

THE GOOGLE BOOK SEARCH SETTLEMENT: A LAW AND ECONOMICS ANALYSIS

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ABSTRACT. Beginning in December 2004 Google has pursued a new project to create a book search engine (Google Book Search). The project has released a storm of controversy around the globe. While the supporters of Google Book Search conceive the project as a first reasonable step towards unlimited access to knowledge in the information age, its opponents fear profound negative effects due to an erosion of copyright law. Our law and economics analysis of the Book Search Project suggests that – from a copyright perspective – the proposed settlement may be beneficial to right holders, consumers, and Google. For instance, it may provide a solution to the still unsolved dilemma of orphan works. From a competition policy perspective, we stress the important aspect that Google’s pricing algorithm for orphan and unclaimed works effectively replicates a competitive Nash-Bertrand market outcome under post-settlement, third-party oversight.

1. INTRODUCTION

George Orwell’s metaphor of a “big brother [who] is watching you” (Orwell, 1949) appears to be no dystopia in 2011. The technological revolution ushered in by the internet and the increase of possibilities in the digital environment have facilitated a framework in which spying on the data of everyone is a real possibility anywhere and at any time. Meanwhile, to

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“google” you and me has evolved into a widespread social sport.¹ As the “googlization of everything” (Vaidhyathan, 2009) accelerates information flows, the institutional framework is set in a rapidly changing and challenging environment. Beginning in December 2004 Google has pursued a new project to create a book search engine by digitizing large numbers of books from public and university library collections and subsequently making them available and searchable worldwide via the internet. Since its inception, the Google Book Search Project² has released a storm of controversy around the globe.³ While the supporters of Google Book Search (GBS) conceive the project as a first reasonable step towards unlimited access to knowledge in the information age, its opponents fear profound negative effects due to an erosion of copyright law. The recent class action settlement will entitle Google to “make digital copies of the book collections of a number of [...] libraries” (Macqueen, 2009), inducing a significant paradigm shift in digital copyright development. Despite this imminent revolution in the history of copyright law, a comprehensive analysis from a law and economics perspective – particularly regarding the amended settlement released in November 2009 – remains rather scarce. Extending on the analysis of Lichtman (2008) and other scholars and considering the changes made within the Amended Settlement Agreement (ASA),⁴ we provide a law and economics analysis of the Book Search Settlement. First, we briefly outline the history of the Google Book Search Settlement. Section three provides an analysis of the Google Book Search Settlement from a copyright and competition policy

¹See Lehmann and Schetsche (2005) for a differentiated picture on the googlization in the information age.

²In fact, the project was first announced by Google as “Google Print” and then renamed to Google Book Search.

³See Bechthold (2010, p. 1), Na (2006, p. 418), and Kuhlen (2009, p. 568).

⁴See http://www.googlebooksettlement.com/r/view_settlement_agreement. A list of changes comparing the amended settlement to the first settlement is available at <http://www.googlebooksettlement.com/Supplemental-Notice.pdf>.

perspective. Section four gives a critical perspective on the options for analyzing the project in general. In Section five, we comment on the recent rejection of the ASA by Judge Chin. The conclusion completes the discussion, noting recent developments and suggesting ideas for further research.

2. A BRIEF HISTORY OF THE GOOGLE BOOK SEARCH SETTLEMENT

In the context of the Google Book Search project, Google has launched a process to create a search engine which facilitates searching for particular terms in published books. The project seeks to support users in locating relevant content in books and to either buy the book – implicitly satisfying the interests of publishers – or to find the identical substitute in libraries.⁵

2.1. The Google Book Search Project. The history of the Google Book Search Project is a history of two closely related programs: (1) the Partner Program, and (2) the Library Program.⁶ The former constitutes a formal contract between Google and the copyright holder to provide digital copies of (commercially) available books. In particular, Google works only with books licensed for scanning by publishers or authors and hence material which does not raise any copyright issues. Participants of the Partner Program can decide to either send their book to Google to allow for a scanning, or directly provide a full text version in a digital format. In addition, Google may offer to scan the book at a library.⁷ Consequently, Google seeks to maximize the accessibility to books, subject to the approval of the right holders. Furthermore, publishers may determine the number of pages publicly accessible. The search results Google offers its users consist of a short excerpt of

⁵On this point, see Lichtman (2008, p. 57) and Ott (2007, p. 562).

⁶Note that the differentiation between the Partner Program and the Library Program is not necessarily clear cut from the right holder's perspective. Right holders may choose to have some books in the Partner Program and others in the Library Program. Nevertheless, a distinction is reasonable as Google's approach in scanning book content differs considerably between the two programs. See ASA, Section 17.1.

⁷See Na (2006, p. 423).

the book containing the search term entered by the user, allowing the user to browse only a few sample pages. Participation of publishers and authors in the Partner Program is encouraged by appealing to the financial interests of the right holders. Integrated links to online book shops allow purchasing the book. In addition, contextual advertisements enable participants in the program to gain a new source of revenue.⁸

In the context of the Library Program, however, Google expands upon the Partner Program by “scanning books en masse from the collections of university and civic libraries” (Grimmelmann, 2009a, p. 11). This scanning and indexing of books is based on an agreement between Google and the libraries. In contrast to the Partner Program, though, Google operates on the premise of passive consent since Google evades the right holders’ explicit permission. Copyrighted books are generally not excluded from the digitization. However, right holders may opt out of the project. As a result, Google currently gives publishers and authors a choice to either participate in the Partner Program to influence the degree of access to their books or to exclude their books from the Google Book Search by choosing to opt out.⁹

In general, Google will provide access to a greater part of the book as copyright protection decreases by statute or as a consequence of an explicit permission by its right holder (Na, 2006, p. 422). Public domain books of the Library Project appear in full text version with an option to browse a book online or directly download a PDF copy. For in-copyright books, Google generally only allows access to snippets of a book containing the search term, as long as no permission from the right holder has been signaled. Finally,

⁸See Band (2006, p. 1), Na (2006, p. 423 et seq.), and Grimmelmann (2009a, p. 11).

⁹See Ott (2007, p. 563) and Na (2006, p. 424 et seq.). With the amended settlement an important update to the limitations on the right to remove or exclude one’s book has been made. Article 3.5(a)(iii) extends the removal deadline as to Google from April 5, 2011 to March 9, 2012. The removal deadline as to the libraries’ digital copies remains to be April 5, 2011. Besides, the new deadline to claim books and inserts for cash payments has been changed to March 31, 2011.

in-copyright books with permission appear in a limited preview, while the right holder himself may decide on the degree of access. An opt out signal by an author or publisher results in a complete denial of access to the book (Grimmelmann, 2009a, p. 11 et seq., and Na, 2006, p. 422).

2.2. The (Amended) Settlement. A litigation over Google Book Search was initiated by the Authors Guild¹⁰ and five publishers in fall 2005, suing Google for copyright infringement. Google reverted to the so-called “fair use” argument to legitimate their digitization project. In particular, Google argued that their limited preview on the basis of snippets of book contents was a fair and hence a non-infringing use of copyright material since the accessibility of knowledge and information was to be improved by the project. The proceedings of the litigation resulted in a class action settlement, which was announced by the Authors Guild, the Association of American Publishers, and Google Inc. on October 28, 2008.

As a reaction to the concerns brought up against the primary settlement, the parties filed an Amended Settlement Agreement (ASA) on November 13, 2009. The changes particularly have consequences regarding the international scope of the settlement. The new settlement will only include books that were either registered with the US Copyright Office or published in the U.K., Australia, or Canada up to January 5, 2009 (See ASA, Section 1.19). The most important implication of the ASA is that it addresses in-copyright books from the Library Program¹¹ and would allow Google to continue with the project. In particular, Section 2.1(a) of the settlement authorizes Google to “sell subscriptions to the Institutional Subscription Database, sell individual Books, place advertisements on Online Book Pages, and make other

¹⁰The Authors Guild represents an organization of and for publishing authors. In 2008 the Authors Guild amounted to about 8,000 members, among them authors, literacy agents, and attorneys. See <http://www.authorsguild.org> (visited 11 October 2010).

¹¹Note that (in-copyright) books from the Partner Program can not be a subject matter of copyright infringement since their provision by Google is based on explicit permissions of their right holders.

commercial uses of Books” in the United States. In this context, the agreement is of particular relevance with respect to out of print books, and so called “orphan works” for which locating of the copyright holder is virtually impossible.

