

**COPYRIGHT EXTREMOPHILES: DO CREATIVE INDUSTRIES
THRIVE OR JUST SURVIVE IN CHINA’S HIGH-PIRACY
ENVIRONMENT?**

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I. INTRODUCTION

Does copyright piracy actually *benefit* creators and the creative industries in China? Recent scholarship and commentaries suggest that rampant piracy might result in no net social loss in China or might even produce net social benefits.¹ This tracks a broader trend in intellectual property (“IP”) scholarship expressing skepticism about the benefits of exclusive IP rights and emphasizing the importance of public access to knowledge and the cumulative nature of creativity and innovation.²

1. See, e.g., LUCY MONTGOMERY, CHINA’S CREATIVE INDUSTRIES 70 (2010); Jingying Li, *From D-Buffers to the D-Generation: Piracy, Cinema, and an Alternative Public Sphere in Urban China*, 6 INT’L J. COMM. 542, 557–61 (2012) (discussing how the black market for films undermines state censorship and helps to establish a new venue for civil discourse); Kal Raustiala & Christopher Sprigman, *Fake It Till You Make It*, 92 FOREIGN AFF. 25, 26 (2013) (discussing piracy’s contribution to business growth, middle class development, and the encouragement of creativity throughout China); Joe Karaganis, *Media Piracy and the End of Chinese Cultural Exceptionalism? The Ancient History of the DVD*, CHINA L. BLOG (July 10, 2013), <http://www.chinalawblog.com/2013/07/media-piracy-and-the-end-of-chinese-cultural-exceptionalism-the-ancient-history-of-the-dvd.html> [hereinafter Karaganis, *Ancient History of the DVD*]; Joe Karaganis, *Media Piracy and the End of Chinese Cultural Exceptionalism? Part 2 of 3: What Everyone Wants*, CHINA L. BLOG (July 13, 2013), <http://www.chinalawblog.com/2013/07/media-piracy-and-the-end-of-chinese-cultural-exceptionalism-part-2-of-3-what-everyone-wants.html> [hereinafter Karaganis, *What Everyone Wants*] (observing China’s exposure to Western norms and values through pirated goods); Joe Karaganis, *The End of Chinese Cultural Exceptionalism? Part 3 of 3: Forget It, Jack, It’s Chinatown*, CHINA L. BLOG (July 14, 2013), <http://www.chinalawblog.com/2013/07/the-end-of-chinese-cultural-exceptionalism-part-3-of-3-forget-it-jack-its-chinatown.html> [hereinafter Karaganis, *Forget It, Jack, It’s Chinatown*].

2. See, e.g., YOCHAI BENKLER, THE WEALTH OF NETWORKS 38–40 (2006); JAMES BOYLE, THE PUBLIC DOMAIN 8–9 (2008); LAWRENCE LESSIG, FREE CULTURE 183–89 (2004); JESSICA LITMAN, DIGITAL COPYRIGHT 173 (2006); KAL RAUSTIALA & CHRISTOPHER SPRIGMAN, THE KNOCKOFF ECONOMY 7–8 (2012).

As scholars increasingly question the role and value of copyright law in society, some might suggest the “headline” from China’s experience is that creative industries can survive and even thrive despite an ineffectual copyright system. Piracy remains rampant, but China has skyrocketed to become the second largest film market in the world, with production quantitatively on par with Hollywood.³ The music industry is disproportionately small given China’s size and the enormous popularity of music online, but it has not collapsed.⁴ People still write and produce music, and some superstars even earn millions from alternative revenue streams such as concerts, corporate events, and sponsorships.⁵ So, does piracy have an unduly bad reputation in China, and is copyright overrated? As one commentator asks, “[W]here is the problem in need of an enforcement solution [in China]? Where is the evidence that piracy is undercutting production?”⁶

This Article aims to deconstruct and refute the notion that effective copyright enforcement is unnecessary — or even detrimental — to the growth and success of creative industries in China and beyond. Instead, one might liken successful Chinese music and film producers to extremophiles: biological organisms that adapt to environments otherwise uninhabitable to most life.⁷ Just as microorganisms have evolved to thrive in superheated deep-sea vents or highly acidic environments,⁸ so too can a subset of creative professionals find ways to monetize their works even in a high-piracy environment. The fact that some monetization models can work for some types of producers or artists in China does not mean that optimal or even near-optimal conditions exist for the development of flourishing, healthy, and stable creative industries. In short, poor copyright enforcement inflicts significant and persistent harms on China’s music and film industries. To invoke the extremophiles analogy, China’s inhospitable creative industry environment may support narrow strains of creative “life,” but with an effective regime of copyright norms and enforcement, China’s creative ecosystem could more closely resemble a lush, diverse rainforest.

The purpose of this Article is neither to explain why copyright piracy is endemic in China nor to proffer solutions to the profound challenge of piracy; ample literature already addresses these topics.⁹

3. See *infra* Part III.B.

4. See *infra* Part III.C.

5. See *infra* Part III.C.1.

6. Karaganis, *What Everyone Wants*, *supra* note 1.

7. See THE CONCISE OXFORD DICTIONARY 505 (Judy Pearsall ed., 1999).

8. *Extremophile*, WIKIPEDIA, <http://en.wikipedia.org/wiki/Extremophile> (last visited May 7, 2014).

9. See, e.g., WILLIAM P. ALFORD, TO STEAL A BOOK IS AN ELEGANT OFFENSE 2–4 (1995); MARTIN K. DIMITROV, PIRACY AND THE STATE 4–5, 187 (2009); ANDREW C. MERTHA, THE POLITICS OF PIRACY 2–5 (2006); Jiarui Liu, *The Tough Reality of Copyright Piracy: A Case Study of the Music Industry in China*, 27 CARDOZO ARTS & ENT. L.J. 621,

Instead, this Article responds to the contention that eliminating piracy may be a socially wasteful endeavor because piracy in China confers net benefits on creators, Chinese society, and beyond. To this end, this Article examines China's film and music industries to analyze six themes developed in recent scholarly literature about piracy's inconsequentiality or even advantageousness to China's creators, creative industries and, by extension, Chinese society.¹⁰ These themes are: (1) piracy has not harmed the Chinese creative industries, because production continues apace and is even growing; (2) piracy benefits the creative process and consumers by lowering access barriers to a wide variety of information goods; (3) piracy incentivizes copyright owners to adopt innovative business models; (4) piracy is especially important for political discourse in China because it helps information goods circumvent heavy-handed state censorship policies; (5) piracy confers benefits on foreign rights holders in China by providing free advertising and branding for their works; and (6) foreign dominance poses a greater threat to China's creative industries than piracy does.

This Article argues that each of these six hypotheses about piracy in China is wrong, or at least incomplete. In responding to these themes, this Article claims there are three critical functions of copyright that are undermined in a high-piracy environment such as China. First, copyright helps to nurture and enable a professional class of creators, including an ecosystem of support professionals who are critical to the development and maintenance of a vibrant creative sector. Second, copyright enables creators to monetize diverse revenue streams — a crucial but often overlooked function of copyright. Reduced revenue stream diversity harms the creative ecosystem by diminishing monetization opportunities for smaller and independent producers, distorting market signals sent to producers, and dispropor-

623–24 (2010); Eric Priest, *The Future of Music and Film Piracy in China*, 21 BERKELEY TECH. L.J. 795, 801 (2006); Peter K. Yu, *From Pirates to Partners: Protecting Intellectual Property in China in the Twenty-First Century*, 50 AM. U. L. REV. 133–36 (2000); Rogier Creemers, *Explaining Audiovisual Media Piracy in China* 34–36 (Feb. 2, 2012) (unpublished Ph.D. dissertation, Maastricht University) [hereinafter Creemers, *Explaining Audiovisual Media Piracy*], available at <http://arno.unimaas.nl/show.cgi?fid=24067>.

10. While copyright law in China affects many creative industries, numerous scholars have focused in particular on piracy's effects on the Chinese film and music industries. See, e.g., MONTGOMERY, *supra* note 1, at 41–75 (analyzing the music and film industries, among others, in China); Jingying Li, *supra* note 1 (analyzing the effects of piracy on the film industry in China); Jiarui Liu, *supra* note 9, at 631 (analyzing the effects of piracy on the music market in China); Priest, *supra* note 9, at 798–99 (analyzing the effects of piracy on the music and film industries in China); Creemers, *Explaining Audiovisual Media Piracy*, *supra* note 9, at 13 (analyzing the effects of piracy on the market for audiovisual works in China); Karaganis, *Forget It, Jack, It's Chinatown*, *supra* note 1 (addressing the relationship between Chinese censorship of Hollywood films and the business models now prevalent in the Chinese film industry); Karaganis, *What Everyone Wants*, *supra* note 1 (analyzing the effects of piracy on the film industry in China). The focus on the Chinese film and music industries is likely attributable to their domestic cultural and economic importance as well as their economic importance to foreign copyright owners.

tionately exposing producers to the idiosyncrasies of peculiar markets and exploitation by intermediaries.¹¹ Third, a functioning copyright system enables market-supported creative industries independent of government largesse; that is, independent creative industries are crucial to the long-term development of a more open and diverse public discourse. With these three functions of copyright diminished, China's piracy environment threatens the long-term stability and growth of its creative industries.

Part II of this Article provides an overview of China's copyright law and enforcement challenges and discusses the primary causes proffered by scholars for China's poor copyright enforcement record. Part III examines the economic and regulatory ecosystem in which China's film and recording industries are situated. It considers these industries' monetization challenges, areas and causes of their growth, and the role that their economic and regulatory environments — including piracy and censorship — play in aiding and hindering their development. Part IV introduces the six themes about piracy drawn from recent literature, as enumerated above. Part V then responds to and critiques each of these six themes in light of the circumstances of China's music and film industries and reveals how they ignore the three critical functions of copyright that are highlighted above. Finally, Part VI argues that the lessons in Part V are applicable beyond China, and shows in particular how piracy in the United States threatens the stability of the creative industries by diminishing revenue stream diversity.

II. COPYRIGHT PIRACY IN CHINA

Copyright owners have long lamented rampant media piracy in China. For years, international film and music industry groups have estimated the piracy rate for optical disc media (CDs, DVDs, and VCDs) to be at least eighty-five to ninety percent.¹² As recently as 2011, virtually all music downloads in China were unauthorized.¹³ Subsequently, the international major record labels struck an accord with some of China's major search engines — one of the most common sources of links to unauthorized music downloads¹⁴ — which

11. The starkest example of such exploitation is the treatment of record labels by Chinese mobile service providers, which earn more than \$4 billion annually from mobile music services but allegedly keep more than ninety-eight percent of the revenue for themselves. See *infra* Part III.C.1. Labels, with virtually every other source of recorded music revenue foreclosed by piracy, appear to feel they have little choice but to accept what China's mobile providers give them. *Id.*

12. See Jiarui Liu, *supra* note 9, at 631; Priest, *supra* note 9, at 797.

13. INT'L FED'N OF THE PHONOGRAPHIC INDUSTRY ("IFPI"), DIGITAL MUSIC REPORT 2012 23 (2012), available at <http://www.ifpi.org/content/library/DMR2012.pdf>.

14. See *infra* Part III.C.1.a.

resulted in the search engines receiving licenses for at least some music content.¹⁵ It is currently unclear what percentage of music downloads is unlicensed, but by all accounts the rate of online music piracy remains very high.¹⁶ China's recorded music revenue is so disproportionately low that China's total recorded music revenue in 2011 was eclipsed by that of Thailand — itself a high-piracy country with one-twentieth the population of China.¹⁷

The piracy rate for online video has declined in recent years as several leading user-generated content (“UGC”) sites have self-purged pirated content and endeavored to acquire licenses for any professionally produced content they serve.¹⁸ Nevertheless, video piracy remains a serious problem as users migrate from UGC sites to peer-to-peer streaming websites that serve high volumes of pirated content.¹⁹

A. Copyright Enforcement: Legal Framework and International Pressure

While enforcement on the ground remains an extreme challenge, the high piracy rates in China do not necessarily result from a deficient legal infrastructure or a low volume of enforcement. To begin with, China has a relatively sophisticated legal infrastructure for the grant and enforcement of copyright rights. Chinese copyright law in many respects comports with international standards regarding the economic and moral rights granted to creators, the terms of rights, the types of works eligible for protection, and available remedies, includ-

15. IFPI, *supra* note 13 (noting that the deal with China's largest search engine, Baidu, “by no means ends China's piracy problem” and that “[o]ther unauthorized ‘deep-linking’ services are still operating, while cyberlockers and illegal download sites remain a huge barrier to growth”).

16. See OFFICE OF THE U.S. TRADE REP., 2012 SPECIAL 301 REPORT 29 (2012) [hereinafter OFFICE OF THE U.S. TRADE REP., 2012 SPECIAL 301 REPORT] (“[S]ales of IP-intensive goods and services to China from U.S. companies remain substantially below levels in other markets, measured in a variety of ways, ranging from spending on legitimate music as a percentage of GDP to software sales per personal computer.”); IFPI, *supra* note 13.

17. OFFICE OF THE U.S. TRADE REP., 2012 SPECIAL 301 REPORT, *supra* note 16.

18. See *id.*; Loretta Chao, *Top China Video Site Steps Up Its Piracy Fight*, WALL ST. J., Apr. 19, 2010, at B8 [hereinafter Loretta Chao, *Top China Video Site Steps Up Its Piracy Fight*], available at <http://online.wsj.com/news/articles/SB10001424052748703757504575193741461518942>; see also Loretta Chao, *China's Youku Goes Hollywood*, WALL ST. J., Jan. 6, 2011, http://online.wsj.com/article/SB10001424052748703675904576063510245910424.html#_jmp0_.

19. See OFFICE OF THE U.S. TRADE REP., 2012 SPECIAL 301 REPORT, *supra* note 16; Karen R. Thorland, Motion Picture Ass'n of Am., Enforcement Issues in the Entertainment Industries, PowerPoint Presentation Before the Berkeley Center for Law and Technology October 2012 Chinese IP Law Conference (Oct. 4, 2012), available at http://www.law.berkeley.edu/files/bclt_Panel_4_Karen_Thorland.pptx (noting that the “[m]igration of piracy [in China] from video hosting sites to hybrid streaming ‘rogue’ sites using P2P technology are growing immensely in popularity and are difficult to enforce against”).

ing damages and injunctive relief.²⁰ Similar to United States law, Chinese law provides criminal sanctions for copyright infringement.²¹ China also has established specialty IP divisions within courts throughout the nation.²² China is a signatory to the major international copyright conventions, including: the Berne Convention, the World Trade Organization's ("WTO") Agreement on Trade-Related Aspects of Intellectual Property ("TRIPS"), the World Intellectual Property Organization ("WIPO") Copyright Treaty, and the WIPO Performances and Phonograms Treaty.²³ The Chinese copyright law is presently undergoing its third major revision in the past dozen years, much of which is aimed at addressing existing deficiencies in the law.²⁴ In short, China has developed a relatively sophisticated copyright infrastructure in the short time since it adopted its first modern copyright law twenty-four years ago.²⁵

Furthermore, the volume of copyright enforcement in China is high. Controlling for population, China has a higher volume of IP enforcement than any other country in the world.²⁶ In 2011, 35,185 civil copyright cases were litigated in China,²⁷ as compared with 2,225 in the United States.²⁸

Chinese copyright regulations also extend to online activity, where the majority of piracy occurs. China has regulations that provide notice and takedown procedures analogous to those of § 512(c)

20. See OFFICE OF THE U.S. TRADE REP., 2011 REPORT TO CONGRESS ON CHINA'S WTO COMPLIANCE 4 (2011); Priest, *supra* note 9, at 806–17; Peter K. Yu, *The Middle Kingdom and the Intellectual Property World*, 13 OR. REV. INT'L L. 209, 210–11 (2011).

