatory pricing under § 2 of the Sherman Act, a plaintiff must show that a defendant seller is pricing below cost with regard to a particular market, and a dangerous probability of recoupment of the loss.\textsuperscript{226} To apply it to the present case, this would require proof that Google is making a loss on sales to a particular customer group and is offsetting this loss by selling profitably to another group. Putting aside the difficulty of proving recoupment, pricing below cost is most unlikely to be found when it comes to selling IP rights; the marginal cost of making available access to another buyer is close to

\begin{itemize}
\item \textsuperscript{220} \textit{Hovenkamp}, \textit{supra} note 70, at 577.
\item \textsuperscript{221} See \textit{id.} (indicating that this is particularly true if the market is competitive or oligopolistic).
\item \textsuperscript{223} See \textit{Einher R. Elhauge & Damien Geradin, Global Competition Law and Economics} 366, 689 (2007) (indicating that a primary line violation is price discrimination that affects competition at the seller’s level. The anticompetitive concern is that the seller is using high prices in one area to subsidize predatory prices in another; the lower price is targeted at customers of the seller’s rivals and will discipline the rivals or drive them out of the market).
\item \textsuperscript{224} See \textit{Perkins v. Standard Oil Co.}, 395 U.S. 642 (1969); \textit{Hovenkamp}, \textit{supra} note 70, at 581.
\item \textsuperscript{225} \textit{Brooke Grp. Ltd. v. Brown & Williamson Tobacco Corp.}, 509 U.S. 209 (1993).
\item \textsuperscript{226} \textit{id}. The only difference between Sherman Act and Robinson-Patman Act is that the former applies only to predatory pricing that facilitates a single-firm monopoly (therefore requiring proof of monopoly power), whereas the latter applies to predatory pricing that might facilitate oligopoly as well; see \textit{Hovenkamp}, \textit{supra} note 70, at 367, 579.
\end{itemize}
It should be noted that secondary line violation under the Robinson-Patman Act is irrelevant here since institutions subscribing to Google's blanket license are not competing in any downstream market; they are not in the business of reselling the access rights to any buyer that is further downstream.

One commentator has argued that Google should offer "narrower licensing alternatives" (e.g., a subscription covering only medical books specifically for medical schools) if they are "shown to be more efficient than broader blanket licenses in the book digitization context" and that Google's refusal to offer narrower alternatives "could raise antitrust concerns." However, it is difficult to see why having Google offer narrower licenses would lead to a more procompetitive result. It is not even obvious that specific institutions, such as law schools or medical schools, would necessarily be paying lower prices for a tailor-made subscription. The MC of making available another digital book copy is zero for Google, which is typical of most blanket licensing arrangements charging a lump-sum fee upfront (an example is the ASCAP and BMI music-performing license). In any event, the licensing fee that an institution pays Google is only a pure wealth transfer. In contrast, it costs more to the licensor, and to society, to offer several tailor-made licenses than to offer one full blanket license, since the former involves additional costs of categorization and resolving or avoiding disputes over the scope of a specific license. This is the court's primary reason for rejecting the plaintiff's request for "mini" licenses of country and western music in BMI v. Moor-Law: the court did not find BMI's refusal to offer narrower licenses to constitute an illegal tie-in as the licenses would be "significantly more expensive to administer than a full repertory one" and that "‘mini’ blanket licenses [were] not a practical alternative." In any event, a claim for narrower licensing alternatives in the present context will likely fail the standard requirements for establishing anticompetitive tying or bundled pricing: (1) coercion; (2) separate tying

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227. Hovenkamp et al., supra note 182, § 13.5(b). Though this raises the issue of whether MC is the appropriate metric by which to judge predatory pricing in information markets. Some commentators have argued that average cost (AC) is a more appropriate measure since it accounts for the upfront research and development costs that the IP creator has incurred before commercializing his IP rights. There has also been a long-running debate in regulated industries as to whether regulators should allow public utilities to charge prices tied to AC or MC.