Most notably, the settlement will create a new collecting society: The Book Rights Registry (BRR). The BRR will be created to mediate between Google and the right holders and to distribute revenues from the settlement. The BRR will be initially funded by Google with \$ 34.5 million (ASA, Section 2.1(c)) and be responsible to allocate \$ 45 million (ASA, Section 2.1(b)) in settlement funds for past uses of copyrighted books. Most important, however, the BRR will allow Google to continue with their scanning and indexing of in-copyright books without the explicit permission of the right holders. In exchange, 63 percent of all revenues from integrated advertisements and from individual purchases (“buy this book” link) will be redistributed to authors and publishers who have registered their copyright claims at the BRR.¹²

In addition, the ASA changed requirements for the BRR regarding the efforts to search for right holders of unclaimed works. In this regard, the settlement specifies that the BRR may use up to 25 percent of unclaimed funds earned in any one year that have remained unclaimed for five years for attempting to locate right holders.¹³ The residual of unclaimed funds is retained to the benefit of its right holders for a duration of at least ten years and should be distributed to literacy-based charities directly or indirectly benefiting the right holders and the reading public (ASA, Section 6.3(a)(i)(3)). In addition, the ASA stipulates the creation of the Unclaimed

¹²See ASA, Section 2.1(a).

¹³See ASA, Section 6.3(a)(i)(2).

Works Fiduciary¹⁴ as an independent fiduciary monitoring the use of unclaimed funds by the BRR¹⁵. Figure 1 illustrates the organization of the BRR.

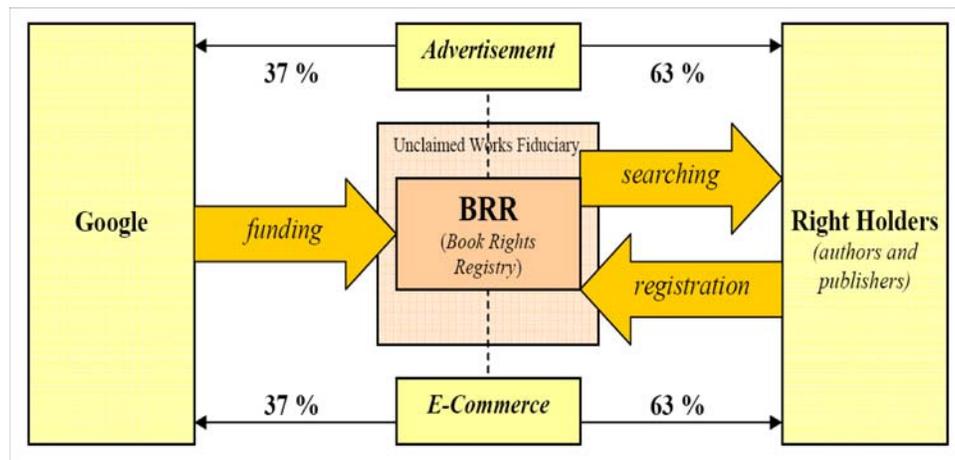


FIGURE 1. The Book Rights Registry (BRR)

The BRR will allow right holders to participate in the revenues that come from the digitization of out-of-print books or orphan works on the basis of a 63/37 split. In addition, the restriction of a redistribution of the accumulated revenues to registered right holders only may induce incentives for authors and publishers to participate instead of choosing an opt-out strategy.

3. GOOGLE BOOK SEARCH: A LAW AND ECONOMICS ANALYSIS

An approval of the aspired settlement requires an in-depth analysis of the proposed economic effects, raising issues with respect to copyright law and competition policy. Copyright as a national law raises different issues

¹⁴See ASA, Sections 1.160 and 6.2(b).

¹⁵The Unclaimed Works Fiduciary may also license “to third parties the Copyright Interests of Rightholders of unclaimed Books and Inserts to the extent permitted by law.” (ASA, Section 6.2(b)(i)). The independent character of the fiduciary is reached by prohibiting activity of any person or entity that is a published book author or book publisher. The Unclaimed Works Fiduciary “will be chosen by a supermajority vote of the Board of Directors of the Registry and will be subject to Court approval.” (ASA, Section 6.2(b)(iii)).

concerning the analysis of a possible infringement since there are differences especially between the US and European national copyright laws. Despite a possible infringement of European national copyright laws, the “*lex loci protectionis*” principle constitutes the competence of the US law from international law perspective.¹⁶ In addition, the amended settlement has narrowed the international scope with respect to US works. Thus, an examination needs to include the argument of the fair use doctrine. From a competition policy perspective, a different set of issues needs to be addressed, such as price regulation, entry barriers or the question whether the Google initiative creates a new monopoly on digital information.

3.1. A Copyright Perspective. In addition to the general catalogue of exceptions in national copyright law, the US copyright law sets forth the sweeping clause of a fair use according to 17 U.S.C. §107. In particular, the courts will be required to consider four statutory factors in the evaluation of a fair use claim, striving for a rule of reason in copyright law. A fair use analysis will have to acknowledge (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 the value of the copyrighted work. None of these four aspects, however, is decisive for the court’s decision since these factors are non-exhaustive. In fact, the court may consider the copyright user’s intention in the particular case to come to a final judgment.¹⁷

3.1.1. *Some Simple Economics of “Fair Use”.* The exceptions in copyright law in general, and the fair use doctrine in particular, follow some simple economics. While the intention of copyright protection is to create incentives for the creation of works in art, literature, and science, its enforcement

¹⁶See Ott (2007) on the competences of national copyright law on international level.

¹⁷See Ott (2007, p. 566 et seq.) and Lichtman (2008, p. 63 et seq.).

results in a fundamental dilemma, trading off the benefits and costs associated with the establishment of a property right on intellectual creations.¹⁸ In this context, three dimensions emerge from the maximization problem:¹⁹ First, the *duration* of copyright, as the number of years a copyrightable work is removed from public domain. Second, the *depth*²⁰ of copyright, which reveals the aspects of the creation that are protected by copyright. Third, the *breadth* of copyright giving advice to the practices considered as an infringement of copyright.

The idea of a fair use is assessed by the latter dimension of breadth. In this respect, the *breadth* of copyright is limited, for example, to academic use, teaching or home recording. From a welfare economics perspective, the maximization problem reveals the existence of an optimal scope of the protection provided by copyright. Landes and Posner (1989) emphasize the relevance of a minimum standard of copyright protection, where “too much” protection induces marginal costs (MC) of an extension in the scope to exceed its marginal benefits (MB). Let $W(S)$ denote the social welfare subject to the scope (S) of copyright protection, where $dW(S)/dS \geq 0$ for $S \leq S^*$ and $dW(S)/dS < 0$ for $S > S^*$, with S^* revealing the optimal scope satisfying for a maximization of the social welfare $W(S)$. Thus, in S^* , it is $dW(S)/dS = MB = MC = 0$ and hence $MB(S^*) = MC(S^*)$. Geometrically, this optimal scope is displayed by the horizontal tangent to

¹⁸The general literature on the economic analysis of intellectual property rights emphasizes the social costs (i.e. dead weight loss) coinciding with the creation of a monopolistic market structure by granting an exclusive right to the creator. In addition, the exclusive character of the use will increase the costs for cumulative innovations, revealing a trade off between static and dynamic efficiency. See Müller-Langer and Scheufen (2011) on this point.

¹⁹See Watt (2004, p. 157), Landes and Posner (1989, p. 347 et seq), and Müller-Langer and Scheufen (2011).

²⁰In this respect copyright differs from patents in so far as copyright does not protect ideas but only expressions.

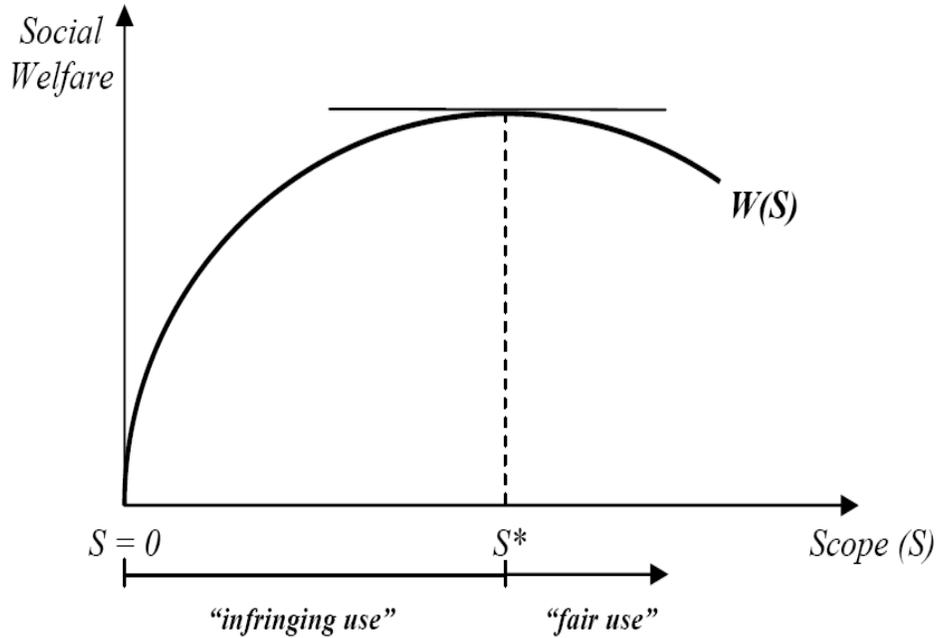


FIGURE 2. Optimal Scope of Copyright and Fair Use

$W(S)$ in Figure 2, leaving us with a maximum in S^* , where $dW(S)/dS = 0$ since $W(S)$ exhibits an inverted u -shape.²¹

Apparently, there will be an optimal scope of copyright since the social welfare is not strictly increasing in S . Consequently, a use will be expected to involve an infringement of copyright as long as a protection of this use comes along with a positive net gain in social welfare. In contrast, the scope is not broadened to uses to the right of S^* because an extension would cause social welfare from copyright to decrease. A “fair use” analysis will then have to balance the costs and benefits following the economics of this simple model. This leaves us with the four stated factors to assess whether the Library Program is justified by fair use or whether it involves an infringement of copyright law.