21. Zhonghua Renmin Gongheguo Zhuzuo Quanfa (中华人民共和国著作权法) [Copyright Law of the People's Republic of China] (promulgated by the Standing Comm. Nat'l People's Cong., Feb. 26, 2010, effective Apr. 1, 2010), art. 48 (China) [hereinafter Copyright Law of the People's Republic of China], translated in WORLD INTELLECTUAL PROPERTY ORGANIZATION, available at <http://www.wipo.int/wipolex/en/details.jsp?id=6062>.

22. See INT'L INTELLECTUAL PROP. INST., *Specialized Intellectual Property Courts Worldwide*, <http://www.iipi.org/map/map.htm> (select "China" hyperlink) (last visited May 7, 2014) ("All High People's Courts, almost all Intermediate People's Courts, and all Primary People's Courts with civil jurisdiction to hear IPR cases have specialized IPR divisions.")

23. See, e.g., U.S. COPYRIGHT OFFICE, CIRCULAR 38A: INTERNATIONAL COPYRIGHT RELATIONS OF THE UNITED STATES 4 (2014), available at <http://www.copyright.gov/circs/circ38a.pdf>.

24. See Hong Xue, *A User-Unfriendly Draft: 3rd Revision of the Chinese Copyright Law*, INFOJUSTICE.ORG (Apr. 25, 2012), <http://infojustice.org/wp-content/uploads/2012/04/hongxue042012.pdf>.

25. See *id.*

26. DIMITROV, *supra* note 9, at 33.

27. Helen Sloan, *The Surge in IP Litigation in China Continues*, INTELL. ASSET MGMT. (Apr. 27, 2012), <http://www.iam-magazine.com/blog/detail.aspx?g=4a132dd6-ed14-4eff-b646-af5bf3638cc7&q=35%2c185#search=%2235%2c185%2>.

28. ADMIN. OFFICE OF THE U.S. COURTS, FEDERAL JUDICIAL CASELOAD STATISTICS: MARCH 31, 2012 50 (2012), available at <http://www.uscourts.gov/Viewer.aspx?doc=/uscourts/Statistics/FederalJudicialCaseloadStatistics/2012/tables/C02Mar12.pdf>.

of the United States' Digital Millennium Copyright Act.²⁹ Websites hosting user-uploaded content are immune from copyright liability if they expeditiously remove the content and follow other procedures upon receipt of notice from the copyright owner.³⁰ For music copyright owners in particular, however, requesting the removal of infringing files has had little effect. Sometimes files linked through search engine results are hosted on a rotating network of surreptitious domains, and "infringement notifications result[] in unlicensed songs simply moving from one of these domains to another."³¹ Moreover, copyright owners allege that the notice and takedown procedures in China offer them little practical benefit. Online service providers' divergent, onerous and unreasonable requirements for establishing copyright ownership and infringement squander copyright owners' time and resources while the infringement continues unabated.³² Although search engines such as Baidu and Sogou have recently executed licensing agreements with international major record labels, music industry executives allege that these sites still host many files not covered by the licenses.³³ Owners of audiovisual copyrights have enjoyed more success enforcing removal of infringing content from video sites, but this has had less to do with notice-and-takedown compliance and more to do with market pressure and business strategy.³⁴

29. 17 U.S.C. § 512(c) (2012).

30. A website enjoys a safe harbor from copyright liability if it: (1) clearly indicates that it provides its storage space to subscribers, (2) does not alter the works in question, (3) has no knowledge of or reasonable grounds for knowing of the infringing act, (4) does not seek to financially benefit directly from the works, and (5) expeditiously removes the content after receipt of the notice. Xinxu Wangluo Chuanbo Baohu Quan Tiaoli (信息网络传播保护权条例) [Regulations for the Protection of the Right of Communication Through the Information Network] (promulgated by the St. Council, May 10, 2006, effective July 1, 2006) ST. COUNCIL GAZ., Jul. 10, 2006, at 13 (China), *translated in* 3 CHINA PAT. & TRADEMARKS 90, 93–94 (2006). The 2012 second revision draft of the Copyright Law of the People's Republic of China provides that a network service provider that fails to expeditiously remove or otherwise disable access to infringing content on its service "bear[s] joint and several liability with the [direct] infringer." Zhonghua Renmin Gongheguo Zhuzuo Quanfa (Xiugai Caoan Di Er Gao) (中华人民共和国著作权法(修改草案第二稿)) [Copyright Law of the People's Republic of China (Second Revision Draft)] (promulgated by the Nat'l Copyright Admin. Mar. 31, 2012, effective Jul. 31, 2012) (Westlaw China 万律 (Westlaw China)), art. 69 (China).

31. Andrew Orlovski, *China's Nonstop Music Machine*, THE REGISTER (Sept. 13, 2008), http://www.theregister.co.uk/2008/09/13/baidu_investigation?page=1.

32. See Mathew D, *China Aims To Redress Copyright Burden of Proof Imbalance*, GLOBAL OUTPOST (May 5, 2011), <http://www.theglobaloutpost.com/archives/45>. For a discussion of sufficiency of takedown notices in Chinese court cases involving Baidu and Yahoo! China, see Seagull Haiyan Song, *A Comparative Copyright Analysis of ISP Liability in China Versus the United States and Europe*, 27 COMPUTER & INTERNET L. 1, 10 (2010).

33. See Mathew D, *supra* note 32; Liu Yuhan, *Sohu, Sogou Settle Music-Piracy Lawsuit with 4 Labels*, CHINADAILY USA (Mar. 5, 2013, 12:42), http://usa.chinadaily.com.cn/paper/2013-03/05/content_16278696.htm.

34. See *infra* Part III.B.1.

Any gains that copyright owners have achieved in China are only modestly attributable to international political efforts — led largely by the United States government — to pressure China. Since the 1980s, United States businesses have lobbied the United States government to pressure China into improving IP protection.³⁵ However, diplomatic pressure from the United States resulted in what scholar Peter Yu calls the “cycle of futility.” That is, the United States, dissatisfied with the state of IP protection in China, repeatedly designated China as an offender of IP rights and then threatened to impose trade sanctions on Chinese imports.³⁶ China, in turn, responded with threats of retaliatory sanctions of its own.³⁷ In each instance, trade wars were averted by eleventh-hour memoranda of understanding in which China agreed to improve IP protection in return for the United States’ agreement not to impose tariffs.³⁸ The fact that the cycle repeatedly played out the same way throughout the 1990s is a testament to the inefficacy of the process.

The cycle of futility ceased, but piracy did not, when China joined the WTO in 2001 and became subject to the WTO’s official dispute resolution process.³⁹ Six years later, after bringing a number of other trade-related WTO cases against China, the United States brought a case concerning protection and enforcement of IP rights (“*China — Intellectual Property Rights*”).⁴⁰ Two of the three issues the United States raised addressed copyright protection. First, it argued that Article Four of the Copyright Law of the People’s Republic of China (“Copyright Law”), which denies protection to works that are not approved for distribution in China, violated TRIPS and the Berne Convention by conditioning copyright protection on the formality of pre-publication review and by effectively depriving unapproved works of the guaranteed minimum standards of protection.⁴¹ Second, the United States argued that Chinese thresholds for criminal prosecution of copyright infringement were too high and therefore inconsistent with requirements under the WTO’s TRIPS Agreement.⁴² The WTO dispute resolution panel held in favor of the United States with respect

35. See, e.g., ALFORD, *supra* note 9, at 112–19; Peter K. Yu, *supra* note 9, at 136–54.

36. Peter K. Yu, *Still Dissatisfied After All These Years: Intellectual Property, Post-WTO China, and the Avoidable Cycle of Futility*, 34 GA. J. INT’L & COMP. L. 143, 149 (2005).

37. *Id.*

38. Peter K. Yu, *supra* note 9, at 137–54.

39. Decision of 10 November, 2001, *Accession of the People’s Republic of China*, WT/L/432 (Nov. 23, 2001).

40. Request for Consultations by the United States, *China — Measures Affecting the Protection and Enforcement of Intellectual Property Rights*, WT/DS362/1 (Apr. 10, 2007).

41. *Id.*

42. *Id.*

to the Copyright Law Article Four claims, but not the criminal threshold claims.⁴³

China — Intellectual Property Rights indicates that the WTO dispute resolution mechanism has been a disappointment as a means of improving copyright enforcement in China. China amended its Copyright Law to comply with the WTO panel's ruling, but it is unlikely this technical amendment will have a significant effect because it fails to remedy many of the principal causes of piracy discussed below.⁴⁴ Therefore, even the partial United States victory in this case was likely Pyrrhic. Moreover, if United States copyright industries pressure the United States Trade Representative to initiate another IP case against China, a new cycle of futility may result.⁴⁵

B. Factors Contributing to China's High-Piracy Environment

Despite formal advances in the law, China's piracy rates remain persistently high. As the following discussion demonstrates, commentators attempt to explain the high piracy rates by pointing to a number of systemic failures that limit copyright law's effectiveness as a deterrent, and to cultural factors that allegedly have inhibited the uptake of IP norms in Chinese society. Identifying a simple explanation or set of factors appears increasingly elusive, however.

One important reason why piracy persists at such a high level in China is that the threat of copyright enforcement provides little deterrence value. Damages awarded in civil infringement cases are often far too low to deter lucrative infringing activities.⁴⁶ Copyright law presently awards prevailing plaintiffs compensation for their actual damages or the defendant's illegal profits; if the evidence is insufficient to substantiate either damages or profits, then the court may award statutory damages up to 500,000 RMB (approximately \$79,000).⁴⁷ Average damages awarded are nowhere near the statutory limit. From 2006 to 2009, the average award for copyright infringement was just 31,189 RMB (slightly more than \$5000).⁴⁸ In a 2009

43. Report of the Panel, *China — Measures Affecting the Protection and Enforcement of Intellectual Property Rights*, WT/DS362/R (Jan. 26, 2009).

44. See Rogier Creemers, *The Effects of WTO Case DS362 on Audiovisual Media Piracy in China*, 31 EUR. INTELL. PROP. REV. 568, 572–73 (2009).

45. *Cf. id.*

46. Compare CIELA Summary Report: *Trend by Year*, CIELA: CHINA IP LITIGATION ANALYSIS, <http://www.ciela.cn/Search/TrendByYear.aspx?pageId=6&ppId=2&language=en> (search "Copyright" for "IP Right" and search "Infringement" for "Cause of Action"; then follow "Submit" hyperlink) (last visited May 7, 2014) (reporting average damages awarded in copyright infringement cases across China as 41,955 RMB in 2006, 39,891 RMB in 2007, 17,039 RMB in 2008, and 25,872 RMB in 2009), with Copyright Law of the People's Republic of China, *supra* note 21.

47. Copyright Law of the People's Republic of China, *supra* note 21.

48. CIELA Summary Report: *Trend by Year*, *supra* note 46.

study of damages claimed and awarded in fifty-four Chinese copyright cases, which included a number of cases involving major Western film studios and record labels as plaintiffs, the median copyright damages awarded were about \$18,000 — a mere nine percent of median damages claimed.⁴⁹ In one example involving unauthorized music downloads, the record label plaintiffs sought one million RMB in damages, but the court entered a judgment of just 60,000 RMB (approximately \$8800) against defendant Baidu,⁵⁰ China's largest search engine and a frequent defendant in copyright infringement lawsuits. Injunctive relief is available under the law,⁵¹ but enforcing injunctive orders in China has been a persistent challenge.⁵² Administrative enforcement actions also do little to deter infringement because they tend to emphasize high-profile campaigns involving agencies with overlapping jurisdiction, which often results in uncoordinated and duplicative efforts.⁵³

Commentators argue that several other systemic deficiencies contribute to the existence and prevalence of piracy, including: high evidentiary thresholds for bringing criminal copyright enforcement actions;⁵⁴ a relatively weak and under-resourced National Copyright Administration (the primary administrative organ tasked with developing copyright policy and enforcing copyright);⁵⁵ and severe censorship and market access policies that greatly restrict the legitimate distribution of foreign copyright owners' works, creating an enormous market for illegitimate copies.⁵⁶

In addition to these systemic factors, some scholars argue that cultural, social, and economic factors such as China's traditional political culture, a lack of local IP stakeholders, and relatively poor economic conditions, among other factors, converge to impede the flourishing of IP norms in Chinese society. One view, most closely

49. See KRISTINA SEPETYS & ALAN COX, NAT'L ECON. RESEARCH ASSOCS., INTELLECTUAL PROPERTY RIGHTS PROTECTION IN CHINA: TRENDS IN LITIGATION AND ECONOMIC DAMAGES 9, 13 (2009), available at http://www.nera.com/extImage/PUB_IPR_Protection_China_0109_final.pdf.

50. See Xue "Snow" Dong & Krishna Jayakar, *The Baidu Music Settlement: A Turning Point for Copyright Reform in China?*, 3 J. INFO. POL'Y 77, 89–90 (2013), available at <http://jip.vhost.psu.edu/ojs/index.php/jip/article/view/118/75> (discussing the 2008 litigation between Baidu and the Music Copyright Society of China).

51. Copyright Law of the People's Republic of China, *supra* note 21, art. 50.

52. See Dan Harris, *Protecting Your IP in China with an Injunction. Yeah, That's the Ticket*, CHINA L. BLOG (Oct. 20, 2012), <http://www.chinalawblog.com/2012/10/protecting-your-ip-in-china-with-an-injunction-yeah-thats-the-ticket.html> ("The problem with injunctions in China . . . has been its courts do not always have or employ the tools to make sure their injunctive orders are obeyed. This makes protecting your IP in China all that more difficult . . .").

53. See DIMITROV, *supra* note 9, at 14, 221–47; MERTHA, *supra* note 9, at 133–47.

54. See Priest, *supra* note 9, at 812–15, 825–26; Request for Consultations by the United States, *supra* note 40.

55. See DIMITROV, *supra* note 9, at 234–35.

56. See Creemers, *Explaining Audiovisual Media Piracy*, *supra* note 9, at 91–114.

associated with Harvard Law School professor William Alford, holds that China's political culture is primarily responsible for impeding the flourishing of copyright norms in China.⁵⁷ In particular, China's Confucian tradition of deemphasizing novelty and innovation while emphasizing mastery through emulation, coupled with the historical and enduring importance to the Chinese state of central information control, has rendered China's cultural soil relatively inhospitable to transplanted laws and norms aimed at establishing exclusive private property rights in creative works.⁵⁸ Others have argued that as China's developing economy further integrates into the world economy and its knowledge industries and innovative capacity mature, China will reach a "crossover" point at which it will transform from a net infringer of IP into a net producer and protector of IP.⁵⁹ This line of reasoning posits that piracy is endemic because China lacks IP stakeholders in sufficient numbers, that IP protection in China primarily benefits foreign rights holders, and that China will "get serious" about IP protection only when doing so is in its stakeholders' best interests.⁶⁰ As Chinese IP owners and the government recognize the value of China's indigenous IP, they will begin to improve rights consciousness and enforcement.⁶¹ Another explanation, closely associated with the "crossover" theory, is that China's relatively poor overall economic conditions exacerbate piracy because much of China's population still has difficulty affording expensive legitimate goods.⁶² According to this view, as China further develops economically and the average income rises, people will choose to purchase legitimate products over cheaper, pirated ones.⁶³

Recent statistics, however, have called some aspects of these theories into question. The notion, for example, that China lacks sufficient numbers of IP stakeholders is undermined when one considers

57. See ALFORD, *supra* note 9, at 1–2, 9–29.

58. See *id.*

59. See, e.g., Peter K. Yu, *Intellectual Property, Economic Development, and the China Puzzle*, in INTELLECTUAL PROPERTY, TRADE AND DEVELOPMENT 173, 202–20 (Daniel J. Gervais ed., 2007) (examining the internal and external relationships that affect private investment decisions to forecast when China will reach a crossover point and find strong IP protection to be in its best interest).