228. Elhaug & Geradin, supra note 223.

229. Suarez, supra note 216, at 201.

230. Id. at 200.


232. Id. at 767

233. Id. at 769.
and tied products; (3) tying product power; and (4) a significant foreclosure of the tied product market.\textsuperscript{234} The second issue is whether the institutional subscription is a tie-in of the desired narrower licenses or a single, new product; the essential question being whether assembling two components into a single package would create synergies (qualitative efficiency) or cost savings (productive efficiency). Similar to the music licensing situation, it would be costly for Google to tailor its blanket license to suit the preferences of each and every institution as the company would run into troubles of categorizing books and defining the scope of works covered by each type of subscription. Antitrust should not intervene on cost-saving arrangements even if certain customers would prefer a predefined subset of works in the licensor's library.\textsuperscript{235} As to the fourth condition, foreclosure only occurs if a buyer would have purchased the tied product separately from an alternative seller had he been given the opportunity.\textsuperscript{236} This will not be the case here since the licensees (institutions) do not want the tied copyrights—i.e. access to books of no relevance or interest to them—at all, since no rival licensor is being foreclosed. The lack of foreclosure or other anticompetitive effects suggests that there is no antitrust concern in Google's insistence on offering a single institutional subscription covering the universe of GBS books as opposed to narrower, institution-specific licenses.

C. Proposed Modifications

The relevant question here is the following: can aspects of the settlement agreement be modified or can new features be added onto the settlement to enhance the procompetitiveness of the GBS project? There are three categories of modifications that Google and rightsholders ought to consider: (1) scope of works; (2) new revenue models; and (3) the offering of complementary and derivative services.

As to the scope of works, the present settlement only covers commercially unavailable books, including orphan works.\textsuperscript{237} Commercially available books and books published after January 5, 2009 are excluded unless and until Google strikes a deal with the relevant rightsholders regarding online search and sales.\textsuperscript{238} Since commercially available books currently constitute ninety-seven percent of total

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  \item \textsuperscript{234} See Jefferson Parish Hosp. Dist. v. Hyde, 466 U.S. 2, 37–41 (1984); Hovenkamp et al., supra note 182, § 22.3.
  \item \textsuperscript{235} Broad. Music Inc., 527 F.Supp. at 765, n.7; Hovenkamp et al., supra note 182, § 22.3(b).
  \item \textsuperscript{236} Hovenkamp et al., supra note 182, § 22.4(a)(2).
  \item \textsuperscript{237} Amended Settlement Agreement, supra note 17, § 3.2.
  \item \textsuperscript{238} Id. §§ 1.97, 3.2.
\end{itemize}
\end{footnotesize}
books sales in the U.S., excluding these books from GBS system will greatly reduce its value as a centralized book distribution and research platform. Although commercially available books are unlikely to be orphan works, it is complicated and costly for Google to identify each and every rightsholder, contact them individually to strike an independent deal, and repeat the process again for every book published in the future. Further complications are caused by the following two factors: (1) it is often unclear whether the publisher or the author has digital rights in a book since the contract between them may not have anticipated digitalization, so neither party may be willing to grant Google a license and bear the risk of being sued by the other party; and (2) tracing copyright usually goes beyond simply identifying the author since the right may have been transferred by contracts, corporate mergers, estates, or operation of statutory provisions. The complicated process of rights clearance entails, at least for newly published books, that Google will be slower than its competitors, such as Amazon or physical bookstores, in launching a new sale, thereby inhibiting the growth of the digital book market.

There is thus a strong case for changing the display and distribution of commercially available books from an opt-in to an opt-out to enhance the procompetitive effects of the GBS settlement. Not only would an opt-out system lead to transaction cost savings and expedited book distribution, but it would also build a near-universal collection of books and hence increase the inherent value of the GBS system. For example, in order for Google's institutional subscription to become a comprehensive research tool, it is important for the system to include all academic books across various disciplines, irrespective of their commercial availability and publication date. It would certainly defeat the purpose if students and researchers still had to search a physical library for the most recently published books which remain commercially available. The GBS project partly aims to promote equalization of resources among higher education institutions. The ultimate goal is therefore to build a digital corpus of millions of books from major research libraries that will be made available through institutional subscriptions at reasonable prices, so that every library around the world will instantly share the features of a world-

239. Elhauge, supra note 38, at 39 n.63.
240. Id. at 30–31.
class research facility. The exclusion of commercially available and post-2009-published books could only mean that major universities and colleges would continue to dominate the resource-constrained institutions in terms of academic resources and scholarly research.