²¹Note that the graphic as well as the technical arguments break things down to an ideal type of the relationship between scope and economic returns.

3.1.2. *A “Fair Use” Analysis.* An investigation of the first factor of the fair use doctrine – purpose and character of the use – raises two important issues to be evaluated. First, one must determine whether the use is commercially driven. The economic intuition behind this aspect is the following: Information goods exhibit the characteristics of a public good causing a market failure in terms of an incentive to free ride on the sunk costs of the creator of the copyrighted work.²² Thus, as a commercial use generates profits from the exploitation of the property right, the original author and the copyright holder should be compensated for his creative efforts. The fact that Google now generates revenues from the Library Program²³ by licensing its collections to Sony for their e-book reader advances its potential for commercial application.²⁴ Consequently, a lone option for future net returns²⁵ already allows for the judgment of a commercial use with respect to the Google Book Search Settlement. Nevertheless, a commercial use in and of itself does not refute a fair use argument.

Second and even more important is the aspect of a transformative use. The transformative nature of a use touches on the closeness and purpose of the use compared to the original work. In this respect, the transformation of an original work requires reasonable efforts to augment the nature or functionality of a work such as parody, while a mere change of the medium of a copyright protected work is not sufficient to infer a transformative nature of the use.²⁶ A transformation of the original work then may legitimate a fair

²²See Müller-Langer and Scheufen (2011) on the free riding problem with respect to information goods.

²³Note that the Partner Program is not subject matter of the settlement since Google seeks to obtain explicit permission of the right holder by signing a formal contract with the publisher of the copyrighted work.

²⁴Garon (2010, p. 12). In particular, see <http://thepublicindex.org/docs/letters/sony.pdf>.

²⁵The option of future net returns is obviously closely related to the question whether Google is able to gain a certain degree of market power (See section 3.2.2.). Notably, the ability for cost recovery eventually reveals a crucial incentive constraint for entering the market in the first place.

²⁶See Lichtman (2008, p. 65), Na (2006, pp. 437 et seq.), and Proskine (2006, p. 227).

use due to two reasons: First, as the transformed work is considered different to the original, it is less likely to infringe the property right of the original author and to reduce sales of the original work. Original and transformed works may serve two different markets. Second, as the process of transformation adds a new purpose to the original work, a transformative use may create additional social benefits.²⁷ Thus, the question is whether the digitization of books adds new purposes to the original works. A broadening of the scope of copyright protection beyond transformative uses would prevent the internalization of additional social surplus. Recalling the rationale of the simple economic model in Figure 2, this first factor seeks a balancing of the benefits and costs on the individual (the author) as well as on the social planer level (social welfare). That is, as long as Google's use would satisfy the criterion of serving a new market ("meaningfully distinct") and adding social surplus ("new purpose"), Google's use could satisfy as to be to the right of S^* in Figure 2. Thus, we could conceive of a scenario where the nature of a transformative use countervails its commercial character. Google's purpose in digitizing books is to create the ability and the innovative tool to search and retrieve snippets and hence to help in locating information. In addition, by digitizing a significant portion of out-of-print works, Google helps to make existing knowledge accessible and searchable; whereas, at present, a significant portion of books are withdrawn from public access.²⁸ Consequently, the Google Book Search Project eventually satisfies both issues of a transformative nature of use: Google creates a product that is meaningfully distinct from the original work, and hence is not likely

²⁷An important case and possible bargaining chip for Google's argumentation in this context, is *Kelly v. Arriba*. See <http://www.linksandlaw.com/decisions-106.htm> (visited 16 September 2010). The Court of Appeal for the 9th Circuit found in a fundamental judgment the creation of thumbnails by the search engine Arriba to be legally admissible. The court argued that Arriba's thumbnail images served the transformative purpose since it improved access to information and did not just portray Kelly's original full-size images (Ott, 2007, p. 566). A more recent case is *Field v. Google* (see Na, 2006).

²⁸See Ott (2007, p. 567), Lichtman (2008, pp. 65 et seq.), and Proskine (2006, p. 227).

to harm the right holder since a displaying of snippets of a book does not substitute a purchased full-text version.²⁹

In this respect, Section 7.2(b)(iv) of the ASA explicitly stresses that “the [finding] tools and generated information will not permit users to read or view any material from the LDC³⁰ [...], except that such users may read or view Front Matter Display and, in response to a search request, a limited number of Snippets for the purpose of enabling the user to verify which Book has been identified”. The project generates additional social welfare as it adds a new functionality to the protected works. Users will be able to locate particular books and book contents containing the search term and hence supporting decision-making according to the user’s interest. Google’s search engine may assist in the matching of demand and supply, and hence increase book revenues. Therefore, the project appears to exhibit a highly transformative use, countervailing its commercial character.

The nature of the copyrighted work is related to the issue of the creativity of a work. Since the general intention of copyright is to reward creativity and innovation, works exhibiting greater creativity “are closer to the core of intended copyright protection” (Campbell, 1994, p. 586) than those exhibiting less creativity.³¹ As a result, a fair use is required to distinguish between highly creative works like fictional novels and less creative works like biographies.³²

²⁹Hausman and Sidak (2009) argue that Google’s platform for accessing books eventually introduces an extraordinary new product. In particular, they argue that the ability to make all books around the world searchable and accessible will facilitate research and hence the creation of subsequent works.

³⁰LDC means “Library Digital Copy”. See ASA, Section 1.81.

³¹See also Lichtman (2008, p. 65).

³²Note that copyright only protects the expression of facts, but not the facts themselves (Na, 2006, p. 441). A biography, chronologically reflecting the facts of a person’s life, is of less creativity as a purely fictional novel that arises from its author’s creative ability.

Another aspect with regard to the nature of the copyrighted work is the availability of an original work to the public. A distinction between commercially available (in-print) and commercially unavailable (out-of-print) works is frequently applied by the courts. As Google's Library Project scans entire library collections, it does not distinguish according to a work's level of creativity.³³ In addition, commercially available books are not generally excluded from digitization. Thus, along both dimensions, Google may eventually infringe copyright law unless its Library Program is justified by fair use. However, the fact that Google's focus is on digitizing particularly out-of-print works may justify a fair use. In addition, Google chooses the Display or No-Display classification³⁴ subject of whether or not a book is determined as being in-print or out-of-print. In this context, the ASA has changed the basis for this determination. Following Section 3.2(d)(i) of the ASA, Google "shall use commercially reasonable efforts to determine whether a book is Commercially available or is not Commercially Available using a methodology reasonably agreed to by Google and the Registry."³⁵ Notably, the Library Program appears to predominantly involve non-fictional works as Google primarily scans books from university libraries. Thus, the content to be digitized should be labeled factual material, i.e. non-fictional works, as opposed to creative fictional works (Varian, 2006a, p. 9). In total, the court may weigh this factor, at most, slightly against Google.³⁶

³³However, attachment F of the ASA provides a list of fictional genres – in particular anthologies, poetry collections and short stories – where No Preview (ASA, Section 1.92 and Section 4.3(b)(ii)) is granted. Furthermore, "for Fiction, Google will block the final five percent (5%) of the Book's pages (or a minimum of the final fifteen (15) pages in the book." (ASA, Section 4.3(b)(i)(1)). This second aspect especially provides Google with a bargaining chip for the third factor of the fair use analysis.

³⁴See ASA, Section 3.2.

³⁵In particular, Google "will use third-party databases from a range of United States, Canadian, United Kingdom, and Australian sources that can be obtained on fair and commercially reasonable terms." (ASA, Section 3.2(d)(i)).

³⁶See Na (2006, pp. 441 et seq.), Ott (2007, p. 568), and Lichtman (2008, pp. 66 et seq.).