60. See, e.g., Patrick Brzeski, *China's Looming Entertainment Problem: Not Enough Lawyers*, HOLLYWOOD REP. (June 21, 2013), <http://www.hollywoodreporter.com/thr-esq/chinas-looming-entertainment-problem-not-572629>; see also Raustiala & Sprigman, *supra* note 1, at 30 ("Chinese attitudes and practices toward copying cannot be expected to change quickly. As China's economy advances further, perhaps the balance of interests will shift, and the country might adopt a less permissive approach.")

61. See Priest, *supra* note 9, at 828; Peter K. Yu, *supra* note 59, at 220.

62. See Priest, *supra* note 9, at 828–29. For an indication of relatively poor economic conditions, consider that China still ranks ninetieth in the world in gross national income per capita. *China Overview*, THE WORLD BANK, <http://www.worldbank.org/en/country/china/overview> (last visited May 7, 2014).

63. See Priest, *supra* note 9, at 828–29.

that China is already the most IP-litigious society in the world.⁶⁴ Moreover, almost ninety-eight percent of all IP litigation in China involves only Chinese parties; in 2011, a mere 2.27 percent of IP cases disposed by Chinese courts involved a foreign party.⁶⁵ These statistics suggest that many Chinese entities now value obtaining and protecting IP rights and believe that enforcing those rights is in their best interests.

Likewise, there is little evidence that high piracy rates directly correlate with poor economic conditions, or that piracy rates decrease as economic circumstances improve. In fact, a recent study by the China Publishing Science Research Institute suggests that wealthy and educated Chinese consume as much or more pirated content than the poor and less educated.⁶⁶ More than half of those surveyed holding college and graduate degrees purchased pirated content.⁶⁷ Likewise, by profession, farmers, laborers, and military personnel were less likely to buy pirated goods than enterprise leaders, management, and professionals, of whom nearly sixty percent bought pirated goods.⁶⁸ Lit-literacy and awareness of copyright infringement issues are likely important variables in the study, but these statistics suggest the majority of educated professionals buy pirated content.⁶⁹ This casts doubt on the hypothesis that China's economic conditions prolong endemic piracy.

In short, piracy's root causes evade simple explanations and solutions, and piracy remains a serious obstacle to the successful monetization of creative works.

64. See RICHARD P. SUTTMEIER AND XIANGKUI YAO, NAT'L BUREAU ASIAN RES., SPECIAL REP. NO. 29, CHINA'S IP TRANSITION: RETHINKING INTELLECTUAL PROPERTY RIGHTS IN A RISING CHINA 13 (2011).

65. See ZHONGHUA RENMIN GONGHEGUO ZUIGAO RENMIN FAYUAN (中华人民共和国最高人民法院)[SUP. PEOPLE'S CT.], ZHONGGUO FAYUAN ZHISHI CHANQUAN SIFA BAOHU ZHUANGKUANG (中国法院知识产权司法保护状况 (2011年)) [INTELLECTUAL PROPERTY PROTECTION BY CHINESE COURTS IN 2011] 26-27 (2012), available at http://chineseip.jmls.edu/sites/en/sites/default/files/2011_CN_IP_Whitepaper.doc (reporting that in 2011, the number of civil IP cases accepted for trial in China totaled 59,612; those disposed totaled 58,201, of which just 1321 (about 2.27 percent) involved foreign parties, a decline of more than three percent from the previous year).

66. ZHONGGUO CHUBAN KEXUE YANJIUSUO (中国出版科学研究所) [Chinese Publishing Science Research Institute], QUANGUO GUOMIN YUEDU DIAOCHA BAOGAO (2008) (全国国民阅读调查报告(2008)) [China's National Reading Survey Report (2008)] 257 (2008).

67. *Id.*

68. *Id.* at 256.

69. See, e.g., Creemers, Explaining Audiovisual Media Piracy, *supra* note 9, at 32 (citing a 2006 study of consumers in Hong Kong, Wuhan and Shanghai finding that "[h]eavy purchasers of pirated DVD discs tend to be males, with tertiary education in white-collar occupations" and that this "tendency is strongest in Hong Kong, followed by Shanghai and Wuhan"); Priest, *supra* note 9, at 829 (noting that because pirated goods are always cheaper than their legitimate counterparts, and because the quality of pirated goods continues to improve and close the gap with legitimate goods, "improved economic conditions alone will not suffice to wean even well-to-do Chinese consumers off cheap pirated goods").

zation of creative works in China. For their part, copyright owners in China focus on the pragmatics of how to subsist as copyright extremophiles, surviving in inhospitable conditions.

III. THE CHINESE FILM AND MUSIC INDUSTRY ECOSYSTEM: EXCLUSION ECONOMICS, CENSORSHIP, AND PROTECTIONISM

A. Introduction

Despite the extremely challenging piracy conditions outlined in Part II, the situation for some copyright owners in China has been improving. Greater copyright enforcement is not a sufficient explanation for this improved situation. Though a few Chinese copyright owners have achieved directly beneficial results through traditional copyright enforcement measures — filing lawsuits and initiating administrative enforcement actions — the creative industries in China have monetized their works primarily through alternative, non-copyright based models. To understand how piracy affects these industries, it is important to understand their business and regulatory environments. This Section, therefore, provides an overview of the business and regulatory environments in which China's music and film industries operate. In particular, it highlights three defining characteristics of their business models and environments: exclusion economics, censorship, and protectionism.

Exclusion economics: The ability to exclude is usually crucial to the monetization of film and musical works. Therefore, in the absence of effective *legal* exclusion in the form of a functioning copyright system, most revenue is derived from services based on physical or technological exclusion. Both the music and film industries in China follow that model, deriving ninety percent of their revenues from excludable services that do not directly rely on copyright exploitation — box office receipts in the film industry (physical exclusion)⁷⁰ and wireless music service downloads, such as ringback tones, in the music industry (technological exclusion).⁷¹ Can copyright owners offset lost revenue from declining DVD, CD, and digital download sales by employing excludable services that do not rely directly on copyright

70. See OFFICE OF THE U.S. TRADE REP., 2013 SPECIAL 301 REPORT 35 (2013) [hereinafter OFFICE OF THE U.S. TRADE REP., 2013 SPECIAL 301 REPORT] (reporting that “90 percent of the revenue generated by U.S. films in China comes in the form of box office revenues, compared to 25–30 percent in the United States”).

71. Francis Tan, *Online Music Sales in China up by 14 Percent*, NEXT WEB (Mar. 10, 2011, 6:53 AM), <http://thenextweb.com/asia/2011/03/10/online-music-sales-in-china-up-by-14/> (referring to 2011 MOC report). This is the case in the music industry despite the fact that the vast majority of ringback tone gross revenues actually accrue to mobile providers, not copyright owners. See *infra* Part III.C.1.c.

exploitation and therefore are less susceptible to illicit copying?⁷² The answer in China is that under current conditions, box office revenue is sufficient to fuel film industry growth, while ringback tone revenue is insufficient to fuel music industry growth. As this Article argues in Part V, piracy remains the biggest hindrance to music industry growth and has significant detrimental effects on the film industry as well, despite that industry's present growth.

Both the film and music industries have, however, begun to benefit from the emergence of copyright licensing revenue from online services. This new but relatively small revenue stream does not rely on physical or technological exclusion. Rather, it relies on legal exclusion via an increasingly functional copyright regime for the protection of content online. This new revenue stream could represent a first step in the evolution of music and film industry business models to include copyright-based revenue streams, but it will be extremely difficult for these revenue streams to reach their potential while so many sources of free, unlicensed content remain available.

Censorship and protectionism: The content industries are inextricably bound up with Chinese politics and state information control policies.⁷³ Producers, importers, and distributors of music and audiovisual works in China engage in politically sensitive activities — i.e., producing and disseminating information — and are therefore strictly regulated and scrutinized by Chinese authorities.⁷⁴ Chinese authorities view cultural products as inherently ideological and therefore subject to strict state control.⁷⁵ Government regulations define what content is culturally or politically appropriate, restrict whether certain types of content may be produced, imported, or distributed, and determine whether private domestic or foreign investment is allowed.⁷⁶

Censorship in China's entertainment industries has two predominant effects. First, it helps China's one-party state keep seditious and socially objectionable content (however the state chooses to define those terms) out of public view.⁷⁷ Second, it establishes legal barriers to foreign participation in content production and distribution. This ostensibly carves out space for domestic creative industries to avoid

72. For a discussion of this debate, see, for example, Sean A. Pager, *Accentuating the Positive: Building Capacity for Creative Industries into the Development Agenda for Global Intellectual Property Law*, 28 AM. U. INT'L L. REV. 223, 268 (2012), and Mark F. Schultz, *Live Performance, Copyright, and the Future of the Music Business*, 43 U. RICH. L. REV. 685, 694–701 (2009).

73. See generally Creemers, Explaining Audiovisual Media Piracy, *supra* note 9, at 122–43; MONTGOMERY, *supra* note 1, at 72–73.

74. See *infra* Parts III.B.2, III.C.2.

75. See *infra* Parts III.B.2, III.C.2.

76. See *infra* Parts III.B.2, III.C.2.

77. See Creemers, Explaining Audiovisual Media Piracy, *supra* note 9, at 113–14.

being overrun by imports,⁷⁸ even though such space no longer appears necessary for domestic industries to compete, if it ever was.⁷⁹ Foreign copyright owners have long complained that piracy is exacerbated by Chinese regulations that permit only certain state-owned Chinese companies to distribute audiovisual and musical works in China, that require official approval of content, and that permit Chinese authorities to set film release dates.⁸⁰ Such rules, they contend, delay or frustrate their ability to distribute their works, giving pirates a comfortable head start from which it is virtually impossible for copyright owners to recover, and giving an unfair advantage to domestic industries that do not have to contend with such a long pre-release delay.⁸¹

78. See MONTGOMERY, *supra* note 1, at 65 (discussing the protectionist effects of censorship policies in China's music industries). Some experts argue that there is little if any protectionist agenda underlying media control regulations, such as the annual thirty-four film import quota, *see infra* Part III.B.2, and that the impetus behind them is primarily if not entirely information control. *See* Creemers, Explaining Audiovisual Media Piracy, *supra* note 9, at 189 ("Even where there is an obvious international aspect, where the question on how to deal with foreign media products is discussed, the barriers to entry for foreign products are not protectionist measures as narrowly defined."); Mathew Alderson, *Protecting Hollywood Films in China Makes Sense for China*, CHINA L. BLOG, (Sept. 12, 2011), http://www.chinalawblog.com/2011/09/protecting_hollywood_films_in_china_makes_sense_for_china.html ("It is not the local Chinese film industry that wants to stop foreign films. Far from it."); Dan Harris, *There Is No Protectionism in China*, CHINA L. BLOG, (Nov. 12, 2011), http://www.chinalawblog.com/2011/11/there_is_no_protectionism_in_china.html (arguing that the foreign film quota is a censorship rule, not a protectionist rule, because the Chinese government does not especially care about protecting the business interests of the Chinese film industry, but rather "cares almost exclusively about the Chinese government"). Nevertheless, some acts of content control seem overtly protectionist. For example, the government manipulates film release dates in what are widely regarded even in China as protectionist measures, pitting Hollywood blockbusters directly against one another at certain times, and at other times ensuring that domestic films have no foreign competition at all. *See, e.g.*, Ben Fritz et al., *In China, Hollywood Blockbusters Face Off on Same Days*, L.A. TIMES, Aug. 28, 2012, <http://articles.latimes.com/2012/aug/28/entertainment/la-et-ct-china-movies-20120828>. Even Chinese media referred to June and July 2012 as "domestic movie protection month" because theaters nationwide in China screened only domestic productions for nearly two months. *See* Wei Xi, *Belay for Hollywood*, GLOBAL TIMES, June 4, 2013, at P19, available at http://www.globaltimes.cn/content/786370.shtml#Uz_NmVIZ_jM (describing the domestic-film-only period of June–July 2012 but noting that the "self-evident domestic protection manner is looser [in 2013] than 2012" because of better box office performance by Chinese films in 2013).

79. *See infra* Part V.F.

80. OFFICE OF THE U.S. TRADE REP., 2013 NATIONAL TRADE ESTIMATE REPORT ON FOREIGN TRADE BARRIERS 87–88 (2013) [hereinafter OFFICE OF THE U.S. TRADE REP., 2013 REPORT ON FOREIGN TRADE BARRIERS]. The United States successfully mounted a WTO challenge to another contentious provision that copyright owners argued exacerbated piracy: Article Four of China's Copyright Law, which altogether denied copyright protection to unapproved works. Report of the Panel, *supra* note 43.

81. *See, e.g.*, OFFICE OF THE U.S. TRADE REP., 2013 REPORT ON FOREIGN TRADE BARRIERS, *supra* note 80, at 87–89.

B. China's Film Industry

1. Exclusion Economics

a. The Box Office Boom

The film industry, which has been expanding by leaps and bounds, is the most visible of the copyright industries experiencing growth in China. In 2005, box office revenue in China totaled a mere \$248 million;⁸² by 2008 it had nearly tripled to \$630 million,⁸³ and in 2012 it soared to \$2.74 billion, thrusting China into its position as the world's second largest box office.⁸⁴ To keep up with demand, China has furiously added theater screens at the pace of eight to ten per day.⁸⁵ By 2011, China had 10,700 screens nationwide,⁸⁶ many of which contained digital projectors.⁸⁷ However, there remains significant room for further growth, since China has only one-third the number of film screens of the United States despite China's much larger population.⁸⁸ At its current pace, China will eclipse the United States as the world's largest film market by 2018.⁸⁹

82. See Priest, *supra* note 9, at 798.

83. Patrick Brzeski & Pamela McClintock, *How Hollywood Can Break Through China's Box Office*, HOLLYWOOD REP. (Mar. 9, 2012 5:28 PM PST), <http://www.hollywoodreporter.com/news/china-trade-deal-hollywood-box-office-revenue-297719>.

84. *China Is World's 2nd Largest Film Market*, CHINA DAILY EUROPE (Jan. 9, 2013, 7:00 PM), http://europe.chinadaily.com.cn/business/2013-01/09/content_16100261.htm; see also Clifford Coonan, *China's 2011 Box Office Take Tops \$2 Billion*, VARIETY (Jan. 10, 2012, 6:23 PM PT), <http://www.variety.com/article/VR1118048424>; Pamela McClintock, *China Box Office Revenue Hits \$2.7 Billion in 2012, Second Only to North America*, HOLLYWOOD REP. (Mar. 21, 2013, 1:15 PM), <http://www.hollywoodreporter.com/news/china-box-office-revenues-hit-430267> ("Box office revenue reached a staggering \$2.7 billion in China in 2012, even more than expected and up 37 percent year over year."). It should be noted that box office figures in China are notoriously dubious due to widespread reporting scams by exhibitors and distributors. See Raymond Zhou, *Cinema Scams*, CHINA DAILY USA (Feb. 26, 2014, 08:47), http://usa.chinadaily.com.cn/epaper/2014-02/26/content_17306872.htm. However, industry insiders believe that, if anything, revenues are underreported. *Id.*

85. See Alexis Lai, *Blockbuster Growth in China's Film Industry*, CNN (Feb. 19, 2013, 11:46 PM), <http://www.cnn.com/2013/02/19/world/asia/china-film-industry-advancer>.

86. Zheng Yangpeng, *China's Movie Sector Becomes 2nd-Largest*, CHINA DAILY, Apr. 13, 2012, 10:37, http://www.chinadaily.com.cn/bizchina/2012-04/13/content_15040274.htm.