On the other hand, an opt-out system for commercially available books is naturally free from anticompetitive concerns. It will not confer on Google exclusivity over such books—individual rightsholders will still have the discretion to sell them at any price through any distributor or multiple distributors. In fact, an opt-out system will help to promote retail price competition and increase output by automatically adding a new distributor—Google—with low distribution costs and without delay in shipping. A more comprehensive GBS system will also help to lower entry or expansion barriers for rivals by providing sellers with information on digital demand for new books and purchasers with an online platform by which they can easily search for books they want. Some may argue that substituting opt-in with opt-out distribution may create a windfall for Google since rivals will be facing higher costs having to negotiate individual deals for every new publication. To ensure that Google and its rivals compete on a level playing field, the settlement agreement should be modified to allow the Registry to grant collective licenses to Google's rivals over the scanning and distribution of commercially available and future books subject to rightsholders' choice to opt out at any time.

The parties earlier amended the settlement agreement to exclude foreign works—books not published in the U.S., Canada, the United Kingdom, or Australia—from its scope. U.S. copyright law protects many foreign works, even without registration or publication in the U.S. These works were excluded due to the concern over the adequacy of representation of foreign rightsholders and hence the ability to meet the requirements of Rule 23 for class action settlement approval. From an antitrust perspective, however, the exclusion of foreign works will severely undermine the procompetitiveness of the GBS system. The change will reduce the coverage of the project by almost fifty percent and will further entrench the dominance of En-

243. Samuelson, supra note 128, at 1310, 1339.
244. Elhauge, supra note 38, at 34–35.
245. Id. at 35 (noting that research by economists had shown that websites such as Amazon.com greatly facilitated the searching of a wide variety of books online, which led to an increase in consumer welfare from $731 million to $1.03 billion).
246. Amended Settlement Agreement, supra note 17, § 1.19.
247. Sag, supra note 2, at 39.
249. Sag, supra note 2, at 39.
English language works in the GBS database. It will hence undermine the utility of the GBS system as a comprehensive research tool and will impede the journey towards resource equalization among global academic institutions, similar to the effects of excluding commercially available books.

The inclusion of foreign works will only enhance the procompetitive effects of the GBS settlement. With regard to Google’s sales of foreign works within the U.S. market, they increase outputs since such works were unlikely offered for sale in the U.S. previously. Google is in no way free-riding on the efforts of foreign authors and publishers since it is only getting thirty-seven percent of the sales revenue (by default)—the remaining sixty-three percent goes to the foreign rightsholders and the split is always variable at the latter’s discretion. These incremental sales of foreign works are Pareto-efficient: they enhance the utility and profit of U.S. consumers, Google, and also foreign rightsholders without making anybody worse off. As regards Google’s sales of foreign works outside the U.S., the enhanced retail price competition between Google and existing foreign booksellers will help to reduce retail price and expand output, which ultimately benefits both foreign consumers and rightsholders in terms of higher consumer and producer surplus. Google will not have exclusivity over the distribution of foreign works, so rightsholders remain free to sell them through Google’s rivals at any price they desire, whether in the U.S. or abroad. According to the above analysis, the fact the foreign rightsholders might not be adequately represented should not be a concern after all, since Google’s distribution of foreign works in the U.S. or overseas could only make these rightsholders better off, not worse off.

The definition of “books” under the settlement agreement expressly excludes periodicals, personal papers, calendars, sheet music, songbooks, and government works (the last category is not copyright protected). There seems to be no good reason for excluding sheet music and songbooks from the GBS system if other utility works—such as cookbooks, atlases, and do-it-yourself guidebooks—are included. But it seems justified to exclude other product categories if some sensible line is to be drawn between books and non-books. The exclusion is necessary to prevent Google from becoming a “supermarket” of all digital products, which, unlike the case of Amazon and eBay, are distributed under an opt-out but not opt-in system. In any

250. Id. at 40.
251. Amended Settlement Agreement, supra note 17, § 1.19(i)–(vi).
event, periodicals and academic papers are already readily available from institutionally subscribed databases (such as Westlaw and HeinOnline) and free research distribution networks (such as the Social Science Research Network), so it will be largely redundant to also include them in the GBS system. Besides, anyone who wants a book-form calendar will prefer to buy them in printed form, allowing Google to distribute scanned versions of printed calendars electronically will do little to enhance efficiency simply due to their lack of demand. Periodicals, personal papers, and calendars are hence rightfully excluded from the GBS settlement.