However, changes made in the ASA may even shift this issue towards a more neutral assessment of factor two in the fair use analysis. In terms of the amount and substantiality of the portion used, two aspects seem relevant: First, the degree to which a work has been copied (i.e. the number of pages), and second, the relevance of the copied fraction in relation to the complete work. As a general rule and proxy, one can say that the greater the amount of copied material, the less likely is a possible justification by fair use. Nonetheless, copying a complete work does not preclude fair use nor does a decrease in the degree of copied material automatically make a fair use more likely (Lichtman, 2008, p. 67). In this context, for instance, the copied excerpts may be of most interest to the reader (e.g. the last chapter of a novel).

As far as the Library Project is concerned, Google needs to digitize the book content entirely to make the information searchable.³⁷ Hence, the fraction copied is 100 percent. Nevertheless, Google's search engine will only display snippets containing the search term. The user will only receive a first impression that establishes the basis for the user's decision in acquiring the searched information.³⁸ In addition, the settlement contains a "20-Percent-Rule" for the Standard Preview. That is, Google may display up to 20 percent of a book but limited to an amount of five adjacent pages at a time.³⁹ For works of fiction, Google blocks the final five percent of each book or a minimum of at least fifteen pages. This aspect seems particularly relevant for novels as the conclusion of a book is typically of highest interests to the reader. Consequently, the third factor might be considered as rather neutral in justifying a fair use by the ASA.

³⁷See Ott (2007, p. 568), Lichtman (2008, p. 67), and Travis (2009, p. 129).

³⁸See ASA, Section 7.2(b)(iv).

³⁹See ASA, Section 4.3(b)(i)(1).

The fourth factor explicitly listed in 17 U.S.C. §107 addresses the expected effect of the use upon the potential market. The intention underlying this consideration is that the new (transformed) product should not narrow the (potential) market of the right holder (Ott, 2007, p. 568). The court will have to consider the effects of the transformed product on the value of the protected work since copyright intends to create a value for creative works through providing incentives for their provision by granting an exclusive right to the creator. As far as the potential market is concerned, the court will as well consider potential effects on the market for derivative works (Hanratty, 2005). Accordingly, the fourth factor is closely connected to the question of a transformative use since a meaningfully distinct transformed product is less likely to harm the right holder and hence to lower the market value. In the case of Google, the snippets are not likely to substitute the original work and therefore are not likely to present a meaningful threat to the value of existing works. Nevertheless, critics fear the threat that the digitized copies can leak out because Google does not store the snippets but the full text version of each book in their databases.⁴⁰ Computer hackers could eventually see Google's security precautions as a challenge to hack the database, inducing a severe threat to the exclusive rights of authors.⁴¹

Despite the potential risks, one can argue that the Library Program may even facilitate a potential increase in the market value of existing and derivative works since the "buy the full text version" link is likely to accelerate book sales and access to information. Whether this issue weighs in favor of Google or the plaintiffs will depend on the court's definition of the existing

⁴⁰See Samuelson (2010b, p. 1368), Band (2006, p. 10), and Lichtman (2008, p. 69).

⁴¹See Ott (2007, p. 568) on this point. This critique does not necessarily account for Google's attempts only. The technological development in general has set the institutional framework in this rapidly changing and challenging environment. Everyone equipped with a scanner may be able to impose a threat to the exclusive rights of authors and publishers.

and potential market and if the redistribution of cash flows by the BRR allows for a compensation of the potential risks of hacked databases.⁴²

A balancing of the pros and cons to factor four may, at the most, result in a slightly negative judgment towards Google’s use. To sum up, the application of the four statutory factors explicitly listed in 17 U.S.C. §107 – used to clarify whether Google’s use is to the left or to the right of S^* in Figure 2 – shows that there will be no uniform conclusion. In particular, the court will have to balance the benefits and costs of a possible fair use judgment.⁴³

Table 1 summarizes the conclusions drawn from each factor of the “fair-use” analysis.

TABLE 1: A “Fair Use” Analysis of the Google Book Search Settlement

Statutory Factors of a “Fair Use” Analysis		Assessment
1	The purpose and character of the use	(+)*
2	The nature of the copyrighted works	(0/–)**
3	The amount and substantiality of the portion used	(0)
4	The effect of the use upon the potential market for or value of the copyrighted work	(0/–)

* Note that the positive effects of a transformative use may counterveil the commercial character of the use

** The Ammended Settlement Agreement may forward a rather neutral assessment of factor 2

The final judgment on the fair or unfair use of copyrighted works by Google will be a matter of how one weighs the arguments against each other. While the purpose and character of the use may weigh the court’s

⁴²See Ott (2007, p. 568), Na (2006, pp. 443 et seq.), and Lichtman (2008, pp. 67 et seq.).

⁴³Note that in *Harper & Row. v. Nation Enterprises* the US Supreme Court highlighted the fourth factor as the “single most important element of [the] fair use” analysis ((Cf. Harper & Row v. Nation Enterprises, 471 U.S. 539 (1985)). However, in *Campbell v. Acuff-Rose Music, Inc.* the Supreme Court more recently argued that “the four statutory factors are to be explored, and the results weighed together”, revealing the need to balance all pros and cons of a possible fair use argumentation (Cf. Campbell, aka Skyywalker et al. v. Acuff-Rose Music, Inc., 510 U.S. 569 (1994)).

judgment rather in favor of Google (+), the assessment of the factors two and four may, at most, be slightly against (-) or even neutral (o) towards the fair use argument. However, the ASA may shift the judgment more in favor of Google's fair use argumentation.

3.1.3. *Additional Considerations.* Despite the equal relevance of all four factors explicitly listed in 17 U.S.C. §107, the list is not exhaustive. That is, the court may consider additional aspects that are decisive in the particular case to come to a final conclusion upon the question whether the Library Program within the amended Google Book Search Settlement constitutes a fair use of copyright protected works.

From an economist's perspective, at least three additional aspects may be considered. First, the project benefits the right holders of the digitized works since an integration of a "Buy this book" link will likely accelerate book sales and hence authors' revenues by an increase in the demand for their works (Lichtman, 2008, p. 72; Band, 2006, p. 12). In addition, Google makes books searchable and creates a basis for potential buyers to seek information as to whether a book is of interest for them. The success of Amazon's "Look Inside" functionality, with an increase of sales by 15 percent, (Varian, 2006a, p. 6) may even support this hypothesis. In contrast to Amazon, however, Google offers the additional opportunity to find a book of interest, subject to a search term that is typed in by the user. Thus, a user will not have to know whether a book is of interest beforehand. The Google Project may then be of particular relevance for books that serve a niche market since the opportunities of a search engine may create an initial signal to a potential consumer (Lichtman, 2008, p. 71). Regarding the great amount of "out-of-print" and orphan works, Google's search engine will initially create a new market and hence expectations to gain revenues for their authors. Consequently, the project will help to lower information

costs on the demand side and likely increase book sales. In this respect, it is important to note that many publishers and authors participate in the Partner Program. This gives the impression that providing partial access to their books via the internet has a positive effect on sales. There is no reason to believe that this does not apply to the right holders in the Library Program.

Second, the opt-out opportunity for copyright holders not interested in participating in the project is efficient from a transaction cost perspective.⁴⁴ Regarding an opt-in model, the parties involved would face high costs for finding each other in a first step and then negotiating a contract face-to-face in a second step. The former cost type is particularly relevant for the large number of orphan works involved in the project. George (2002) emphasizes the problems associated with the process of finding and allocating right holders of orphan works. From this perspective, the resolute approach to opt books out instead of opting them in may as well be a low-cost way of forcing an allocation of the right holders to their works.⁴⁵

Third, Google's recent move via the ASA to extend the responsibilities for the BRR and to create the Unclaimed Works Fiduciary has added one important issue. The BRR establishes a public database of right holders in claimed books and actively takes efforts to search for right holders of orphan works.⁴⁶ The number of orphan works will, therefore, likely decrease in the future. The function of the Unclaimed Works Fiduciary should be seen in its independent character to oversee the license fees that are collected by the BRR. The ASA seeks to provide a credible commitment regarding

⁴⁴Varian (2006b) argues that an opt-in solution would not be feasible in the context of orphan works. He argues that, from the perspective of transaction cost economics, the question should not be who is able to identify the right holders of orphan works, but who exhibits the lowest identification costs. See also Gordon (1982, pp. 1618 et seq.) on market failure associated with prohibitive transaction costs of licensing copyrighted works as a justification for the fair use doctrine.

⁴⁵This argument seems to be particularly true as the BRR creates incentives for registry.

⁴⁶See ASA, Sections 6.1(c) and 6.3(a)(i).

Google’s use of unclaimed funds to actively locate right holders and distribute unclaimed funds to literacy-based charities.⁴⁷ In conclusion, our analysis promotes the opinion that – from a copyright perspective – the settlement between the Authors Guild, the Association of American Publishers, and Google may be met with approval as it appears to be beneficial to all parties involved – the consumers, the right holders (authors and publishers), and Google. Google’s response to emerging concerns by filing an amended version of the settlement may eventually even strengthen a fair use argumentation. Last but not least, the Google Book Search Project may provide a solution to the unsolved dilemma of orphan works – a problem that Congress has repeatedly tried but failed to address in the history of legislative efforts (Ji, 2010, p. 34).