87. Coonan, *supra* note 84.

88. Jonathan Landreth, *Hollywood and China: In Figures*, THE ATLANTIC (Nov. 7, 2013, 7:00 AM ET), <http://www.theatlantic.com/china/archive/2013/11/hollywood-and-china-in-figures/281222/> (reporting that the United States had 39,662 screens and China had 13,118).

89. See Pamela McClintock & Kim Masters, *Hollywood Studios Haven't Been Paid by China in Months (Exclusive)*, HOLLYWOOD REP. (July 29, 2013, 3:11 PM PDT), <http://www.hollywoodreporter.com/news/hollywood-studios-havent-been-paid-594939>.

China's importance to Hollywood is difficult to overstate.⁹⁰ China can be a lucrative market for foreign producers whose films are approved for theatrical release.⁹¹ Foreign films — particularly Hollywood blockbusters — have had success at the box office in China and now account for about half of Chinese box office revenues.⁹²

A healthy box office is vital to the success of China's film industry. Due in part to piracy, the vast majority of film industry revenue in China is generated from theatrical distribution, which monetizes the movie-going experience rather than the sale of copyrighted products.⁹³ The theatrical experience is easy to monetize because it excludes non-paying customers from the premises and is difficult for unauthorized providers to replicate, especially now that Chinese consumers are accustomed to viewing movies in state-of-the-art cinemas with stadium seating and digital 3D projection.⁹⁴

Despite the rapid growth in China's box office revenues, copyright piracy remains a vexing problem for the film industry. Piracy undercuts box office revenues because many consumers will not pay to watch popular first-run movies in the theater when pirated copies are cheaply or freely available for home or mobile viewing.⁹⁵ Piracy also has a significant impact on aftermarket revenues, such as DVD and Blu-Ray sales.⁹⁶ The inability to stem offline and online piracy to a point that would permit development of a viable market for physical media, or legitimate online movie distribution (until a few years ago), left copyright owners of audiovisual works with virtually no aftermar-

90. See, e.g., Beh Lih Yi, *China's Just the Ticket for Studios' Future*, CHINA DAILY, Apr. 9, 2012, http://www.chinadaily.com.cn/bizchina/2012-04/09/content_15002468.htm (commenting on Hollywood's interest in China's booming movie industry in light of slowdown in North America).

91. See *infra* Part III.B.2.

92. See Melanie Lee, *Hollywood Studios Find Online Channels Key to China*, CHINA DAILY, Aug. 9, 2011, 8:37, http://usa.chinadaily.com.cn/us/2011-08/09/content_13074501.htm (“Although they form a small percentage of movies screened, Hollywood films drew 44 percent of all 10 billion yuan in sales receipts in 2010.”).

93. See Zheng Yangpeng, *supra* note 86 (stating that box office receipts account for ninety percent of film industry revenues in China, as compared with the United States where they account for just thirty percent of a film's gross revenue).

94. See Coonan, *supra* note 84 (noting that “[o]f the 803 cinemas that opened [in China in 2011], 90% were equipped with digital projectors”); Frank Langfitt, *What a Show! China's Movie Theaters Have Improved Dramatically*, WGBH (May 25, 2012, 11:34 AM), <http://www.wgbhnews.org/post/what-show-chinas-movie-theaters-have-improved-dramatically> (describing the author's trip to a Shanghai movie theater with “stadium seating, assigned seats, three-story screen and English with Chinese sub-titles,” and concluding that the experience was “as good as anything you would find in a Western, post-industrial country and probably better than some”).

95. Priest, *supra* note 9, at 828–29.

96. See Dan Levin & John Horn, *DVD Pirates Running Rampant in China*, L.A. TIMES, Mar. 22, 2011, <http://articles.latimes.com/2011/mar/22/entertainment/la-et-china-piracy-20110322> (describing the detrimental effects piracy has had on legitimate aftermarket sales in China, and quoting one Chinese home video consumer as saying, “Legal DVDs are like democracy — they don't exist in China”).

ket revenue in China.⁹⁷ This represents significant loss; in the United States, aftermarket revenue from DVD sales and television distribution rights can exceed \$100 million for a single major film.⁹⁸

b. The Growth of Internet Video

Fortunately, in the past few years, the prospects for generating aftermarket revenue in the online video space have improved. Before 2009, Chinese online video services such as industry leaders Youku and Tudou were notorious for serving full-length, unlicensed and unremunerated movies and television shows, both domestic and foreign, together with UGC.⁹⁹ With pirated premium content readily available for free, online license fees for film and TV programs were meager.¹⁰⁰ The market for online content licenses has improved dramatically, however, with online video piracy on China's major UGC video streaming websites experiencing a remarkable downturn.¹⁰¹ The sites began to purge pirated content primarily due to their perception that major international brands, which were key advertisers on the video sites, had grown concerned about underwriting and being associated

97. Zheng Yangpeng, *supra* note 86 (contrasting “overwhelming dependence” on box office receipts in China with United States aftermarket revenues that amount to as much as seventy percent of a film’s gross revenues and come primarily from DVD sales and television distribution). “[C]ontent theft,” according to Mike Ellis, Asia-Pacific president of the Motion Picture Association of America, “has prevented China from developing a film industry value chain based on copyright trade.” *Id.* For an example of the type of online video piracy site that continues to plague the movie industry, see Sophie Song, *China Closes Giant Movie Downloading Website, Accusing It of Being Nation’s Largest Illegal Such Service; Other Movie Piracy Sites Voluntarily Shut Down*, INT’L BUS. TIMES (Apr. 26, 2013, 11:10 AM), http://www.ibtimes.com/china-closes-giant-movie-downloading-website-accusing-it-being-nations-largest-illegal-such-service#_jmp0 (detailing how authorities shut down China’s “largest illegal high-definition movie downloading site” that boasted a workforce of more than 100 employees and was earning as much as \$135 million annually from 1.4 million subscribers who each paid a monthly fee of \$8 to access unlimited downloads from the site’s more than 10,000 high quality HD films and television dramas).

98. Charlie Jane Anders, *How Much Money Does a Movie Need To Make To Be Profitable?*, 109 (Jan. 31, 2011, 2:24 PM), <http://io9.com/5747305/how-much-money-does-a-movie-need-to-make-to-be-profitable>.

99. See, e.g., Bruce Einhorn, *The YouTube of China Goes Legit*, BLOOMBERG BUS. WK., Apr. 4, 2011, at 44, 47. (“Youku launched in 2006 as a local version of YouTube, which China’s censors have long banned, and quickly became a premier place to download pirated movies and TV shows.”).

100. See Wang Fei’er, *The Copyright Clash*, GLOBAL TIMES, Jan. 12, 2012, 13:53, <http://www.globaltimes.cn/content/691864.shtml> (noting that in 2009 it cost websites a mere 10,000 RMB (approximately \$1500) per episode to license the most popular television show in China at the time).

101. See Clifford Coonan, *‘Saturday Night Live’ Launches on Chinese Video Site Sohu*, HOLLYWOOD REP. (Jan. 2, 2014, 12:03 AM PST), <http://www.hollywoodreporter.com/news/saturday-night-live-launches-chinese-668177> (quoting Charles Zhang, CEO of Chinese Internet giant Sohu.com, as saying that “for domestic TV drama and American TV series, the majority of the Chinese audience is now watching legitimate content . . . This is an industry with law and order.”).

with pirated content.¹⁰² The situation came to a head in 2009 when Coca-Cola and PepsiCo were sued as contributory copyright infringers after ads for their products were associated with unlicensed videos on Youku.¹⁰³

Concerned about their relationships with their biggest advertisers, Youku, Tudou, and other online video portals proactively purged their services of unlicensed content, have sought exclusive licenses from copyright owners, and have been willing to pay top dollar for them.¹⁰⁴ A content licensing bubble has developed, in which the market price for online licenses of popular Chinese television series experienced as much as a one-hundred-and-eighty-fold increase in just two years.¹⁰⁵ Content acquisition accounted for one-half of Youku's total expenditures in 2012, as Youku paid out over \$100 million in content licensing fees to Chinese and foreign copyright owners,¹⁰⁶ including Hollywood studios.¹⁰⁷ The content licensing bubble comes as a wind-

102. See Eric Priest, *Acupressure: The Emerging Role of Market Ordering in Transnational Copyright Enforcement* 37–38 (Apr. 21, 2014) (unpublished manuscript) (on file with author); see also Loretta Chao, *Top China Video Site Steps Up Its Piracy Fight*, *supra* note 18 (“Youku is betting [that its] new [antipiracy technology] will help it improve its reputation among advertisers who don’t want to be associated with piracy. That association can be risky. Last year, an antipiracy group of Chinese Internet companies filed a number of lawsuits against Youku in Chinese courts, including one that alleged that a Coca-Cola Co. ad had run on Youku accompanying a clip from a Chinese TV show that Youku hadn’t licensed.”). Several other factors probably helped motivate the Chinese video websites’ reduction in pirated content, but none satisfies as the primary explanation for the change. These factors include that the websites: (1) were concerned about copyright liability and litigation and therefore decided to “clean up their acts”; (2) buckled under pressure from Chinese authorities; (3) sought to burnish their reputations ahead of initial public offerings in the United States; and (4) were motivated to improve copyright compliance because they viewed subscription and on-demand, pay-per-view content delivery as an important next-stage business model. See Priest, *supra*, at 14–22 (discussing each of these factors and explaining why it was not the primary motivation for Chinese video websites to purge unlicensed content).

103. See Wang Xing, *Web Video Piracy War Heats Up*, CHINA DAILY, Sept. 29, 2009, http://www.chinadaily.com.cn/bw/2009-09/28/content_8744294.htm#_jmp0; Loretta Chao, *Top China Video Site Steps Up Its Piracy Fight*, *supra* note 18.

104. See Priest, *supra* note 102, at 14–22.

105. The price for online licenses for popular Chinese shows increased from 10,000 RMB (approximately \$1500) per episode in 2009 for the most popular show of that year to more than 1.85 million RMB (approximately \$270,000) per episode for one of the most popular shows of 2011. See Wang Fei'er, *supra* note 100. The high-water mark was \$320,000 per episode, paid by Baidu-owned video portal Qiyi.com for a top-rated Chinese drama. Simon Montlake, *Go Big or Go Home*, FORBES, Dec. 10, 2012, at 52.

106. See Montlake, *supra* note 105; YOUKU TUDOU INC., FORM 20-F: ANNUAL REPORT PURSUANT TO SECTION 13 OR 15 (D) OF THE SECURITIES EXCHANGE ACT OF 1934 FOR THE FISCAL YEAR ENDED DECEMBER 31, 2012 74 (Apr. 26, 2013) [hereinafter YOUKU TUDOU INC., 2012 ANNUAL REPORT].

107. See Steven Millward, *Youku Inks Deal with Warner Bros. Will Add 400+ Premium Titles*, TECHINASIA (June 28, 2011, 5:30 PM), <http://www.techinasia.com/youtu-warner-bros-deal/> (reporting on deal signed between online video site Youku.com and Warner Home Entertainment by which Youku acquired licenses to 400 to 450 Warner Bros. titles to Youku's pay-per-view premium site, although not providing information on the licensing fees).

fall for video copyright owners who, just a few years earlier, had no options for meaningful aftermarket earnings.¹⁰⁸

The growth in licensed video online also presents an opportunity for independent filmmakers. Short films called “micro movies” — so-named because they are short and promoted through micro-blogging services — have become immensely popular in China.¹⁰⁹ Micro movies are produced on a low budget in a short time frame (typically within a few days), and are distributed for free via online video portals.¹¹⁰ The immense popularity of micro movies online and the low barriers to entry have provided new, inexperienced directors with a platform for professional development and self-promotion.¹¹¹ Micro movies currently generate revenue for producers through advertisements, either through revenue sharing with video portals or through product placement advertisements.¹¹²

2. Censorship and Economic Protectionism

a. Production and Market Access Restrictions

The film industry’s transition from a centralized, state-funded production model to a market-based production model has set the stage for a gradual expansion of the scope of acceptable content. Until 2002, only state-owned entities could produce feature films, which was a holdover from the days when film was primarily a propaganda tool.¹¹³ Today, private entities (other than wholly foreign-owned enti-

108. See Clifford Coonan, *Hollywood’s New Chinese Gold Mine: Youku Tudou*, HOLLYWOOD REP., Aug. 30, 2013, at 36. Even though Youku merged with Tudou largely to reduce the price-inflating competition for exclusive content licenses, see Montlake, *supra* note 105, the bubble has not yet burst. See YOUKU TUDOU INC., 2012 ANNUAL REPORT, *supra* note 106, at 74 (“[T]he average [Youku] license fee for both television serial dramas and movies increased in 2012 by more than 203% as compared to 2011.”). However, consolidation among online video portals, as well as the fact that major portals such as Youku remain unprofitable, may mean video license price inflation will slow down, likely sooner rather than later. See Montlake, *supra* note 105.

109. See Clarissa Sebag Montefiore, *Micro Movies Beat China’s Censors*, BBC (Aug. 12, 2013), <http://www.bbc.com/culture/story/20130812-micro-movies-beat-chinas-censors>; Tang Lei, *Micro-Movies Move Toward Mainstream*, NEWS CHINA (Jan. 2012), <http://www.newschinamag.com/magazine/move-toward-mainstream>.

110. See Montefiore, *supra* note 109; Tang Lei, *supra* note 109.

111. See Tang Lei, *supra* note 109 (citing @Who Who, a micro movie that attracted more than ten million views in the first few days after its release); Press Release, Youku Tudou Inc., Tudou Video Festival Empowers UGC Talents with Sponsors and Marketing Support (June 13, 2013), available at <http://online.wsj.com/article/PR-CO-20130613-904937.html> (announcing Tudou.com’s new fund and revenue-sharing program for users “who [can] apply [to] . . . receive extensive financial, technical, and marketing support, including having their videos prioritized in search results on Tudou”).

112. See Tang Lei, *supra* note 109; Press Release, Youku Tudou Inc., *supra* note 111.

113. See Dianying Guanli Tiaoli (电影管理条例) [Film Administrative Regulations] (promulgated by the St. Council, Dec. 25, 2001, effective Feb. 1, 2002) (Westlaw Chi-

ties) are eligible to produce feature films in China, but the process remains highly regulated via state permitting requirements.¹¹⁴ Likewise, a latticework of regulations governs who can produce television content and what type of content they can produce.¹¹⁵ Private enterprises other than wholly foreign-owned enterprises may establish television production operations in China, but must receive approval from the State Administration of Radio, Film, and Television (“SARFT”) to produce a television program.¹¹⁶

Some areas of the film business remain off limits to private enterprise. In particular, SARFT tightly controls the importation and distribution of foreign films.¹¹⁷ State-owned China Film Group (“CFG”) and state-owned Huaxia Film Distribution exclusively possess SARFT-conferred licenses to distribute foreign films in China.¹¹⁸ In 2007, the United States mounted a largely successful WTO challenge (“*China — Publications and Audiovisual Products*”) against Chinese regulations restricting foreign participation in the market for importation and distribution of copyrighted works, including films for theatrical release and audiovisual home entertainment products.¹¹⁹ Despite this victory, China has at best only partially complied with the WTO ruling.¹²⁰

Censorship rules greatly limit the number of revenue-sharing foreign films imported for theatrical release.¹²¹ The thirty-four import

na万律 (Westlaw China)), art. 8 (China) [hereinafter Film Administrative Regulations]; Creemers, Explaining Audiovisual Media Piracy, *supra* note 9, at 100.

114. Radio and Television Program Production Business Management Regulations (promulgated by the State Admin. of Radio, Film and Television, Jul. 19, 2004, effective Aug. 20, 2004), art. 5 (China), *translated in* CHINA COPYRIGHT AND MEDIA, <http://chinacopyrightandmedia.wordpress.com/2004/07/19/radio-and-television-programme-production-business-management-regulations> (last visited May 7, 2014).