The settlement agreement contemplates several new revenue models on which Google and rightsholders have yet to agree.\footnote{Id. § 4.7.} First, there are added features of print-on-demand (allowing purchasers to obtain a print copy of commercially unavailable books from a third party)\footnote{Id. § 4.7(a).} and file-download (enabling purchasers to download the online books as electronic files that can be read on mobile phones, e-book devices, and other electronic devices).\footnote{Id. § 4.7(b).} The print-on-demand feature is procompetitive for it will enable GBS-distributed books to compete directly with hardcopy sales sold through physical or online bookstores, and there seems to be no reason why the feature should not be expanded to cover commercially available books especially after they have become part of the opt-out distribution system proposed above. Meanwhile, the file-download service will enable GBS books to enter into direct competition with electronic books currently only available on a Kindle, Nook, or other proprietary devices. The only concern for allowing the downloading of GBS books is piracy of digital books and the diminished incentives for authorship that may follow. But the piracy problem can be easily resolved by utilizing digital-rights-management technology. Files downloaded from the GBS system can be configured so that they can only be read using a Google-designated software program. The program itself can be installed in any electronic device including desktop computers, laptops, mobile phones, e-readers, and portable media players, so as to ensure medium neutrality. In order to prevent unauthorized distribution of GBS files to multiple electronic devices for use by multiple users, each GBS-program must be registered online using a unique name and a buyer of a GBS book can specify up to five to ten unique names which will have the right to access the purchased copy. In this way, every copy of a GBS book will be used only by a limited number of users on
a limited number of electronic devices, which can effectively solve the piracy and disincentive issue. On the other hand, the General Counsel of Google claimed that it has plans to partner with bookstores, publishers, and device manufacturers to develop an open platform whereby readers can purchase electronic books from any bookstore and read them on multiple electronic devices from multiple vendors. While the movement towards medium neutrality and a single standard for digital books is itself welcoming, antitrust authorities must make sure the partnership is not a pretext for cartelization among distributors of digital books and manufacturers of electronic reading devices. As noted above, a cartel among rightsholders over multitudes of books would be difficult to sustain; but this is not necessarily true for a distribution cartel in respect of the same book and a manufacturing cartel over a handful of electronic reading devices with minimal differential features that separate them.

The second new revenue model is consumer subscription, which is an individualized version of the institutionally subscribed blanket license under the existing agreement. Consumer subscriptions will suit the needs of an individual who does not have access to an institutional subscription but needs to “sample” a range of books in a particular field before delving into the details of a particular book. Examples of such individuals would be potential Ph.D. students writing research proposals for their doctoral applications or a freelance writer authoring a new book pending submission to a commercial publisher. Without the consumer subscription, such individuals will choose not to buy the books at all (since they do not know which ones are useful and purchasing individual books is too costly anyway) and will resort to whatever resource that is available in a nearby public library. Introducing the consumer subscription is hence procompetitive because of its output-enhancing effect. The subscription service will also constitute a new form of collective sales arrangement, with “users pay[ing] upfront fees [for] broad access rights to options without regard to publisher,” which has gradually become the norm for newspapers, music, movies, and television. Meanwhile, the offering of a consumer subscription service is unlikely to result in anticompetitive effects. As discussed previously in the context of institutional subscription, Google’s refusal to offer tailor-made licenses at lower prices than the full-access subscription should not raise concerns of

255. Drummond Testimony, supra note 242, at 8.
256. Amended Settlement Agreement, supra note 17, § 4.7(c).
anticompetitive tying or bundled pricing. It is true that Google will have de facto exclusivity over orphan works offered as part of its consumer subscription service (similar to its institutional subscription), but as explained above, such exclusivity is necessary to preserve the incentives for business enterprises like Google to undertake risky and innovative projects in the future. The exclusivity does not entail that Google will proceed to raise consumer subscription fees to supracompetitive levels for two reasons: (1) Google’s pricing decisions will be always be constrained by the need to promote its brand and greater use of its search engine;\textsuperscript{258} and (2) the free access that individuals have to public library resources as a last resort.

The third new revenue model involves a joint venture between Google, the Registry and university copy shops whereby the copy shops will be granted access to GBS content for an annual fee per concurrent user and a fee per printed page.\textsuperscript{259} Since the mid-1990s Circuit Court decision in \textit{Princeton University Press},\textsuperscript{260} copy shops have no longer been able rely on the fair use defense under the Copyright Act to reproduce academic course packs and have since then either affiliated with established clearance services (examples being Copyright Clearance Center and University Readers) or proactively obtained copyright clearances on behalf of course instructors.\textsuperscript{261} If copy shops are now given the option to clear copyrights by accessing and copying books through the GBS system, Google will divert part of the copyright royalties (most likely thirty-seven percent by default) from the rightsholders. However, this does not necessarily raise concerns of free riding or disincentives for authorship. If the rightsholders consider sixty-three percent to be too low a percentage to compensate them for their authorship efforts—even after accounting for the possible output increase due to professors including more book excepts in course packs as they become cheaper—rightsholders are always free to request for an upward adjustment in revenue split or their books to be dropped form the GBS system altogether. On the other hand, since copy shops are spared from obtaining individual clearances for every book that goes into a course pack, there will be huge savings in transaction costs which could in turn be translated into cheaper course packs and more extensive use of books as reading