3.2. A Competition Policy Perspective. The Google Book Search Settlement not only raises concerns from copyright perspective. Recently, Picker (2009) and Grimmelmann (2009a, 2009b) have promoted a discussion as to whether the class action settlement poses an antitrust threat that should be an issue of a close investigation. In particular, some concern has arisen that the settlement could facilitate a setting of an orphan works monopoly and could pose an antitrust threat by the creation of the BRR as a cartel of authors and publishers.

3.2.1. Class Action and Cartelization. Particularly the creation of the BRR – as a new collecting society and intermediary between Google and the right holders – has raised antitrust concerns. Several scholars have claimed that the BRR may eventually help to leverage Google’s market dominance for

⁴⁷In particular, Section 6.3(a)(i)(2) constitutes that the BRR may use up to 25 percent of unclaimed funds after five years to locate right holders of orphan works. Beginning ten years after the effective date, unclaimed funds “should be distributed to literacy-based charities in each such country that directly or indirectly benefit the Rightsholders and the reading public.” (ASA, Section 6.3(a)(i)(3)).

search engines to the market of digital books by creating an exclusive joint venture between Google and right holders.

In September 2009, the online bookseller Amazon filed a formal objection claiming that the BRR was likely to induce a cartel of authors and publishers with a potential to raise book prices and reduce output.⁴⁸ Amazon argued that the creation of the BRR would be detrimental to consumers and future right holders, who would have to compete with the predominant cartel members.⁴⁹

Grimmelmann (2009a) argues that the settlement will create a centralized collecting society which exhibits a substantial power to negotiate on behalf of the class of right holders. That is, the BRR will create the baseline for collective action and have a broad discretion to even work out a pricing algorithm for dividing the revenues from integrated advertisements and e-commerce activities. Furthermore, the BRR will be empowered to negotiate the terms and conditions of potential new revenue models, such as file downloads (limited to books that are not commercially available), print-on-demand and consumer subscription.⁵⁰ Note, however, that at launch Google is likely to only use institutional subscriptions and consumer purchase models (Fraser, 2010, p. 7). Picker (2009) takes such apprehension to the extreme as he views Google as an agent acting on behalf of right holders that has the power to set the prices for online access to consumers and hence to engage in price discriminating practices. He also raises concerns that both active individual right holders as well as the BRR would

⁴⁸*Amazon.com* Objection to Proposed Settlement, *Authors Guild, Inc. vs. Google Inc.*, S.D.N.Y. Case No.05 CV 8136-DC, on pp. 18 et seq. (1 September 2009).

⁴⁹*Amazon.com* Objection to Proposed Settlement, pp. 15 et seq. See also <http://www.istockanalyst.com/article/viewarticle/articleid/3457080> (last visited 16 September 2010). However, U.S. District Judge Denny Chin rejected Amazon's objection.

⁵⁰ASA, Section 4.7. See also Grimmelmann (2009a, p. 13), Wang (2010, p. 3), and Picker (2009, p. 390).

have little incentives to grant Google's rivals licenses of claimed and orphan works (Picker, 2009, p. 408).

Nevertheless, it is important to note that right holders and the BRR as upstream suppliers would have incentives to license a Google rival if it charges a lower distribution markup than Google and distributes the work more efficiently (Elhauge, 2010, p. 12). Furthermore, the ASA prescribes that the BRR shall, at the request of right holders, facilitate the distribution of works through alternative licenses for consumer purchase such as the Creative Commons license.⁵¹

As for orphan works, the Google Books Search service "will create all value above the value that consumers derive from having physical access to orphan books" (Hausman and Sidak, 2009, p. 423). This is likely to lead to an increase in consumer welfare in this regard. Besides, Google creates the institutional subscription, which is to be set at competitive market rates under the amended settlement. It will allow institutions to view all books included in the subscription upon the permission of the right holders and all thus far commercially unavailable books that have been made available for purchase under the amended settlement (Elhauge, 2010, p. 6). Thereby, Google would add a new market option, which potentially increases consumer welfare.

Against this background, a closer investigation of the ASA and, in particular, of the design of the BRR and the Unclaimed Works Fiduciary may weaken some of the antitrust concerns. First, the establishment of the BRR can be seen as an essential step in saving transaction costs from otherwise one-to-one negotiations and in permitting more transactions to occur as it establishes a public database of right holders in claimed books and finances a search for right holders of orphan works (Elhauge, 2010, pp. 4 et seq.).

⁵¹See ASA, Sections 1.44 and 4.2(a)(i).

It thus makes identification of right holders of in-copyright books and the licensing of orphan works easier (Besen, Kirby and Salop, 1992, pp. 383 et seq. and Fraser, 2010, p. 6). It is also likely to decrease the number of orphan works in the future by gathering and providing precise information about right holders (Hausman and Sidak, 2009, p. 433). Also, the amended settlement requires the independent Unclaimed Works Fiduciary to oversee the license fees collected for unclaimed works, to use up to 25 percent of unclaimed funds to locate right holders, and to distribute unclaimed funds held at least 10 years to literacy-based charities.⁵² In this light, it is recommended that the court conditions the acceptance of the ASA subject to the work of the BRR and the Unclaimed Works Fiduciary “to set standards designed to further reduce the volume of unclaimed works”.⁵³ Nevertheless, by acting on behalf of all right holders, the BRR eventually establishes an institutional framework that may facilitate a coordination of authors’ and publishers’ interests. A deeper analysis hence raises questions regarding the conditions and determinants for cartel stability.

In this context, the Horizontal Merger Guidelines – provided by the U.S. Department of Justice and the Federal Trade Commission – may provide a good guide for our analysis.⁵⁴ (19 August 2010). Three crucial conditions abound that facilitate a successful coordinated interaction: First, an agreement that reaches terms of coordination that are profitable to the firms, preventing the cartel members from defection. Second, a mechanism or conditions that allow for a detection of deviant behavior of a member. Third, an

⁵²See ASA, Sections 6.1(c) and 6.3(a)(i).

⁵³Cf. United States of America Regarding Proposed Amended Settlement Agreement, *The Author’s Guild, et. al. v. Google Inc.*, No. 05-CV-8136 (S.D.N.Y. 4 February 2010), p. 24.

⁵⁴Federal Trade Commission, Horizontal Merger Guidelines

effective sanctioning mechanism which makes it more profitable to cooperate than to pursue short-term profits from deviation.⁵⁵

In addition, several determinants and market conditions may help to assess the proposed effects on cartel stability, i.e. the number of firms in the market, the heterogeneity of products, etc.⁵⁶ As a general rule, the smaller the number of market actors and the more homogeneous their products, the easier it is to coordinate the terms and parameters agreed on (Motta, 2004, pp. 142 et seq.). It has been argued that the BRR eventually provides an institutional framework for an agreement on the terms that are subject to a registration (Picker, 2009). Besides, by giving each right holder the right to opt out, they are eventually provided with the opportunity to choose the exit option. However, especially for the great number of commercially unavailable works, this option may not be profitable to firms since it is the “googlization” that actually establishes a market for these books in the first place. The possible threat of an alleged cartel member choosing the exit option may, therefore, lack credibility. Furthermore, this option is by definition irrelevant in the case of unclaimed works for which right holders remain unknown. However, for orphan works and works whose right holders choose not to set a price, the ASA requires Google to use a pricing algorithm that replicates a competitive Nash-Bertrand market outcome.⁵⁷ As this pricing algorithm is subject to inspection, a coordinated increase in prices of such works may not be feasible. Weighing these arguments, one may assert that the first condition to facilitate a successful coordinated interaction may only be satisfied for claimed, commercially unavailable works and works whose

⁵⁵Motta (2004), p. 139. Also, U.S. Department of Justice and Federal Trade Commission, Horizontal Merger Guidelines (19 August, 2010), pp. 24 et seq..

⁵⁶Other determinants to assess whether a cartel is likely to result in a stable coordination equilibrium are, for instance, market entry barriers, the frequency of interaction, market transparency and demand characteristics (Van den Bergh and Camesasca, 2006, pp. 368 et seq.).