115. *Id.* Production of news programming is strictly limited to a narrow range of approved government entities, *id.* art. 21, while the range of potential producers of television dramas is broader but still closely regulated. *Id.* arts. 23–30.

116. *Id.* art. 5.

117. Shalia Sakona, *Frankly, My Dear America, We Don't Give a Damn: Comparing Chinese and European Trade Barriers to American Audiovisual Works and the American Response*, 54 B.C. L. REV. 1385, 1390 (2013).

118. *Id.*

119. Report of the Panel, *China — Measures Affecting Trading Rights and Distribution Services for Certain Publications and Audiovisual Entertainment Products*, WT/DS363/R (Aug. 12, 2009).

120. See OFFICE OF THE U.S. TRADE REP., 2013 SPECIAL 301 REPORT, *supra* note 70, at 26. The United States stopped pressing the issue at the WTO when China signed a Memorandum of Understanding in which China agreed to increase market access for foreign films (though not for film distributors) and increase the revenue share for foreign film owners. See OFFICE OF THE U.S. TRADE REP., 2013 REPORT ON FOREIGN TRADE BARRIERS, *supra* note 80, at 68.

121. See Scott Ross, *Biden Convinces China To Grant Hollywood Greater Access*, NBC NEW YORK (May 30, 2012, 2:46 PM EST), <http://www.nbcnewyork.com/blogs/popcornbiz/Biden-China-Hollywood-139709713.html>. The thirty-four foreign film quota applies only to revenue-sharing theatrical releases. See Creemers, Explaining Audiovisual Media Piracy, *supra* note 9, at 113. The limit would not apply to films distributed in China

slots currently available are highly coveted and often go to established studios and blockbuster films.¹²² Hollywood film studios touted their 2012 Memorandum of Understanding, in which the Chinese government increased the number of annual slots from twenty to thirty-four and increased the foreign film box office revenue share to twenty-five percent.¹²³ The quota increase will only subtract screen time and revenue from other foreign films, however, as SARFT still requires theaters to allot two-thirds of their screen time to domestic productions.¹²⁴

b. Content Restrictions

Unsurprisingly, even entities that obtain state approval to produce audiovisual content are not afforded *carte blanche*. Every project must undergo official content review through submission of a script outline to SARFT before production commences.¹²⁵ SARFT officials have sweeping discretionary power to censor audiovisual productions based on verboten political or social content.¹²⁶ For example, films that, in the authorities' view, contain content or subject matter that is seditious, divulges state secrets, endangers national security, incites hatred or discrimination, "propagates evil cults or superstition," or disturbs the public order, are disallowed.¹²⁷ In addition, films cannot contain elements that criticize revolutionary heroes or important historical figures or works of literature, nor can films "maliciously" criticize the People's Liberation Army or other public security or judicial organs.¹²⁸ Officials are not merely concerned with curtailing politically sensitive expression; the regulations also incorporate a powerful strain of paternalistic social censorship.¹²⁹ For example, regulations require filmmakers to edit or revise films containing "intermittent" sexual content including promiscuity, sexual behavior, homosexuality, and

under a non-revenue-sharing agreement, such as a flat-fee arrangement. *Id.* This is a far less desirable arrangement for filmmakers than revenue-sharing deals, however, even if China is below the international standard revenue-sharing rate. *Id.*

122. See, e.g., Brzeski & McClintock, *supra* note 83; Ross, *supra* note 121.

123. See Brzeski & McClintock, *supra* note 83. The prior revenue share for foreign films ranged from thirteen to seventeen percent. See McClintock & Masters, *supra* note 89.

124. Film Administrative Regulations, *supra* note 113, art. 44.

125. *Id.* art. 13.

126. See Dianyingjuben (Genggai) Beian, Dianyingpian Guanli Guiding (电影剧本(梗概)备案、电影片管理规定) [Film Script (Outline) Filing, Film Management Regulations] (promulgated by the St. Admin. of Radio, Film, and Television, Apr. 3, 2006, effective June 22, 2006) arts. 4, 14 (China) [hereinafter Film Script (Outline) Filing], translated in CHINA COPYRIGHT AND MEDIA, <http://chinacopyrightandmedia.wordpress.com/2006/05/22/film-script-outline-filing-film-management-regulations> (last visited May 7, 2014).

127. *Id.* art. 13.

128. *Id.* art. 14.

129. *Id.*

“filthy lines, songs, background music and sound effects.”¹³⁰ Paternalism in SARFT’s censorship rules is further apparent in regulations requiring the editing or revision of films that contain “intermittent content such as murder, violence, terror, monsters, occultism, etc., value orientations reversing true and false, good and bad, beauty and ugliness, blurring the basic nature of righteousness and unrighteousness,” and even “excessively displaying excessive drinking, smoking and other bad habits.”¹³¹

The approval and review process is not the only tool Chinese authorities use to control content. In addition to the “stick” of content review and affirmative censorship practices, authorities shape the production of audiovisual content by providing the “carrot” of incentives for producing works that promote party objectives.¹³² Such incentives include subsidies and favorable release windows.¹³³

Although regulations such as the film script rules quoted above may appear sweeping and unfathomably restrictive on their face, SARFT does not always enforce them to the letter. SARFT stakes out its territory in advance by announcing sweeping content restrictions, expressly reserving the right to enforce them strictly but doing so at its pleasure.¹³⁴ Foreign and domestic producers and distributors are all on notice about what constitutes acceptable film content, but SARFT’s application of the rules is inconsistent, nontransparent, and subjective.¹³⁵ One recent example involves the 2012 science fiction blockbuster film *Looper*, a Sino-American joint production involving time-traveling hit men.¹³⁶ *Looper* appears to repeatedly violate SARFT rules by portraying graphic violence, murder, and mayhem — some of

130. *Id.*

131. *Id.* Indeed, the prohibition on horror and monsters in film is quite detailed in practice. Films cannot portray real ghosts because that encourages superstition, so ghosts in Chinese films can only appear in dreams, imagination, or if real individuals pretend to be ghosts as an element of the plot. See Li Anlan, *Why Scary Chinese Movies Are So Scarce*, SHANGHAI DAILY, Oct. 30, 2012, at B1, available at <http://www.shanghaidaily.com/feature/Why-scary-Chinese-movies-are-so-scarce/shdaily.shtml>. There is, however, an exception to the rule: ghosts and monsters are permitted if portrayed in film adaptations of classical literary works that contain such horrors. *Id.*

132. See Creemers, *Explaining Audiovisual Media Piracy*, *supra* note 9, at 93.

133. *Id.* Going too far to shape one’s production to please censors and secure government backing and incentives can be counterproductive for producers if the content ends up being dry or unappealing. Consider, for example, the cautionary tale of the 2013 film *Young Lei Feng*, chronicling apocryphal events in the life of a famed communist revolutionary hero. Screening of the state-backed propaganda film was terminated in cinemas in several major Chinese cities after the film “failed to sell a single ticket.” Clarence Tsui, *Chinese Cinemas Cancel Propaganda Film Screenings*, HOLLYWOOD REP. (Mar. 5, 2013, 11:31 PM PST), <http://www.hollywoodreporter.com/news/chinese-cinemas-cancel-propaganda-film-426236>.

134. See OFFICE OF THE U.S. TRADE REP., 2013 REPORT ON FOREIGN TRADE BARRIERS, *supra* note 80, at 87–89.

135. *See id.*

136. See Simon Montlake, *Hollywood’s China Fixer*, FORBES, Nov. 19, 2012, at 126.

which occurs in Shanghai in the year 2074.¹³⁷ Indeed, even time travel plot elements raise SARFT's ire,¹³⁸ violating SARFT dictates that prohibit the "twisting" of culture and history and "violat[ion]" of historical facts.¹³⁹ Nevertheless, as a local co-production,¹⁴⁰ *Looper* underwent, and passed, SARFT's obligatory pre- and post-production censorship reviews, and was released in cinemas throughout China — murder, mayhem, and time travel notwithstanding.¹⁴¹

Why are films such as *Looper* permitted to screen in China?¹⁴² Perhaps in this case, censorship concerns were outweighed by the Chinese government's interest in boosting cultural production and cultural exports,¹⁴³ which could be appeased with the release of a

137. *LOOPER* (Endgame Entertainment 2012); see also Zhang Zihan, *Hasta La Vista, Maybe?*, GLOBAL TIMES, Oct. 14, 2012, <http://www.globaltimes.cn/content/738191.shtml>.

138. See Gregg Goldstein, *Producer's China Endgame Goes Well*, VARIETY, Oct. 8, 2012, at 10. In 2011, SARFT publicly purported to enforce a prohibition against time travel stories in TV and film. See Guangdian Zongju Guanyu 2011 Nian 3 Yue Quan Guo Paishe Zhizuo Dianshiju Beian Gongshi De Tongzhi (广电总局关于2011年3月全国拍摄制作电视剧备案公示的通知) [Notice Concerning the Nationwide Television Drama Shooting Filing Announcement for March 2011] (promulgated by the St. Admin. of Radio, Film, and Television, Mar. 29, 2011, effective Mar. 29, 2011) (China), translated in CHINA COPYRIGHT AND MEDIA, <http://chinacopyrightandmedia.wordpress.com/2011/03/29/notice-concerning-the-nationwide-television-drama-shooting-filing-announcement-for-march-2011> (last visited May 7, 2014). Most Chinese time travel serials followed the same superficially apolitical story arc: a modern-day protagonist travels in time to ancient China, interacts with inhabitants of the period, and becomes romantically involved with a famous Chinese historical figure. Olivia, "No More Time-Travel Drama," *Authority Says It Disrespects History*, CHINAHUSH (Apr. 3, 2011), <http://www.chinahush.com/2011/04/03/no-more-time-travel-drama-authority-says-it-disrespects-history>; Zhang Zihan, *supra* note 137. As innocuous as time travel-based fiction may seem, stories that explore alternative pasts or envision a future with divergent social structures can reverberate with messages critical of the present. See *id.* Chinese authorities are well aware that depictions of the past have long been used in Chinese literature to veil criticism of the present. See Rogier Creemers, *SARFT Introduces Limits on Provincial Television Dramas*, CHINA COPYRIGHT AND MEDIA (Jan. 9, 2012), <http://chinacopyrightandmedia.wordpress.com/2012/01/09/sarft-introduces-limits-on-provincial-television-dramas/>.

139. Film Script (Outline) Filing, *supra* note 126, art. 14.

140. In fact, SARFT was apparently dissatisfied with what it deemed an inadequate level of Chinese involvement in the film, and therefore denied *Looper*'s Chinese financiers a full co-production credit, instead giving the film only "assisted co-production" status. Goldstein, *supra* note 138. Nevertheless, the move appears to have been little more than an official slap on the wrist, as SARFT granted *Looper*'s producers the larger revenue share and favorable theatrical release conditions generally available to full co-productions. *Id.*

141. See Steven Zeitchik, *Extra 'Looper' Scenes for Some*, L.A. TIMES, June 21, 2012, at D2.

142. After all, *Looper* depicted not just the future, but China's future, if only fleetingly. Moreover, at the insistence of Chinese investors, *Looper*'s China release contained more footage depicting China's future than the United States release version. See *id.*

143. See Yu Hua, *Censorship's Many Faces*, N.Y. TIMES, Feb. 28, 2013, at A29, available at http://www.nytimes.com/2013/02/28/opinion/you-censorships-many-faces.html?_r=4&utm_source=Sinocism+Newsletter&utm_campaign=cce1e9d743-Sinocism03_01_13&utm_medium=email (describing various players and considerations involved in official censorship decisions, and observing the tensions that arise between economic interests and politics and how the former often trumps the latter).

high-profile Sino-Hollywood joint production. Or, more cynically, perhaps there were other motivations in play: the United States Securities and Exchange Commission has recently investigated some Hollywood studios for making illegal payments to Chinese officials in return for their approval of films for theatrical release,¹⁴⁴ a potential violation of the United States Foreign Corrupt Practices Act.¹⁴⁵

Censorship and micromanagement of film content is no small irritant to Chinese film and video producers and consumers. For example, the *Shanghai Daily* recently lamented SARFT's prohibition on horror films.¹⁴⁶ Chinese audiences crave horror films, the newspaper said, but "China's own horror industry seems drained of blood and vitality. Thus, viewers get their fix from abundant Asian and Western fare."¹⁴⁷

c. Censorship and Internet Video

Some audiovisual content producers live in the interstices of SARFT regulation because their productions do not fall cleanly within the traditional media categories of feature film or television programs, and their works are not distributed through traditional channels such as broadcast or cable television or cinema. In the past, films produced in China without government approval were considered "underground films."¹⁴⁸ They could not be legally screened in China and so were usually made for overseas distribution only.¹⁴⁹ However, online video and micro-blogging sites present independent filmmakers with an opportunity unavailable just a few years ago.¹⁵⁰

To date, censors have taken a relatively hands-off approach to micro movies,¹⁵¹ thereby enhancing the format's appeal and utility to filmmakers. The short production and release schedules, free of the burdens of lengthy state licensing and content approval procedures, means more timely content and less convolution in the delivery of the director's vision to her audience.¹⁵² This directness is refreshing to Chinese audiences and adds to the films' appeal, as the stories often

144. See Edward Wyatt et al., *S.E.C. Asks if Hollywood Paid Bribes in China*, N.Y. TIMES, Apr. 25, 2012, at B1, available at http://www.nytimes.com/2012/04/25/business/global/sec-asks-if-hollywood-paid-bribes-in-china.html?pagewanted=all&_r=0.

145. 15 U.S.C. §§ 78dd-1 to 78dd-3 (2012).

146. Li Anlan, *supra* note 131.

147. *Id.* Nevertheless, Chinese producers do attempt to push the boundaries. The aforementioned *Shanghai Daily* article, for example, cites a few Chinese films that flirt with the horror genre through plot devices — such as living characters who pretend to be ghosts — that technically adhere to the regulations but still add elements of horror. *Id.*

148. MONTGOMERY, *supra* note 1, at 1.

149. *Id.*

150. See Tang Lei, *supra* note 109.

151. See *supra* Part III.B.1.b.

152. See Tang Lei, *supra* note 109.

have a personal and unfiltered quality.¹⁵³ Said one director, “[Making micro movies] has given me more freedom to show my own message.”¹⁵⁴ The director continues, “I received a lot of feedback . . . from the public, and as I don’t have any pressure from the box office with this type of film, I can think to myself, ‘why don’t I shoot something different?’”¹⁵⁵

In July 2012, SARFT issued a notice officially asserting its power to regulate micro movies, but this action probably does not signal an impending crackdown.¹⁵⁶ Rather, SARFT’s admonishment that Internet video portals are responsible for filtering “unhealthy content” is likely an unsubtle reminder, of the sort SARFT often gives, that Internet video falls within its jurisdiction and that SARFT remains watchful of the developing medium.¹⁵⁷ In SARFT’s shadow, however, private self-censorship occurs within the online video community.¹⁵⁸ As the general manager of one small public relations company that produces micro movies put it, “Basically, there’s no [official] censorship.”¹⁵⁹ One micro movie director notes, “Don’t shoot pornography or nudity and don’t talk about the Party or politics,” but, “[o]ther than that, anything goes.”¹⁶⁰

The importation of films and television programs for online distribution through popular video portals such as Youku and Tencent also falls within a gray area to which SARFT officials take a comparatively hands-off approach.¹⁶¹ Online service providers have begun

153. *See id.*

154. Matthew Scott, *Censors Catch Up with China’s ‘Micro Film’ Movement*, YAHOO! NEWS SINGAPORE (July 16, 2012), <https://sg.news.yahoo.com/censors-catch-chinas-micro-film-movement-052603970.html> (quoting Chinese filmmaker, Gu Changwei).