\textsuperscript{258} Elhauge, \textit{supra} note 38, at 55.
\textsuperscript{259} Amended Settlement Agreement, \textit{supra} note 17, § 4.8(b).
\textsuperscript{260} See 99 F.3d 1381, 1385–86 (6th Cir. 1996).
materials, ultimately benefiting both students (who pay a lower price) and rightsholders (who earn higher revenue due to output expansion).

Lastly, commentators are expecting Google to offer innovative services which are either complements or derivatives of the GBS project. These include four services: (1) improving search algorithms used in Google’s web-search service; (2) displaying parts of GBS books as search results; (3) developing improved automatic translation services for GBS books and web pages generally; and (4) integrating the GBS system with communication devices (including web browsers, email, and social networking tools). Google is authorized under the settlement agreement to develop these complementary or derivative services as part of its right to engage in “Non-Display Uses,” which means “uses that do not display Expression from Digital Copies of Books or Inserts to the public.”

These new or improved services are qualitative-efficiency-enhancing and courts should encourage the services as part of the GBS settlement insofar as competitors (e.g., Yahoo and Microsoft) equally have the opportunity to carry out similar research to develop competing services. Indeed, the settlement agreement does provide for the creation of a “Research Corpus” for non-consumptive and non-commercial research by qualified users. “Non-Consumptive Research” refers to “research in which computational analysis is performed on . . . Books, but not research in which a researcher . . . understand[s] the intellectual content presented within the Book,” which is precisely the type of research that Google is expecting to perform as “Non-Display Uses” of GBS books. However, the limitations imposed on the use of the Research Corpus are problematic and provide opportunities for Google to block its competitors from engaging in innovative research. First, a fine distinction is drawn between “[c]ommercial exploitation of algorithms developed when performing Non-Consumptive Research,” which is permissible, and “direct, for profit, commercial use of information extracted from Books,” which is prohibited unless the user has express consent from both Google and

262. See, e.g., Picker, supra note 128, at 394–95; Samuelson, supra note 128, at 1354; Suarez, supra note 216, at 209–13.
263. See, e.g., Picker, supra note 128, at 394–95; Samuelson, supra note 128, at 1354; Suarez, supra note 216, at 209–13.
264. Amended Settlement Agreement, supra note 17, § 1.94.
265. Id. § 7.2(d)(i), (iii).
266. Id. § 1.93.
268. Id. at 395.
269. Amended Settlement Agreement, supra note 17, § 7.2(d)(x).
the Registry.\textsuperscript{270} Ironically, it would seem that any improvement in search or translation algorithms necessarily requires "information extracted from books."\textsuperscript{271} Even more problematic is the express prohibition against "[u]se of data extracted from . . . Books . . . to provide services to the public or a third party that compete with services offered by the Rightsholder[s] . . . or Google."\textsuperscript{272} In any event, Google's competitors—the majority being "for-profit entities"—must seek consent from both Google and Registry to become "qualified users" of the Research Corpus.\textsuperscript{273}

It is submitted these restrictions on competitors' access to the Research Corpus should be removed so that Google will not be insulated from competitive pressures to innovate. Judge Hand famously remarked in the \textit{Alcoa} case "that possession of unchallenged economic power deadens initiative, discourages thrift and depresses energy; that immunity from competition is a narcotic, and rivalry is a stimulant, to industrial progress[.]."\textsuperscript{274} Admittedly, there is some degree of free riding when competitors make commercial use of the Research Corpus for Internet services which compete with Google, but the extent of free riding must be weighed against the amount of effort that competitors must put in before they can develop an innovative search or translation service based on information extracted from the GBS database. Contrast this to the decision of empowering the Registry or the UWF to license any intermediary who wishes to sell digitized orphan works in competition with Google; not only would the free-riding problem be serious, but it would also take little effort for a competitor to set up a website allowing consumers to order digital copies of orphan works under a just-in-time inventory business model (under which books are only scanned after receiving an order so that the competitor will not face the high fixed costs of digitizing every book in the world). In contrast to the above analysis, which rejects the idea of granting orphan work licenses to new entrants, there is no convincing reason to provide Google with exclusivity over the research and development of ancillary Internet services. One should note that courts should discourage free-riding only to the extent necessary to allow Google to capture sufficient returns for recouping its