⁵⁷We will analyze this aspect in more detail in section 3.2.2.

right holders explicitly choose to set a price. However, both latter conditions are hardly satisfied for the following reasons. First, the number of books covered by the settlement – and hence the group of right holders that would have to be coordinated – is extremely large, making it difficult to detect deviant behavior of a member (Wang, 2010, p. 4). Second, right holders of claimed commercially available in-copyright books are free to set their own prices for sale through Google or can sell their books through Google’s rivals. This will make it difficult for the BRR to control prices (Elhauge, 2010, pp. 3 et seq. and Wang, 2010, p. 4). Third, the book market is very heterogeneous. A novel is by its very nature a singular good. One novel will be no perfect substitute for another novel. This holds even more with respect to different genres of books. As a result, the ability of right holders to reach a stable cooperative equilibrium and to coordinate an increase in book prices may be limited (Wang, 2010, p. 4). Nevertheless, as the BRR negotiates on behalf of the whole class of registered right holders, awareness with respect to the composition of the BRR is strongly required.⁵⁸ In particular, owners of unregistered copyrights as well as potential future copyright holders are excluded from the settlement. That is, not all interests of the total class of authors and publishers are represented by the BRR. The most immediate danger from this is that the BRR may negotiate terms at the expense of unregistered right holders. It is, however, important to note that the ASA requires the Unclaimed Works Fiduciary to independently represent the interests of right holders regarding the exploitation of unclaimed

⁵⁸This follows from the nature of the legal concept of a class action. A class action allows that questions of law – which might be relevant for a class of different claimants – are decided on uniformly and binding to all members of this class. A class action meanwhile constitutes a special legal concept in US law. However, the question as to whether or not the settlement is beyond the court’s authority is beyond the scope of this paper. See Department of Justice (2010, p. 2), which states that the ASA “is an attempt to use the class action mechanism to implement forward-looking business arrangements that go far beyond the dispute before the Court in this litigation.”

works.⁵⁹ Finally, Grimmelmann (2009a) claims that the BRR should be required to represent any copyright holder. In addition, it should be ensured that non-plaintiff and future copyright holders receive contracts at the very same (or better) conditions (Grimmelmann, 2009a, pp. 13 et seq.).

3.2.2. *Market Power, Barriers to Entry, Pricing, and Access to Knowledge.*

In addition to the antitrust concerns regarding the BRR, some scholars as well as the Department of Justice fear a monopolization of the digital book market by Google.⁶⁰ They argue that, with respect to the large number of orphan works, the settlement will provide Google with an exclusive right and considerable freedom to set prices⁶¹ as well as terms for all commercial services involved in the Book Search Project.

However, the simple fact that Google is the first to enter a new market does not necessarily mean that Google will reach a monopoly position. In competition law, a monopolistic position poses a severe threat to competition where there are significant barriers to entry. As a result, the analysis focuses on the question whether the settlement helps to establish such barriers to entry. Critics in this respect have seen the so-called “Most Favored Nations” (MFN) clause as the most pressing problem of the settlement agreement (Picker, 2009, pp. 400 et seq. and Grimmelmann, 2009a, p. 15). This clause could have guaranteed Google that none of its competitors could gain a competitive advantage within ten years of the settlement’s effective date, which could have resulted in less incentives to enter the market (Ji, 2010, p. 15). The settlement could eventually have deterred market entry of potential competitors such as Yahoo!, Microsoft, or Amazon. However, the ASA has eliminated the MFN clause. More specifically, seeing as the ASA

⁵⁹See ASA, Section 6.2(b)(iii).

⁶⁰In particular, see Samuelson (2010a), Grimmelmann (2009a), Fraser (2010), and Department of Justice (2009).

⁶¹Grimmelmann (2009a) emphasizes the threat of price discriminating practices on consumer surplus.

is non-exclusive,⁶² the BRR could produce a licensing deal with Google's rivals on better terms than Google gets. Furthermore, Google's rivals may license claimed books from the BRR and unclaimed books from the Unclaimed Works Fiduciary⁶³ "to the extent permitted by law".⁶⁴ In contrast to Google, which bears the costs of scanning profitable as well as unprofitable books and the settlement cost, a follow-on competitor could make a deal with the BRR and license only commercially profitable books for digital use without bearing the cost of digitizing books and the settlement cost. A Google rival may, therefore, free ride on Google's upfront investment in the digitization of books. In the long-run, books digitized by Google that are currently copyright protected will go out of copyright and will then be fully available to Google's rivals without incurring cost of digitization. Google's rivals may also benefit from a facilitated determination of the value of digital books as the amended settlement may help to reveal the right holders' sales volumes and thus the extent of buyer demand (Elhauge, 2010, p. 2). As the BRR will use settlement funds to attempt to locate right holders of orphan works, Google's rivals may also benefit from lower search costs.⁶⁵ It is, therefore, harder to accuse Google of possessing market power by establishing barriers to entry (Elhauge, 2010, pp. 7 et seq.). The establishment of the BRR and the Unclaimed Works Fiduciary as required in the ASA may even result in lower barriers to entry for Google's rivals, for instance, by lowering digitization cost barriers and costs of identifying out-of-copyright works and valuing digital books (Elhauge, 2010, pp. 9 et seq.). Furthermore, Google already offers out-of-copyright books to users of the Apple's iPhone, Sony's Reader, and the Android mobile (Fraser, 2010, p. 8).

⁶²See ASA, Sections 2.4 and 3.1(a).

⁶³See ASA, Section 6.2(b)(iii).

⁶⁴See ASA, Section 6.2(b)(i). See Elhauge (2010), p. 5.

⁶⁵See ASA, Section 6.1(c).

However, it could be asked whether the Google Book Search service has the characteristics of a natural monopoly. The digital book market can be characterized by means of a large fixed cost for the creation of a database of digital books, high economies of scale and positive network effects.⁶⁶ Google, as a first mover in the digital book market, has already laid out significant irreversible upfront investments in digitizing books and negotiating the settlement. The marginal costs of providing its service, however, are likely to approximate zero once the settlement is approved. Furthermore, it can be argued that Google alone has the resources to create a database for digital books on a massive scale (Darnton, 2009). As such, the picture of a natural monopoly could be drawn from an economic perspective. The database may be considered as an essential facility that is necessary for all participants to operate in the digital books industry (Motta, 2004, p. 66). It may be reasonable to have a monopoly on digital databases and be even socially desirable to avoid additional social costs for the provision of the very same good. Hence, one could make the case for having only one supplier of such a database if the saved costs of duplication associated with the absence of a competing database more than outweigh the value of competition associated with an additional database. This, however, is more likely to be the case if the pricing algorithm for settlement controlled prices successfully mimics the outcome under competition as the additional procompetitive effect associated with a second database would be lower in this case.

In addition, it might be better to have only one supplier – realizing the social benefits of such a search engine – than having none. Nevertheless,

⁶⁶See Grimmelmann (2009a), p. 14 and Picker (2009), pp. 400 et seq.. For instance, positive network effects may arise as right holders of unclaimed works are more inclined to register when there are more users of the Google Books database. Also, right holders of claimed works may be less inclined to opt-out when more individuals use the Google Books database. Furthermore, more individuals may use it as soon as more books are available for search and purchase, which is the case when more right holders register their works.

consciousness of Google’s resulting market position is strongly needed. In this respect, the essential facilities doctrine⁶⁷ and particularly the decision of the Seventh Circuit Court of Appeals in *MCI v. AT&T* may provide a valid guide for our analysis.⁶⁸ The Court stated that there were “four elements necessary to establish liability under the essential facilities doctrine: (1) control of the essential facility by a monopolist; (2) a competitor’s inability to practically or reasonably duplicate the essential facility; (3) the denial of the use of the facility to a competitor; and (4) the feasibility of providing the facility.”⁶⁹ The U.S. Supreme Court’s ruling in the case of *Verizon v. Trinko* added another condition: (5) a court must prove absence of regulatory oversight with the power to compel access.⁷⁰

As for the first condition, Google arguably is a monopolist in the digital books market and to a significant degree – indirectly via the BRR – in control of the database (Samuelson, 2010a; Grimmelmann, 2009a; Fraser, 2010). Condition (1) might therefore be satisfied.

As for the second condition, if it is reasonable for competitors such as Amazon, Yahoo! or Microsoft to create their own databases, then there is no monopolization. One may argue that it is practically possible for competitors to create their own database by negotiating with single right holders.⁷¹ Prohibitively high transactions cost of one-to-one negotiations with hundreds of thousands of right holders may deter rivals to create a comparable database. The second condition might therefore also be satisfied because

⁶⁷See Viscusi, Harrington and Vernon (2005, pp. 323 et seq.). For a critique of the essential facilities doctrine, see Areeda and Hovenkamp (2008, §7.06 b). The question, however, as to whether the essential facilities doctrine should generally be abandoned – as several commentators have argued – is beyond the scope of this paper.

⁶⁸*MCI Communications Co. v. AT&T*, 708 F.2d 1081 (7th Cir. 1982).

⁶⁹*MCI Communications Co. v. AT&T*, 708 F.2d 1081 (7th Cir. 1982), at 1132-33. See Pitofsky, Patterson and Hooks (2002, pp. 448 et seq.).

⁷⁰See *Verizon Communications v. Law Offices of Curtis V. Trinko, LLP*, 540 U.S. 398 (2004).