155. *Id.*

156. *See id.*

157. *See id.* (“State media reported last week that SARFT called on Internet video service providers to ensure ‘unhealthy content’ was not screened and urged them to form an association of censors to ensure content was more controlled.”). The contents of SARFT’s July 2012 notice concerning micro movies are not public, but indications are that the notice merely reiterates longstanding SARFT policy that “[he] who operates the web is responsible”; in other words, the video websites that publish such films are responsible for ensuring their content adheres to SARFT guidelines. Rogier Creemers, *SARFT Spokesperson Talks with Journalist on the ‘Notice Concerning Further Strengthening Network Drama, Microfilm and Other Network Audiovisual Programme Management’*, CHINA COPYRIGHT AND MEDIA (July 9, 2012), <http://chinacopyrightandmedia.wordpress.com/2012/07/09/sarft-spokesperson-talks-with-journalist-on-the-notice-concerning-further-strengthening-network-drama-microfilm-and-other-network-audiovisual-programme-management/>.

158. *See* Scott, *supra* note 154 (“[T]hose in the micro film industry say the ruling will have little impact because filmmakers already rely on web portals that employ people to pre-screen all content uploaded to the site. The mostly dramatic content is also seen as relatively inoffensive. ‘There are certain rules the filmmakers have to follow — like no porn — as there are in mainstream Chinese cinema,’ said [leading online video website] Youku [executive] Shao.”).

159. Tang Lei, *supra* note 109 (quoting Song Huanyu, general manager of micro movie producer Linksus).

160. *Id.* (quoting micro movie director Jin He).

161. *See, e.g.,* Coonan, *supra* note 108.

licensing foreign as well as domestic video content, thereby creating opportunities both for foreign copyright owners and Chinese video portals. For example, despite SARFT's rules banning horror films, *The Walking Dead* became China's most popular foreign television show online in 2013 after Youku licensed the zombie series from its United States producers.¹⁶² Internet video, therefore, might be an area where censors are willing to experiment with a more permissive approach. So far, this tactic has resulted in tangible gains for copyright owners, as it has enabled the sometimes highly lucrative licensing of domestic and foreign content that has not undergone official review.

C. China's Music Industry

1. The Failure of Exclusion Economics

Chinese netizens' appetite for music is voracious and unabated. According to Chinese government statistics, music was the third most-consumed network application in China in 2012, behind instant messaging and web search and ahead of online video and online gaming.¹⁶³ More than seventy-seven percent of China's 564 million Internet users consume music online.¹⁶⁴ And Chinese consumers' love of music shows no signs of ebbing: the consumption of music online in 2012 increased by thirteen percent over the previous year.¹⁶⁵

The Chinese music industry should be booming as a result, but it is not. While the Chinese box office has grown so rapidly and profitably that Hollywood now routinely crafts and alters scripts to appease Chinese audiences and censors,¹⁶⁶ China's music industry has been decimated by piracy and is greatly impeded by its inability to fully capitalize on its most lucrative exclusion-based monetization model: mobile ringback tones. The result is that the music industry, as the *China Daily* recently put it, "languishes on life support . . ."¹⁶⁷ In January 2012, in a move that spoke volumes about the tribulations facing the Chinese music industry, China's most prominent music executive, Song Ke, abruptly quit his job as CEO of the Mainland's

162. *Id.*

163. *Statistical Report on Internet Development in China*, CHINA INTERNET NETWORK INFO. CENTER 38 (2013), <http://www1.cnnic.cn/IDR/ReportDownloads/201302/P020130312536825920279.pdf>.

164. *Id.* at 5, 38.

165. *Id.* at 38.

166. Steven Zeitchik & Jonathan Landreth, *Hollywood Gripped by Pressure System from China*, L.A. TIMES, June 12, 2012, <http://articles.latimes.com/2012/jun/12/entertainment/la-et-china-censorship-20120612>.

167. Chen Nan, *Staging a Comeback*, CHINA DAILY, June 29, 2012, 10:56, http://www.chinadaily.com.cn/entertainment/2012-06/29/content_15534983.htm.

most successful record company¹⁶⁸ in order to launch a Peking duck restaurant.¹⁶⁹ “When I make good roast duck,” Song lamented, “people pay and thank me. When I make good music, nobody pays me and some even ridicule me.”¹⁷⁰

Industry revenue from the sale of recorded music in China has fallen in the past decade from an estimated \$198 million in 2003,¹⁷¹ derived almost exclusively from the sale of CDs and other physical media,¹⁷² to \$92.4 million in 2012, derived mostly from digital music.¹⁷³ China currently ranks as the world’s twentieth largest music market with a mere one percent share of global revenue.¹⁷⁴ China’s market for legitimate CDs is small — estimated at approximately \$17 million in 2012, it accounts for 0.002 percent of the global music industry’s physical-format sales.¹⁷⁵ Revenues are so small in part because legitimate CDs compete with pirated copies, but mostly because Internet music downloads have long been Chinese consumers’ preferred method of music delivery. Piracy in the form of unauthorized downloads is thus a major source of the Chinese music industry’s woes.¹⁷⁶ While the Chinese music industry has managed to survive on alternative revenue sources, such as licensing deals with search engine providers, live performances, and mobile ringback tones, it is far from thriving.

a. Search Engines and Unauthorized Music Downloads

For many years, major search engines were the biggest contributors to unauthorized downloading, providing consumers with deep

168. Bai Shi, *The CD Is Dying*, BEIJING REV., Feb. 16, 2012, http://www.bjreview.com.cn/life/txt/2012-02/13/content_425377.htm.

169. Mu Qian, *Music Isn’t a Dead Duck*, CHINA DAILY, Feb. 24, 2012, http://www.chinadaily.com.cn/life/2012-02/24/content_14686101.htm.

170. *Id.* Song Ke returned to the music industry in June 2012 as managing director of Evergrande Music, founded by a major Chinese real estate investment group. *See Evergrande Music Lays out Grand Plans*, CHINA DAILY, June 21, 2012, 10:28, http://www.chinadaily.com.cn/entertainment/2012-06/21/content_15516703.htm.

171. IFPI, THE RECORDING INDUSTRY COMMERCIAL PIRACY REPORT 8 (2004), available at <http://www.ifpi.org/content/library/piracy2004.pdf>.

172. *See id.* at 1–2.

173. IFPI, *Recording Industry in Numbers: The Recorded Music Market in 2012*, 2013 IFPI 62 [hereinafter *Recording Industry in Numbers 2012*].

174. *Id.* at 62, 91.

175. *See Recording Industry in Numbers 2012*, *supra* note 173 at 7, 62.

176. *See* IFPI, *Digital Music Report 2013*, 2013 IFPI 28–31 (noting that Internet piracy has had a “continued serious impact” on the music industry because “copyright protection and enforcement help underpin the industry’s business,” and discussing ways in which the industry is trying to stamp out online piracy). *But cf.* Luis Aguiar & Bertin Martens, *Digital Music Consumption on the Internet: Evidence from Clickstream Data* (Eur. Comm’n Joint Research Ctr. Inst. for Tech. Studies, Digital Economy Working Paper 2013/4, 2013) (finding no evidence of displacement of digital sales from illegal downloading in a European study).

links to illegal files.¹⁷⁷ Baidu, China's largest search engine with more than sixty percent of the Chinese search market, provided a music search feature called Baidu MP3 Search that enabled users to effortlessly search for and download thousands of popular recordings.¹⁷⁸ According to a 2008 investigative article by *The Register's* Andrew Orłowski, the majority of music files available through MP3 Search were hosted on "a network of mysterious sites with closely related domain names . . . [that] were unreachable except through the Baidu search engine."¹⁷⁹ Though it is uncertain whether Baidu or some other entity operated these mysterious music file-hosting domains,¹⁸⁰ it is clear that while Baidu was offering MP3 Search the "cumulative effect [was] to keep the 'free music flowing' for Baidu's users — with devastating consequences not just for creators, but for rival Internet businesses."¹⁸¹

In response to this threat, copyright owners have sued Baidu and other search engines in Chinese courts multiple times since 2005, with very limited success.¹⁸² After the international major record labels sued Baidu for the third time in four years, the parties settled in 2011 (allegedly at the insistence of the Beijing Higher People's Court).¹⁸³ Baidu signed an agreement with the record companies in which the labels agreed to license a 500,000-song catalog to Baidu, and Baidu reportedly agreed to pay upfront licensing fees as well as per-stream

177. Jiarui Liu, *supra* note 9, at 628–29.

178. *Id.*

179. Orłowski, *supra* note 31.

180. At least one Chinese search engine providing music search services similar to Baidu MP3 Search was revealed to actually host the music files itself. *See id.* ("[L]egal authorities finally managed to pin down full liability on music search engine Zhongsou for hosting illegal music files on its servers . . . Zhongsou's network of domains was registered under false names of individuals, and it required laborious investigation to track down the servers.").

181. *Id.*

182. In 2005, the IFPI sued Baidu, alleging that Baidu's provision of deep links in its search results constituted direct infringement. *Seagull Haiyan Song*, *supra* note 32, at 9. Baidu successfully argued, however, that it did not infringe because it is merely a search engine that provides links to content but does not actually host the content. *See id.* Six months later, the IFPI brought a similar search engine liability case against Alibaba/Yahoo! China. *Id.* In this case, unlike the Baidu case, the IFPI brought an indirect liability claim as well as a direct liability claim. *Id.* While the court again dismissed the direct liability claim, it held that the defendant was liable under a theory of indirect liability because it "should have known" of the infringing materials based on repeated takedown notices sent by the plaintiffs. *Id.* In 2008, the Music Copyright Society of China ("MCSC"), a performing rights organization, sued Baidu and sought \$140,000 in damages for infringing fifty musical works. *Xue "Snow" Dong & Jayakar*, *supra* note 50, at 89–90. Just a few months after MCSC filed its lawsuit, three of the four major international record companies — Universal Music Group, Warner Music Group, and Sony BMG — sued Baidu, seeking \$9 million in damages. *Id.* at 90. The Beijing First Intermediate People's Court again ruled in Baidu's favor, based on reasoning similar to that of the 2005 decision. *Id.* The appellate court, however, directed the parties to enter mediation due, according to one account, "to the sensitivity and international ramifications of the case." *Id.*

183. *See Xue "Snow" Dong & Jayakar*, *supra* note 50, at 90.

or per-download fees.¹⁸⁴ Most importantly, Baidu agreed to phase out its MP3 Search feature in favor of a new, licensed service through which users can stream or download music for free under an ad-revenue-sharing arrangement between Baidu and the major labels.¹⁸⁵ At the time of this writing, the MP3 Search feature appears to be no longer available, replaced by Baidu's allegedly legal music service.

Commentators suggest that a convergence of factors led to Baidu's change of heart.¹⁸⁶ These included a changing political environment following the United States' high-profile 2007 WTO proceeding against China;¹⁸⁷ recent strengthening of copyright regulations, especially with respect to online infringements;¹⁸⁸ heightened efforts by the Ministry of Culture ("MOC") to enforce music copyrights online;¹⁸⁹ concerns about the brand-tarnishing effects of piracy; and Baidu's apparent desire to build value-added services around a licensed music ecosystem.¹⁹⁰

Whether or not these are Baidu's real motivations for settling, questions remain about what the licensing agreement means for copyright owners. Some commentators believe it heralds a new age in online music monetization in China.¹⁹¹ Indeed, the trend is spreading,

184. *Id.* at 90–91.

185. *Id.*

186. *Id.* at 91–99.

187. *Id.* at 92–93; *see also supra* notes 40–43 and accompanying text. With regard to the issue of government pressure, the court's adjuration that the parties settle may indicate that state actors wanted to see an end to the cat-and-mouse game between Baidu and music copyright owners. Alternatively, it may have been an attempt to force the major record companies to the negotiating table with Baidu — something the record labels had resisted so long as Baidu continued to provide deep links to infringing files in its search results. Beyond this, it seems unlikely that government pressure significantly influenced Baidu's decision. While the Ministry of Culture made public efforts at the time to "punish" Baidu and other websites for providing infringing music content, few details were released about who was punished or what the sanctions were, and Baidu's punishment apparently amounted to, as The Register noted, a mere slap on the wrist. Kelly Fiveash, *China Gently Chides Baidu over Deep-Linking MP3 Naughtiness*, REGISTER (Apr. 26, 2011), http://www.theregister.co.uk/2011/04/26/baidu_illegal_music_downloads/.

188. Xue "Snow" Dong & Jayakar, *supra* note 50, at 93–94.

189. *Id.* at 94–95. This includes superintending the establishment of the Alliance of the Digital Music Industry, an "industry-coordinating organization" comprised of record labels, wireless operators, and websites such as Baidu, which reportedly joined under pressure from authorities. *See* Alex Bojalad, *Chinese Online Music Providers Form Industry Association*, BILLBOARD (June 20, 2011, 3:00 PM EDT), <http://www.billboard.com/biz/articles/news/1177456/chinese-online-music-providers-form-industry-association>; Xue "Snow" Dong & Jayakar, *supra* note 50, at 95.

190. Xue "Snow" Dong & Jayakar, *supra* note 50, at 96–97.

191. *See* Louis Hau, *Chinese Search Giant Baidu's Major-Label Licensing Pacts Signal a Promising Shift*, BILLBOARD (July 22, 2011, 1:46 PM EDT), <http://www.billboard.com/biz/articles/news/1177005/chinese-search-giant-baidus-major-label-licensing-pacts-signal-a-promising>.

as Baidu became one of several major Chinese online music services that license music.¹⁹²

Other commentators, however, are skeptical that Baidu's agreement with the major record labels indicates marked improvement, alleging that even services that pay licensing fees to copyright owners still carry pirated content in order to drive traffic and increase ad revenue for the site owners.¹⁹³ It remains to be seen whether Baidu too will ultimately revert to what one commentator calls "partial licensing as cover for pirate activity and traffic magnet . . ." ¹⁹⁴ As another commentator put it, far from indicating that copyright owners are finally getting the best of infringing sites in China, deals such as Baidu's and a similar agreement between international major record labels and Chinese web portal Sohu are actually "reluctant interim concessions from desperate rights owners."¹⁹⁵ Further, these deals may not help independent and domestic labels and artists. "Indie labels," as one Chinese music executive said, "don't really have a say in [such] negotiation[s], since their catalogs are usually too small to matter."¹⁹⁶ According to reports, only about ten percent of the content licensed to Baidu was in Mandarin or Cantonese, suggesting that the deal would have little impact on most Chinese artists.¹⁹⁷ Most importantly, while the licensing fees were not disclosed, it is generally believed they were too small to lead to a meaningful turnaround in the fortunes of the music industry and individual musicians in China.¹⁹⁸ In short, the licensing agreements were a positive first step, but much room for improvement remains.

192. According to this Author's communications with Chinese music industry sources, Internet giant Tencent's QQ Music, Internet portal Sina, music downloading and streaming start-up Xiami, and Internet music streaming service Douban.fm all pay copyright owners for content. Indeed, there is a confluence of evidence indicating that broader change is afoot. The Alliance of the Digital Music Industry exemplifies more high-profile government efforts to bring together copyright owners and online service providers, and in 2012 new regulations went into effect requiring entities that publicly perform music, including radio stations, TV stations, and business establishments, to pay public performance royalties to musical composition copyright owners. See Music Copyright Society of China, 电视台使用音乐作品付酬协议集体签约仪式在京隆重举行, 中国音乐著作权协会 (Jan. 12, 2012), <http://www.mcsc.com.cn/informationSociety.php?partid=13&pid=973>.

193. See Mathew D, *China Aims To Redress Copyright Burden of Proof Imbalance*, GLOBAL OUTPOST (May 5, 2011, 2:22 PM), <http://www.theglobaloutpost.com/archives/45>.

194. *Id.* (internal quotation marks omitted).

195. Ed Peto, *Majors Settle with Sogou MP3 Search*, OUTDUSTRY (Mar. 5, 2013), <http://outdustry.com/post/44612920249/majors-settle-with-sogou-mp3-search>.