\textsuperscript{270} \textit{Id}, § 7.2(d)(viii).
\textsuperscript{271} Picker, \textit{supra} note 128, at 395.
\textsuperscript{272} Amended Settlement Agreement, \textit{supra} note 17, § 7.2(d)(ix).
\textsuperscript{273} \textit{Id}, §§ 1.123, 7.2(d)(xi).
\textsuperscript{274} United States v. Aluminum Co. of Am., 148 F.2d 416, 427 (2d Cir. 1945).
upfront investment, but not the full value of Google's initial innovation.\textsuperscript{275}

Some commentators are concerned about potential tying arrangements between GBS and complementary and derivative services (e.g., web search, translation, communication tools) also offered by Google. For example, Suarez is worried that “[GBS] is tied to Google Web Search when Google Web Search includes results from books in its results pages,” because “Google could [thereby] further entrench its monopoly power over the purchase of digitized books.”\textsuperscript{276} But if GBS is the tied product, there could not be anticompetitive foreclosure in the tied product market provided that Google also displays links to competing book databases (e.g. Amazon.com, websites of physical bookstores, catalogs of university and public libraries) as part of web search results, though reasonable disputes could arise regarding the ordering of results. On the other hand, Judge Chin raised in the judgment rejecting the settlement the concern that “Google’s ability to deny competitors the ability to search orphan books would further entrench Google’s market power in the online search market.”\textsuperscript{277} If web search service is viewed as the tied product, as the Judge seems to suggest, this effectively amounts to a claim that Google should allow users to search the GBS database using the search engine or algorithm of its competitor (e.g., that of Yahoo or Bing). But an anticompetitive tie-in cannot possibly be made out because the GBS database and the search function are technologically integrated and do not constitute separate products.

Alternatively, if the tied product is translation service, we could imagine a situation where a competitor of Google makes use of the Research Corpus to develop a powerful automatic translation tool that can be used on GBS books and other Internet content. Provided that computer users can successfully install this translation program and use it to translate GBS books by clicking a web-browser button, there could be no anticompetitive foreclosure by tying. Google would only be blocking its competitors if it refuses to provide the necessary program codes and interoperability information for the development of a GBS-translation software, thereby forcing readers to use Google’s own translation tool on GBS content. On the other hand, it would be going too far to require Google to display competing translation tools on the same webpage, or web browser, in which GBS books are

\textsuperscript{276} Suarez, supra note 216, at 210.
viewed online, as competitors would then be free-riding on Google’s promotional efforts (unless competitors pay Google for advertising their translation products). In sum, while the GBS project will inevitably have spillover benefits for Google in promoting wider use of its complementary or derivative services—which courts should encourage as an add-on to the present settlement—the concern for anticompetitive tying is absent provided that competitors can still engage in the research and development of Internet search, translation, and communication products which interact with the GBS system.

V. CONCLUSION

This paper has established the analogy between the GBS settlement and the ASCAP and BMI blanket licenses in the music industry and emphasized the importance of evaluating the antitrust issues of the GBS dispute in its broader context of copyright collectives. It has argued that the LRA analysis—as a “maximizing” test—is preferred to the “satisficing” overall-efficiency test as the normative standard for applying the antitrust rule of reason in the present context, and how concerns of increasing decision error costs and chilling procompetitive behavior can be effectively addressed through doctrinal, legislative, and institutional adjustments. This paper has also developed a rule of reason framework for evaluating and balancing the anticompetitive and procompetitive effects of the ancillary restraints to the GBS settlement and copyright collectives generally. It embraces a “reverse” rule of reason analysis asking whether efficiency-enhancing modifications can be made to render the collective arrangement even more procompetitive. A substantial part of the present paper is devoted to a thorough, rule of reason analysis of the central anticompetitive concerns of the GBS settlement and certain proposed modifications suggested by Google and commentators. Perhaps surprising to many readers, it concludes that Google’s de facto exclusivity over orphan works and its pricing mechanisms for consumer purchases and institutional subscriptions are legitimate under antitrust law and should be upheld (without substitution of an LRA) by an antitrust or settlement-approval court. Indeed, this result is not immediately obvious unless and until a full fledged rule of reason evaluation is conducted in the manner suggested in this paper.