⁷¹Alternatively, Google’s rivals may digitize books without right holders’ permission in the hope that a similar class action lawsuit may be settled on terms comparable to the ASA. However, Department of Justice (2010, p. 21), states that this suggestion “is poor public policy and not something the antitrust laws require a competitor to do.”

the creation of a competing database would be prohibitively expensive when rivals are forced to negotiate with right holders on a one-to-one basis.

The third condition would require Google to deny the commercial usage of the database to rivals such as Amazon, Microsoft or Yahoo!. As mentioned earlier, Google's rivals may license claimed books from the BRR and unclaimed books from the Unclaimed Works Fiduciary to the extent permitted by law. Provided that Google's rivals can use the database through licensing agreements with the BRR, condition (3) is hardly satisfied.

Consider now the fourth condition. Arguably, it is technically feasible for Google to provide rivals with access to the database. Also, sharing the database is not likely to inhibit Google from serving its customers adequately (Pitofsky, Patterson and Hooks, 2002, p. 450). But are there legitimate business rationales for Google to refuse commercial usage of the database by rivals? (Viscusi, Harrington and Vernon, 2005, p. 323). For instance, one could argue that Google should be able to recover some of its sunk investment in scanning books.⁷² Also, would Google have created the database, which is likely to benefit consumers, if it had known that it would be required to share it?⁷³ Against this background, it appears reasonable to cast doubt on whether condition (4) is satisfied.

⁷²This is a common rationale for the legitimate possession of temporary monopoly power in industries with high upfront investments such as the pharmaceutical industry. If expected future profits are too low, producers would *ex ante* not be willing to invest in R&D in the first place. See Supreme Court in *Verizon Communications Inc. v. Law Offices of Curtis V. Trinko LLP*, 540 U.S. 398 (2004), p. 7: "The mere possession of monopoly power, and the concomitant charging of monopoly prices, is not only not unlawful; it is an important element of the free-market system. The opportunity to charge monopoly price 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. To safeguard the incentive to innovate, the possession of monopoly power will not be found unlawful unless it is accompanied by an element of anticompetitive conduct."

⁷³See Areeda (1989, p. 851), who states that "the justification for refusing to share a research laboratory does not focus on the practical infeasibility of letting another use the laboratory, but on the general concern that the defendant would never have built a laboratory of that size and character in the first place if he had known that he would be required to share it. Required sharing discourages building facilities such as this, even though they benefit consumers."

To sum up, the analysis of the four conditions set forth in *MCI v. AT&T* leads us to the conclusion that antitrust liability may not be established under the essential facilities doctrine. Taking the fifth condition added in *Verizon v. Trinko* into account could confirm this impression (Samuelson, 2010a; Grimmelmann, 2009a; Fraser, 2010). Nevertheless, even though liability may not be established under the essential facilities doctrine, the antitrust authorities will still have to ensure that Google does not leverage its market dominance to up- or downstream markets.⁷⁴ In doing so, compulsory licensing, for example, may be required. In reference to the downsides of compulsory licensing,⁷⁵ however, the literature emphasizes the imposition of a consent decree as a promising alternative in thinking antitrust policy in the case of Google's monopoly.⁷⁶ As compared to compulsory licensing, Ji (2010) stresses that a consent decree with a rate-setting court provision would be a more efficient form of liability for monopoly regulation. In particular, a consent decree crafted in the fashion of the American Society of Composers, Authors, and Publishers (ASCAP) would allow courts to act as quasi-regulators, providing an efficient mechanism design in bargaining reasonable and non-discriminatory⁷⁷ licensee fees for third parties (Ji, 2010, pp. 33 et seq. and Crane, 2009, pp. 307). As for settlement controlled prices, the ASA does not provide a "carte blanche" for setting book prices, nor does it enable gaining control over the amount of accessible copies. It rather requires Google to set a price using a competition-mimicking pricing

⁷⁴For instance, one may consider the integrated links to online book stores. In this regard, it will have to be ensured that Google does not take advantage of his dominant market position.

⁷⁵See Merges (1996, pp. 1376 et seq.) on the downsides of compulsory licensing in a multimedia context.

⁷⁶See Ji (2010, pp. 23 et seq.), Grimmelmann (2009a, p. 13), and Grimmelmann (2009b, pp. 13 et seq.). Crane (2009) provides a general perspective regarding the effectiveness of a consent decree.

⁷⁷See Frischmann and Weber Waller (2008, pp. 36 et seq.) on licensing in the context of the essential facilities doctrine.

algorithm for orphan books and for books whose right holders choose not to set a price.⁷⁸

For claimed, commercially unavailable in-copyright books,⁷⁹ however, right holders can sell their books through Google’s rivals or set their own prices for sale through Google (Elhauge, 2010, pp. 3 et seq.). For instance, according to the ASA, right holders may even offer their books for free.⁸⁰

As far as prices of out-of print books go, note that consumers of such works benefit from Google Book Search. The search engine reduces the transactions costs of finding out-of-print books and therefore it also reduces the prices of such works. Finally, note that alternative sources of supply, such as document delivery services, will still be accessible. The Google Book Search program will rather increase access to books by providing additional free public access services. For instance, Google may provide one computer terminal with free access to the collection of works for every four thousand full-time students of higher education institutions in the United States⁸¹ as well as one terminal per building of each public library.⁸²

3.3. Policy Implications. From a copyright perspective, the court will have to approach the question as to whether the Google Book Search Settlement is either a fair use or an infringement of copyright.⁸³ Our analysis

⁷⁸See ASA, Sections 4.2(b)(i)(2), 4.2(c)(ii)(2), and 4.2(c)(iii).

⁷⁹Commercially unavailable books are in-copyright books that are not offered for sale as digital copy or in print.

⁸⁰See ASA, Section 4.2(b)(i)(1). This option might be particularly attractive for academics who are likely to be more interested in a maximum distribution and readership of their works than in direct financial gains. See Shavell (2010) as well as Feess and Scheufen (2011). See also Müller-Langer and Watt (2010) for an analysis of the potential effects on universities if copyright for academic works were abolished.

⁸¹The number of computer terminals depends on the Carnegie Classification of Institutions of Higher Education. For higher education institutions that qualify (do not qualify) “as Associate’s Colleges”, Google may provide one terminal per four (ten) thousand full-time students, according to ASA, Sections 4.8(a)(i)(1) and 4.8(a)(i)(2), respectively.

⁸²See ASA, Section 4.8(a)(i)(3).

⁸³Note that an application of the “fair-use” doctrine is only a subject matter of U.S. copyright law. In German copyright law, the Book Search project would infringe the copyright of the particular authors and publishers. The competence of U.S. national law follows from

of the “fair use” argument reveals a need to balance the social benefits and costs assigned to the Library Program. Particularly the first statutory factor of the analysis – the purpose and character of the use – weighs the judgment in favor of a fair use. Accordingly, Google’s approach constitutes a transformative use for two reasons. First, Google creates a product that is meaningfully distinct from the original work and hence is not likely to harm the right holder since a displaying of snippets of a book is no substitute for a purchased, full-text version. Second, the project generates additional social welfare as it adds a new functionality to the protected works. Nevertheless, as the results of the analysis of all four statutory factors listed under 17 U.S.C. §107 are to be weighed together,⁸⁴ a final judgment is complex. However, the ASA has shifted the final judgment in favor of a fair use argumentation.

Some additional considerations may help in the assessment. Arguments from transaction cost and welfare economics may push our qualitative conclusions in the direction of a fair use. The project will especially benefit authors since the demand for books is likely to increase due to a decrease in information costs on the demand side.⁸⁵ This argument will be particularly true for authors of formerly out-of-print works. Google will create a new market for these works. It is also important to note that consumers of out-of-print works will benefit from lower transaction costs of finding such works. In addition, the provided opt-out strategy is efficient from the transaction costs perspective. Especially considering the large number of orphan works, the opting out of books instead of opting them in will be the only way to

the “*lex loci protectionis*” principle. See Ott (2007) on this point. Besides, the amended settlement induced changes to the international scope towards US works.

⁸⁴See footnote 43.

⁸⁵Google’s platform will create a fundament to make book content accessible and searchable. Accordingly, the search engine will affect the decision making of potential readers, as it enables them to locate relevant information by the typing of a search term.

force an efficient allocation of right holders to their works.⁸⁶ In addition, the creation of the BRR will ensure that authors and publishers will participate in the revenues gained. Finally, Google is about to provide a reasonable solution to the orphan works dilemma.

In conclusion, copyright policy may be advised to allow for a “fair-use” argumentation. As for competition policy, the conclusions made reveal a need to investigate the class action settlement in more detail. In particular, however, some of the arguments made by Grimmelmann (2009a, 2009b), Picker (2009) and Samuelson (2010a) – who strongly advocate a modification or even rejection of the settlement – were weakened. Accordingly, a cartel of authors and publishers using the BRR to coordinate their prices and other market parameters is rather unlikely due to the market conditions. Apart from that, Google’s introduction of the Unclaimed Books Fiduciary as an independent monitoring agency will ease some of the concerns.