196. *Building China's Music Industry, from the Internet up*, KNOWLEDGE@WHARTON (July 18, 2012), <http://www.knowledgeatwharton.com.cn/index.cfm?fa=viewfeature&articleid=2628&languageid=1> (quoting Felix Cheng, music blogger and A&R executive at Universal Music China).

197. Dan Levine, *China's Biggest Search Engine, Known for Illegal Downloads, Makes Music Deal*, N.Y. TIMES, July 19, 2011, <http://www.nytimes.com/2011/07/19/technology/baidu-chinas-search-giant-announces-music-licensing-deal.html>.

198. *See id.*

b. Alternative Revenue Streams: Live Performance and Corporate Sponsorship

Because recordings are extremely difficult to monetize, many labels and artists naturally emphasize developing “alternative” revenue streams — that is, revenue that does not derive directly from copyright exploitation. Live performance income is an extremely important revenue stream for pop superstars. Similar to in-theater movie screening, live musical performances by well-known artists are highly monetizable and less vulnerable to piracy because non-paying individuals can be excluded from the experience of seeing a performer live. Yu Quan, one of China’s most successful pop music acts since 2000, reportedly earns \$25 million annually from live performances alone.¹⁹⁹ Only superstars can reach this level of live performance income. However, increasingly numerous concerts and multi-day, government-sponsored music festivals provide a growing source of income to the best-known alternative musicians,²⁰⁰ and corporate and commercial gigs can be profitable for mid-level pop artists.²⁰¹ While few reliable statistics are readily available to substantiate the number and earnings of middle-class artists, the number of artists able to earn a subsistence living from festivals and commercial performances alone is likely small.²⁰²

199. MONTGOMERY, *supra* note 1, at 68.

200. See Jonathan Kaiman, *Beijing Spends a Billion To Get China Rocking*, GUARDIAN (Dec. 25, 2012, 5:17 PM EST), <http://www.guardian.co.uk/world/2012/dec/25/china-music-valley-cultural-profile> (“Yan Haisong, the lead singer of the veteran Beijing rock band P.K.14, said his band made a decent living performing at festivals and producing records for up-and-coming artists.”); Sinica Podcast, *The China Rock Podcast*, POPUP CHINESE (Aug. 8, 2011), <http://popupchinese.com/lessons/sinica/the-china-rock-podcast> (featuring a panel discussion of the China music scene in which China rock music experts Michael Pettis and Archie Hamilton noted that popular Chinese alternative rock band Carsick Cars had recently earned 90,000 RMB (about \$14,400) in less than two months performing at festivals and concerts, and another “top rock band” booked a festival for a fee of “well into six figures [RMB]”).

201. See *‘Chaos’ of China’s Music Industry*, BBC (Feb. 21, 2008), <http://news.bbc.co.uk/2/hi/asia-pacific/7251211.stm> (reporting that mid-level Chinese pop artist Long Kuan can earn as much as \$4100 per performance at a “commercial gig” — a private or promotional corporate event); *Building China’s Music Industry, from the Internet up*, *supra* note 196 (“[M]ost artists . . . rely on a combination of corporate sponsorships and events for their bread and butter . . . [T]he most important source of revenue for these musicians is performing at corporate events . . . [where] an artist can charge anywhere from one thousand to several hundred thousand RMB a day.”).

202. See, e.g., A.A., *Subcultural Sounds*, ECONOMIST, (May 1, 2013, 11:36), <http://www.economist.com/blogs/analects/2013/05/music-festivals> (describing the burgeoning concert and festival scene in China, but noting that “with few exceptions no one can make a living out of alternative music in China”); *Building China’s Music Industry, from the Internet Up*, *supra* note 196 (quoting one China music promoter as saying, “For non-mainstream artists and bands, there is no particularly viable business model and most musicians will also hold day jobs”). Anecdotally, at least, some mainstream Chinese pop stars cannot earn a living from live performances and commercial appearances, and rely on mobile music royalties. See *id.* (quoting China music promoter as saying, “I’ve had mid-level

Corporate sponsorship and product endorsement provide another important revenue stream for pop superstars. These opportunities can involve the use of the artist's image on products, artist appearances at promotional events, or product placement advertising in the artist's videos and live performances.²⁰³ Of course, these revenue opportunities are unavailable to most artists.²⁰⁴

c. Mobile Music: Opportunity and Exploitation

For many recording artists and virtually all Chinese record companies, mobile music is the most important source of revenue. According to the MOC, revenue in China's recorded music industry increased by fourteen percent in 2010 over the previous year, and ninety percent of total revenue derived from mobile value-added music services²⁰⁵ provided by mobile telecommunications companies China Mobile, China Unicom, and China Telecom. More than 600 million mobile subscribers — comprising approximately seventy percent of China's mobile subscribers — used mobile music services in 2010,²⁰⁶ including full-track downloads and ringtones.

Color ringback tones ("CRBTs") are by far the most important source of mobile music revenue. CRBTs are especially lucrative for two reasons. First, unlike ringtones, CRBTs are not files that are downloaded or otherwise loaded onto the mobile handset. Rather, they are broadcast in real time from the mobile service provider to a caller's handset. CRBTs are thus an excludable service, not a product, which helps make them impervious to piracy. Subscribers must pay for the service, which is delivered via a centrally administered system.²⁰⁷ Second, because they are purchased as an automatically renewable monthly subscription, CRBTs are "set and forget": users that order the service once often retain it and pay the recurring fee indefinitely, ensuring recurring revenue as opposed to the one-time purchase fees paid for full-track downloads. CRBT subscriptions cost as little as two RMB (about \$0.32 per month),²⁰⁸ making them affordable

Chinese pop stars tell me that China Mobile is like mom and dad — the money made from China mobile is the only thing that is keeping them housed, clothed and fed").

203. See Jiarui Liu, *supra* note 9, at 637; 'Chaos' of China's Music Industry, *supra* note 201.

204. See Jiarui Liu, *supra* note 9, at 637–38.

205. Tan, *supra* note 71.

206. *Id.*

207. See MONTGOMERY, *supra* note 1, at 71.

208. Zhu Hong, the general manager of China Mobile's wireless music division, reported that 470 million of the company's 650 million mobile users had ringback tone subscriptions in 2011, "and each of them contribute[d] around CNY2.00 per month." Joyce Fan, *China Mobile Hits the Right Note with Legit Music*, WINWIN, Dec. 2012, at 17, available at http://www.huawei.com/us/about-huawei/publications/winwin-Magazine/hw-201235-hw_201263-135300-135327-hw_201255.htm.

for lower-income individuals and thereby greatly expanding the range of customers paying for music services. Music industry executive Song Ke stated that mobile music sales in China in 2011 were 27.9 billion RMB, or more than \$4 billion.²⁰⁹ By comparison, in the United States (the world's largest recorded music market), total record industry revenue from all sources, physical and digital, amounted to \$4.48 billion in 2012.²¹⁰ Royalties from mobile music have become an indispensable source of income for many labels and artists. As one Chinese music industry executive put it, "I've had mid-level Chinese pop stars tell me that China Mobile is like mom and dad — the money made from China [M]obile is the only thing that is keeping them housed, clothed and fed"²¹¹

The problem, according to Song and other Chinese recording industry executives, is not that digital music cannot be monetized in China; rather, it is that the revenue distribution is drastically skewed in favor of wireless service providers so that creators and copyright owners receive only a tiny fraction of gross revenue.²¹² This explains why China's music industry faces dire financial circumstances despite the fact that, according to MOC statistics, 600 million people — nearly twice the entire United States population — use paid digital music services in China.²¹³ While the agreements between mobile service providers and record companies reportedly stipulate a fifty-fifty mobile music royalty split, in reality the mobile service providers pay music copyright owners a royalty of just two percent or less of mobile music revenue²¹⁴ — unconscionably small as compared with royalties customarily paid by major digital music retailers in the United States. Apple Inc., for example, reportedly pays copyright owners a royalty of seventy percent of the song purchase price for full-track downloads bought through its iTunes digital music store.²¹⁵ Song suggests that

209. Wang Xiaofeng (王小峰), Song Ke: Zhongguo Changpian Ye de Shuailuo Zhi Yin (宋柯：中国唱片业的衰落之因) [Song Ke: The Reason for the Decline of the Chinese Record Industry], SAN LIAN SHENG HUO (三联生活) [LIFEWEEK] (Jan. 30, 2012), <http://www.lifeweek.com.cn/2012/0130/36358.shtml>. A corporate magazine for Huawei Technologies, a technology provider to China Mobile, reports that China Mobile alone earned \$3.55 billion from its mobile music division in 2011. Fan, *supra* note 208, at 17.

210. *Recording Industry in Numbers 2012*, *supra* note 173, at 39.

211. See *Building China's Music Industry, from the Internet up*, *supra* note 196 (quoting Nathaniel Davis, the co-founder of Shanghai-based music promotion company Split Works).

212. See Yang Yang, *A Record Tailspin*, CHINA DAILY, June 29, 2012, 9:00, http://usa.chinadaily.com.cn/weekly/2012-06/29/content_15534133.htm ("When talking about the music market, people always say the business is very bad. But actually, it is not bad at all. Music makes enormous money. It's only we producers don't get much" (quoting Chinese record company executive Zhan Hua) (internal quotation marks omitted)).

213. See Tan, *supra* note 71.

214. See Wang Xiaofeng, *supra* note 209.

215. See Philip Bump, *Apple's Streaming Music Deal Broke Down over These Few Cents*, ATLANTIC WIRE (Mar. 7, 2013, 2:43 PM ET), <http://www.theatlanticwire.com/technology/2013/03/apple-streaming-music-deal/62870/>.

even a sixty-forty royalty split favoring mobile providers would provide the basis for a robust, vibrant recording industry in China.²¹⁶ At present, however, the likelihood that music copyright owners can obtain that figure is remote.

The astonishing and under-appreciated fact, therefore, is that for all the attention the Chinese box office numbers receive, digital music revenue in China dwarfed China's \$3 billion box office revenue in 2012. The fact that total recording industry revenue in China still amounts to less than \$100 million annually indicates severe dysfunction throughout the Chinese music industry ecosystem. Major contributors to the problem, of course, are the mobile service providers, which have long managed to pay music copyright owners an audaciously low percentage of revenues. However, it is difficult to escape the conclusion that piracy still looms as the ultimate culprit. The recording industry's inability to exploit copyright leaves it vulnerable to severe bargaining asymmetries in negotiations with powerful distributors, who are free to overreach and extract unconscionable fees because copyright owners lack the leverage to negotiate a better rate or enforce the existing terms of their agreements with the distributor.

2. Censorship in China's Music Industry

Approval of music content in China lies with two separate authorities: the General Administration for Press and Publications ("GAPP") has authority over music on physical media,²¹⁷ while the MOC has authority over online music distribution.²¹⁸ Unsurprisingly, this bifurcation of authority can lead to interagency conflicts as each agency stakes out its turf in China's shifting digital media landscape.²¹⁹ (In-

216. See Wang Xiaofeng, *supra* note 209.

217. Creemers, Explaining Audiovisual Media Piracy, *supra* note 9, at 90–91.

218. See Wenhua Bu Guanyu Jiaqiang he Gaijin Wangluo Yinyue Neirong Shencha Gongzuo de Tongzhi (文化部关于加强和改进网络音乐内容审查工作的通知) [Notice Concerning Strengthening and Improving Network Music Content Examination Work] (promulgated by the MOC, Aug. 18, 2009), *translated in* CHINA COPYRIGHT & MEDIA (Aug. 18, 2009), <http://chinacopyrightandmedia.wordpress.com/2009/08/18/notice-concerning-strengthening-and-improving-network-music-content-examination-work/> [hereinafter Network Music Content Examination Work]; Wenhua Bu Guanyu Wangluo Yinyue Fazhan he Guanli de Ruogan Yijian (文化部关于网络音乐发展和管理的若干意见) [Some Opinions Concerning Network Music Development and Management] (promulgated by the MOC, Dec. 20, 2006), *translated in* CHINA COPYRIGHT & MEDIA (Dec. 20, 2006), <http://chinacopyrightandmedia.wordpress.com/2006/12/20/some-opinions-concerning-network-music-development-and-management/> [hereinafter Some Opinions Concerning Network Music Development and Management].

219. In one recent example, the MOC issued a list of one hundred songs by foreign artists, including popular artists from the United States, Australia, Korea, Taiwan, and Hong Kong, that it banned from Chinese websites. See Loretta Chao, *Culture Ministry Goes After Online Music, Again*, WALL ST. J. CHINA REAL TIME REP. (Jan. 12, 2011, 2:43 PM HKT), <http://blogs.wsj.com/chinarealtime/2011/01/12/culture-ministry-goes-after-online-music->

deed, to confuse matters more, recall that the National Copyright Administration of China is yet another agency with enforcement and policy-setting authority over copyrighted works, including music.²²⁰)

Any business seeking to distribute music online, or to import or produce music for online distribution, must obtain an MOC permit.²²¹ As with film, all domestic and imported music must undergo official

again/. The ban order sowed confusion, however, because the MOC gave no reasons for the ban and GAPP had previously approved most of the same songs for CD distribution. *See id.*

220. *See supra* note 55 and accompanying text.

221. Network Music Content Examination Work, *supra* note 218, para. 2. In the wake of WTO Report WT/DS363/R, *see supra* notes 119–120 and accompanying text, China agreed to liberalize its rules concerning foreign involvement and investment in the importation and distribution of copyright-intensive works, including recorded music. To date little has happened in that regard. Wholly foreign-owned enterprises (“WFOEs”) still may not directly invest in music distribution services. Sino-foreign joint ventures may distribute music on physical media (CDs). *See* Yinxiang Zhipin Guanli Tiaoli (音像制品管理条例) [Audiovisual Products Management Regulations] (promulgated by St. Council, Dec. 12, 2001, effective Feb. 1, 2002), art. 35, *translated in* CHINA COPYRIGHT & MEDIA, <http://chinacopyrightandmedia.wordpress.com/2001/12/25/audiovisual-products-management-regulations-revised/> [hereinafter Audiovisual Products Management Regulations], *revised by* Guowuyuan Guanyu Xiugai “Yinxiang Zhipin Guanli Tiaoli de Jueding” (国务院关于修改〈音像制品管理条例〉的决定) [State Council Decision Concerning Revising the “Audiovisual Product Management Regulations”] (promulgated by St. Council Mar. 19, 2011, effective Mar. 19, 2011), *translated in* CHINA COPYRIGHT & MEDIA, <http://chinacopyrightandmedia.wordpress.com/2011/03/19/state-council-decision-concerning-revising-the-audiovisual-product-management-regulations/> [hereinafter State Council Decision Concerning Revising the “Audiovisual Product Management Regulations”]. However, any entity engaged in distribution must first receive state approval through an opaque process subject to broad administrative discretion. *See* Audiovisual Products Management Regulations, *supra*, art. 32; *China Fails To Implement WTO Ruling in Audiovisuals Case, or What Did We Expect?*, CHINA COPYRIGHT & MEDIA (Mar. 24, 2011), <http://chinacopyrightandmedia.wordpress.com/2011/03/24/china-fails-to-implement-wto-ruling-in-audiovisuals-case-or-what-did-we-expect/>.