Nevertheless, some modifications – especially with respect to the composition of the BRR – will be required. From a consumer perspective, it is essential that Google’s pricing algorithm effectively mimics a competitive Nash-Bertrand market outcome. We therefore recommend post-settlement third-party oversight and scrutiny in this regard as an important safeguard in order to ensure the pricing algorithm’s adherence to competitive pricing.

4. A CRITICAL PERSPECTIVE

The analysis of the Amended Google Book Search Settlement and the Library Program still leaves us with several questions to be addressed. In particular, economists will have to forward a more economic approach to balance all associated benefits and costs in the context of a comprehensive

⁸⁶It is, however, important to note that the Statement of Interest of the United States of America Regarding Proposed Amended Settlement Agreement, *The Author’s Guild, et. al. v. Google Inc.*, No. 05-CV-8136 (S.D.N.Y. 4 February 2010), p. 25, remains to favor an opt-in regime.

welfare analysis. In this context, Google's platform is expected to revolutionize information flows and hence also the creation of future innovation. Thus, the effects of the settlement on the creation of derivative and subsequent works will have to be considered.

In addition, several aspects beyond the dimensions of copyright law and competition policy have been neglected. First, technological aspects will have to be considered. How secure is Google's database against the threat of hackers? In this context, particularly Google's argument to allow for a display of maximum 20 percent of book content may eventually be restricted in regard to its technical implementation. The "fair use" defense would fall with the technical vulnerability of Google's database.

Furthermore, Ott (2007) criticizes the quality of Google's scanning. He argues that Google seeks a high quantity instead of a high quality in its scanning process. Finally, a legitimation of the settlement would also raise concerns of cultural and moral science. As such, the effects of a "googlization of everything" in society (Vaidhyanathan, 2009) will have to be discussed. Moreover, the settlement would discriminate against lawful competitors of Google. While other initiatives that seek for an explicit permission of the right holder of a work actually follow the requirements provided by law, Google's thrust forward may be rewarded by the class action settlement.

5. A NOTE ON JUDGE CHIN'S DECISION

The very recent proceedings resulted in a (first) decision on the pending litigation process. On March 22, 2011, judge Denny Chin issued his order in *The Authors Guild et al. v. Google, Inc.* (05 Civ. 8136 (DC)) rejecting the GBS class action settlement (henceforth, Chin, 2011).⁸⁷ Following rule 23 of

⁸⁷The statement of Judge Denny Chin can be found at <http://amlawdaily.typepad.com/googlebooksopinion.pdf> (visited 23 March 2011).

the Federal Rules of Civil Procedure he concludes that the proposed settlement (ASA) “is not fair, adequate and reasonable” (Chin, 2011, p. 45). In particular, he argues that the ASA goes too far as it would grant Google a significant advantage over other competitors while rewarding Google for engaging in wholesale copying of copyrighted works without permission (Chin, 2011, pp. 1 et seq.). In reviewing the amended deal and more than 500 submissions commenting on the ASA and its original version, Judge Chin shares concerns in copyright and antitrust issues. In addition, questions regarding the guardianship over orphan works as well as international concerns may advance the argument that this matter should be assigned to Congress rather than being crafted as a class action lawsuit (Chin, 2011, pp. 22 et seq.).

At the end of his order Chin suggests that “many of the concerns raised in the objections would be ameliorated if the ASA were converted from an “opt-out” settlement to an “opt-in” settlement.” (Chin, 2011, p. 46).

Our analysis may push the conclusions reached by Judge Chin into debate and eventually forward a claim for a more comprehensive theoretical as well as empirical assessment.

In terms of copyright, Chin (2011) highlights primarily Google’s “opt-out” policy as being most problematic against a fair use claim. The problem, however, may be rather twofold from a transaction cost perspective as it seems necessary to distinguish non-orphan from orphan works. While in the first case, a face-to-face negotiation with each right holder seems costly but feasible, the latter may detract from the solution to the orphan works dilemma as the right holders are by definition unknown. In this context, also George (2002) emphasizes the problems associated with the process of finding and allocating right holders of orphan works. Converting the settlement from

an “opt-out” to an “out-in” principle as Chin (2011) suggests may consequently raise the question on how to better serve the need for solving the problem. Alternative initiatives like the Open Access or Creative Commons movement may be limited in providing a promising solution as they fail to provide a retro-digitization.⁸⁸

From an antitrust perspective, Judge Chin mentions two main concerns in his opinion on the proposed settlement. First, the ASA may grant Google a monopoly over unclaimed works, in particular over orphan works (Chin, 2011, pp. 36 et seq.). Second, it may allow Google to control the search market (Chin, 2011, pp. 37 et seq.). Consider the first antitrust concern. From a consumer perspective, one may weigh the negative effects of a de facto monopoly over orphan works and the benefits of having digital access to those works (see Sections 3.2.1 and 3.2.2 of this article). The ASA may be beneficial to consumers as the value consumers derive from digital access to orphan works is likely to exceed the value from only having physical access to those works.⁸⁹ Also, the negative effects of a monopoly of orphan works associated with monopoly pricing can be reduced if explicit third-party inspection ensures that Google’s pricing algorithm for orphan works effectively replicates a competitive market for books.⁹⁰ This suggests that a comprehensive welfare analysis is required to assess the first antitrust concern mentioned by Judge Chin.

Secondly, the question whether the ASA would give Google control over the search market relates to the question whether it would grant Google a monopoly on digital books databases. We suggest an empirical analysis of whether the saved costs of duplication associated with having only one

⁸⁸In this context, Samuelson (2010c) argues that many academic authors would prefer that orphan works should be treated on open access basis.

⁸⁹For instance, Chin (2011) states on p. 3 that “books will become more accessible. Libraries, schools, researchers, and disadvantaged populations will gain access to far more books”.

⁹⁰See ASA, Sections 4.2(b)(i)(2), 4.2(c)(ii)(2), and 4.2(c)(iii).

supplier of a digital books database may more than outweigh the value of competition associated with an additional database. This is an empirical question beyond the scope of this article, but certainly a promising avenue for further research. An analysis of the welfare effects of competing databases for scientific works such as Lexis and Westlaw appears to be a natural starting point. However, one may also take into consideration that additional procompetitive effects associated with a rival digital books database may be lower if the pricing algorithm for settlement controlled prices replicates an outcome under competitive market conditions.

6. CONCLUSIONS

The amended Google Book Search Settlement may ensure the realization of the social benefits associated with the implementation of Google's search engine. The class action settlement would entitle Google to continue with the creation of a platform to make book content accessible and searchable worldwide via the internet. Especially with regard to the large amount of orphan works, the settlement would finally create a new market and hence additional social surplus. In this respect, the settlement seems to be socially desirable from a copyright law perspective. From a competition policy perspective, the conclusions made reveal a need to investigate the class action settlement in more detail. However, some of the arguments made by Grimmelmann (2009a, 2009b), Picker (2009) and Samuelson (2010a) – who strongly advocate a modification or even rejection of the settlement – may be weakened. Nevertheless, the composition of the class action settlement still requires a modification to reduce antitrust concerns. We therefore recommend post-settlement third-party oversight and scrutiny as an important safeguard in order to ensure the pricing algorithm's adherence to competitive Nash-Bertrand pricing. Competition policy will have to ensure a reduction

of Google's monopolistic position in order to safeguard against a monopolistic bottleneck. Nevertheless, attention with regard to the conclusions drawn is needed. A comprehensive welfare analysis is required to balance all costs and benefits associated with the Google Book Search settlement. Particularly the effects on the creation of derivative and subsequent copyright works reveal an interesting field of further research. Also, the analysis of interests of the different parties involved in the Google Book Search settlement appears to be an interesting avenue for further research from a political economy perspective (Bechtold, 2010, p. 252). Above all, the Google Book Search Settlement raises concerns beyond the dimensions of law and economics. In particular, several aspects regarding technological questions as well as moral and cultural issues still need to be considered. In the end, the Google Book Search Settlement will be a first reasonable step towards an unlimited access to knowledge in the 21st century and a substantial impulse for the future scientific discussion on the role of copyright law in the information age or "the future of books in cyberspace" (Samuelson, 2010b). Google is about to fill an important gap regarding the accessibility of knowledge, as it provides a retro-digitization in contrast to the Creative Commons and Open Access movements. However, especially in regard to the field of scientific research, Google's search engine provides an added value. Scholars are given a tool to locate information, lowering their (information) costs to write and publish academic works. In addition, the option to provide free access to books to force a maximum distribution and readership may forward the discussion on the role of copyright in academic works.⁹¹ Google could be a third road to free access to scientific research and create an additional counterbalance with respect to the conventional publishing model.

⁹¹See Shavell (2010) on the recent discussion on whether copyright for academic books should be abolished. See also Feess and Scheufen (2011).

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