Likewise, due to political sensitivities surrounding information distribution, a foreign business must establish a Sino-foreign joint venture to operate within China as an online music distribution service — a “value-added telecommunications service[.]” according to Chinese authorities. *See* Waishang Touzi Dianxin Qiye Guanli Guiding (外商投资电信企业管理规定) [Provisions on Administration of Foreign-Invested Telecommunications Enterprises] (promulgated by the Ministry of Info. Tech., Dec. 11, 2001, effective Jan. 1, 2002), art. 4, <http://www.wipo.int/wipolex/en/details.jsp?id=6570>. The joint venture model presents many risks, however, including the lack of foreign entity control, the potential for conflict between joint venture partners, and the transfer of proprietary information or technology. *See* DANIEL C.K. CHOW & ANNA M. HAN, *DOING BUSINESS IN CHINA: PROBLEMS, CASES, AND MATERIALS* 90 (2012). Most foreign-invested Internet businesses operating in China, therefore, prefer to operate as WFOEs. They typically “creatively comply” with the sole foreign ownership restrictions by establishing a “variable interest entity” (“VIE”). *See* Shen Wei, *Will the Door Open Wider in the Aftermath of Alibaba? — Placing (or Misplacing) Foreign Investment in a Chinese Public Law Frame*, 42 H.K. L.J. 561, 561, 565–70 (2012). VIEs are local companies owned by Chinese nationals nominated by the WFOE. The VIE is eligible to obtain the required permits and operate the service, but is controlled by the WFOE through a series of contracts rather than through share ownership. *See* Ke Chen, “Rule By Law” and Its Impact on Cross-Border Transactions Affecting Chinese Interests, 34 T. JEFFERSON L. REV. 161, 167 (2011).

content review before distribution.²²² MOC rules also oblige online distributors to review the works and guarantee their legality.²²³ Despite these seemingly oppressive music censorship rules, however, Chinese music industry insiders suggest that in practice Chinese authorities are less concerned about the ideological impact of music and therefore have paid comparatively less attention to it than they do to the film industry.²²⁴ Indeed, one Chinese music industry executive wished that Chinese censors would scrutinize the music industry as much as they do the film industry. While censorship is “very twisted,” he said, “at least [the government] is providing a relatively healthy environment for the film industry. But the music industry is left on its own to take care of itself.”²²⁵

The MOC’s content examination rules highlight the nexus between administrative copyright enforcement and censorship, despite the MOC’s insistence that the rules are primarily meant to address online piracy by helping the agency track and identify “illegal” music online. According to the MOC, its use of the term “illegal” refers primarily to infringing content rather than censored content, as ninety-nine percent of music content is approved by censors and is therefore “legal” in that sense.²²⁶ Furthermore, as the MOC is a culture agency, officials say a content-oriented regulation must be in place for the MOC to be able to engage in copyright enforcement.²²⁷ Whatever the real impetus behind the MOC’s content review regulations, their effect on piracy remains dubious. Despite the MOC’s closure of more than 300 websites operating without online music service permits in

222. See Audiovisual Products Management Regulations, *supra* note 221, art. 28; Network Music Content Examination Work, *supra* note 218, art. 8.2. Domestically-produced music must also undergo review, but ostensibly on a faster track (a maximum of ten as opposed to twenty days). See *id.* art. 8.2, 14.

223. Network Music Content Examination Work, *supra* note 218, art. 15.

224. Wang Xiaofeng, *supra* note 209.

225. *Id.* (quoting former Taihe Maitian executive Song Ke).

226. See Susan Butler, *6 Questions with Chen Tong*, BILLBOARD, Feb. 10, 2007, at 30 (interviewing Chen Tong, chief of the audio and video division of the MOC’s Department of Cultural Market). Songs may fail to pass MOC review more frequently than Chen suggests, but in any event, when the MOC disapproves of a song the reasons are often opaque. For a colorful look at some of the songs that failed to pass MOC review, including songs from famous Western artists, see Elaine Chow, *In Pictures: Music Stars China’s Ministry of Culture Doesn’t Want You Listening to on the Internet Without Permission*, SHANGHAIIST (Aug. 25, 2011, 5:30 PM), http://shanghaiist.com/2011/08/25/in_pictures_music_stars_chinas_mini.php.

227. See Butler, *supra* note 226 (“The U.S. is a very regulated society, and [when there is] any pirated product, people who infringe can be sued through a civil case. But in China, the administration . . . has more legal power. So there needs to be a regulation first [for them to enforce].” (alteration in original) (quoting Chen Tong, chief of the audio and video division of the MOC’s Department of Cultural Market) (internal quotation marks omitted)).

2010,²²⁸ and despite other official efforts to crack down on online music piracy,²²⁹ the problem remains as robust as ever.²³⁰

IV. CHINA: A CHALLENGE TO TRADITIONAL ASSUMPTIONS ABOUT COPYRIGHT?

As the previous Sections demonstrate, copyright enforcement in China remains weak. Nevertheless, creators invest in the production of thousands of new commercial works of music and film each year, generating billions of dollars in gross receipts. It is little wonder that some commentators question whether piracy is causing any discernible harm to content creators at all, or whether it in fact might be contributing to industry growth.

The standard economic rationale for copyright is that authors and creators must be able to cost-effectively exclude competitors and the public from accessing and copying their works in order to recover the investment they made in creating those works.²³¹ Copyright enables exclusion by creating legal barriers to access, allowing authors to capture the economic value of their works.²³² Copyright therefore increases social welfare by incentivizing creators to invest in producing and disseminating new, original works. However, efficiency requires that copyright exclude others only to the extent necessary to provide this incentive. Otherwise, the public's ability to access works of expression, and creators' ability to build upon existing works, will be unduly burdened.²³³

228. Tan, *supra* note 71.

229. *See, e.g.*, Yang Yang, *supra* note 212 (“Since 2005, [the government] has been cracking down on online music piracy. Last year, the State Council . . . established the National Leading Group for IPR Enforcement In a three-month campaign in 2011, 17 major illegal websites that offered unauthorized services . . . were shuttered.”). One reason such efforts appear to bear little fruit is that they focus on high-profile, campaign-style enforcement, which has been shown to be among the weakest and least effective forms of IP enforcement — they tend to be poorly organized, short-term, and inconsistent, and therefore provide little long-term deterrence. *See* DIMITROV, *supra* note 9, at 226–30.

230. *See* OFFICE OF THE U.S. TRADE REP., 2012 SPECIAL 301 REPORT, *supra* note 16, at 29.

231. *See* WILLIAM M. LANDES & RICHARD A. POSNER, *THE ECONOMIC STRUCTURE OF INTELLECTUAL PROPERTY LAW* 38–41 (2003). Landes and Posner also point out that

[t]he problem of recoupment is magnified . . . by the fact that the author's cost of creating the work, and many publishing costs (for example, editing costs), are incurred before it is even known what the demand for the work will be. Because demand is uncertain, the difference between the price and marginal cost of the successful work must not only cover the cost of expression but also compensate for the unavoidable risk of failure.

Id. at 40.

232. *See* William Fisher, *Theories of Intellectual Property*, in *NEW ESSAYS IN THE LEGAL AND POLITICAL THEORY OF PROPERTY* 168, 169 (Stephen R. Munzer ed., 2001) (describing the standard utilitarian rationale for intellectual property).

233. *See id.*

Creative industry growth in China's high-piracy environment might appear to challenge the standard economic rationale for copyright.²³⁴ Six related themes emerge from optimistic accounts of the relationship between piracy and creativity in China. The remainder of Part IV introduces each of these themes, and summarizes arguments in the literature advancing the viewpoint expressed in each theme. Then, Part V will critique the premises and assumptions underlying each theme, and make a normative case for why better copyright enforcement would yield more benefits to Chinese creative industries and society than widespread piracy does.

A. Theme #1: "Piracy Has Not Harmed the Chinese Creative Industries, Because Production Continues Apace and Is Even Growing."

In her book, *China's Creative Industries: Copyright, Social Network Markets and the Business of Culture in a Digital Age*, Lucy Montgomery analyzes the effect of piracy on China's music and film industries.²³⁵ She asks whether "weaker copyright mean[s] stronger creative industries," and concludes that piracy has helped bring economic growth to China's domestic copyright industries.²³⁶ Regarding the music industry, for example, Montgomery says that while Chinese record labels continue to produce music at a high rate, they place "less emphasis on producing popular albums and more emphasis on gaining popularity and profile through single hits that lead to lucrative product endorsement and live appearance or performance deals."²³⁷ Such "approaches that are proving successful in China may well turn out to be at the vanguard of models for monetizing creativity in a digital age."²³⁸ Western record companies, on the other hand, struggle in China because their traditional revenue model is based on recorded music "sold independently of the physical presence of the artist."²³⁹ Montgomery concludes that "[t]he rapid development of the creative industries in China appears to contradict the hypothesis that stronger IP is the pathway to economic growth. Instead . . . weaker IP is a much overlooked source of evolutionary development."²⁴⁰ She also argues that the protectionist effects of Chinese censorship help fuel

234. See, e.g., Wang Xin, *Growth in Industries Based on Copyrights*, CHINA DAILY USA, June 28, 2012, 8:16, http://usa.chinadaily.com.cn/epaper/2012-06/28/content_15530641.htm; Zheng Yangpeng, *supra* note 86; Lai, *supra* note 85.

235. See generally MONTGOMERY, *supra* note 1. Montgomery also analyzes the role of IP in the Chinese fashion industry, but that analysis is less salient to this discussion.

236. *Id.* at 93–106.

237. *Id.* at 104.

238. *Id.* at 106.

239. *Id.* at 67.

240. *Id.* at 106.

the growth of the creative industries by raising barriers to market entry for foreign works, thereby “increasing incentives for the production of domestic content and reducing foreign competition.”²⁴¹

Media piracy researcher Joe Karaganis similarly argues that piracy has hardly dented the fortunes of Hollywood or Chinese movie studios. He points out that despite widespread piracy, China’s theatrical market has emerged as the world’s second largest, and domestic film production is “comparable in numerical terms to Hollywood.”²⁴² This leads him to ask, “Where is the problem in need of an enforcement solution [in China]? Where is the evidence that piracy is undercutting production?”²⁴³

B. Theme #2: “Piracy Benefits Creators and Consumers by Lowering Access Barriers to a Wide Variety of Information Goods.”

Montgomery argues that endemic piracy promotes economic growth in the domestic Chinese copyright industries in part by giving creators broader access to existing works on which to build.²⁴⁴ Likewise, professor and filmmaker Jinying Li observes that piracy provides filmmakers with access to a vast array of films otherwise unavailable due to censorship. She chronicles how this has benefited at least one group of Chinese filmmakers: underground, independent digital filmmakers that Li dubs the “D-Generation.” D-Generation filmmakers began as movie buffs weaned on pirated DVDs of films from around the world that were unavailable in China through official channels.²⁴⁵ According to Li, piracy also helps to ensure that consumers can access D-Generation works by providing the filmmakers “with an important platform for distributing [their] works, which otherwise would never be able to reach a large audience.”²⁴⁶ Piracy networks have long served as an important form of domestic distribution for underground Chinese filmmakers, Li observes.²⁴⁷ Indeed, “the viral infrastructure of piracy, with the density, ubiquity, and flexibility of its ‘long tails,’ has proven a suitable channel for distributing alternative cinemas that target only a niche audience.”²⁴⁸

Legal scholars Kal Raustiala and Christopher Sprigman argue in their book, *The Knockoff Economy: How Imitation Sparks Innovation*,

241. *Id.* at 104.

242. Karaganis, *What Everyone Wants*, *supra* note 1.

243. *Id.*

244. See MONTGOMERY, *supra* note 1, at 102.

245. Jinying Li, *supra* note 1, at 552–55.

246. *Id.* at 555.

247. *Id.*

248. *Id.* at 556.

that in numerous industries copying fails to stifle innovation.²⁴⁹ In fact, they conclude, in many cases copying actually *drives* innovation.²⁵⁰ While their book does not discuss the creative industries in China, Raustiala and Sprigman have argued elsewhere that the lessons from their book are generally applicable to the piracy debates in China.²⁵¹ They argue that copying is a critical part of the creative process, so piracy is unlikely to have hurt innovation in China.²⁵² They acknowledge that piracy allows Chinese copyists to undercut Western competitors, but argue that piracy has other “irresistible benefits” for Chinese copyists, including the acquisition of design and technical skills.²⁵³ The net social benefits, Raustiala and Sprigman conclude, are unmistakable: piracy has resulted in “affordable products and services that have allowed millions of Chinese to enjoy the trappings of a consumer society.”²⁵⁴ Because piracy can elevate the standard of living for many in society, the argument goes, it helps mask the widening income gap in China, which is a major threat to social stability.²⁵⁵ It is in the Chinese government’s interest, therefore, to enforce IP rights laxly or even encourage copying.²⁵⁶

C. Theme #3: “Piracy Incentivizes Copyright Owners To Adopt Innovative Business Models.”

Montgomery argues that piracy drives business model innovation in China’s creative industries by forcing creators to adapt to market conditions and explore new business models that do not rely directly on copyright exploitation. She provides examples from the music industry such as CRBTs²⁵⁷ and what some refer to as “360 deals,”²⁵⁸ so-called because they allow labels to partake in all “360 degrees” of an artist’s potential income streams. These deals are contractual arrangements in which labels share in artists’ revenues beyond record

249. See generally RAUSTIALA & SPRIGMAN, *supra* note 2 (canvassing the phenomenon of widespread copying and relevant norms and legal rules in diverse industries, including fashion, cuisine, comedy, and finance, and finding that “even though others can freely copy in these industries, creativity remains surprisingly vibrant”).

250. *Id.* at 168 (“In some creative endeavors imitation has little effect on innovation. And in others, imitation can even spark innovation.”).

251. See generally Raustiala & Sprigman, *supra* note 1.

252. *Id.* at 26 (“American anxiety and anger over Chinese piracy are misplaced. Copying is not the plague that American business leaders and politicians often make it out to be. In fact, far from always being an enemy of innovation, copying is often a critical part of creativity.”).

253. *Id.*

254. *Id.*

255. See *id.* at 26–28.

256. See *id.* at 28.

257. See MONTGOMERY, *supra* note 1, at 66–68, 71.

258. See Jiarui Liu, *supra* note 9, at 642–43 (noting several shortfalls of the 360 deal model).

sales, such as income from live performances and product sponsorship or endorsement activities. Such deals are a marked expansion of the label-artist relationship in the West, where labels' income from artists was traditionally limited to record sales revenue.

D. Theme #4: "Piracy Is Especially Important for Political Discourse in China Because It Helps Information Goods Circumvent Heavy-Handed State Censorship Policies."

In her analysis of piracy and independent Chinese cinema, Li reasons that piracy helps support democratic discourse. Piracy provides underground filmmakers with the raw materials of preexisting works upon which to build at the front end, and a vast (albeit unremunerated) distribution network at the back end.²⁵⁹ These provide key elements of "an alternative public sphere structured by pirate cinema" that exists outside the realm of state-sanctioned speech.²⁶⁰

E. Theme #5: "Piracy Benefits Foreign Rights Holders in China by Providing Free Advertising and Branding for Their Works."

According to Karaganis, China's creative industries are not the only ones to have benefited from piracy.²⁶¹ He argues that in the heavily censored China market, in which only a handful of foreign films are approved for theatrical release on a revenue-sharing basis,²⁶² affordable and ubiquitous pirated DVDs of Hollywood films have served as "brand development," exposing and acclimating Chinese viewers to Hollywood's brand of filmmaking.²⁶³ It is far from clear that more stringent copyright enforcement would help Hollywood, he notes, as piracy is "part of the distribution, branding, and advertising system [for feature films] — not just a drain on it."²⁶⁴

Echoing Karaganis, Raustiala and Sprigman argue that piracy provides a form of advertising for the legitimate product, and that the substitution effect of piracy is overstated since those who can afford to purchase the original usually do.²⁶⁵ Ultimately, Raustiala and Sprigman argue, Western businesses should take heart since the long-term benefits of piracy also accrue to them: "[T]he wealth created by

259. See Jingying Li, *supra* note 1, at 555.

260. *Id.* at 558.

261. Karaganis, *What Everyone Wants*, *supra* note 1.

262. See Part III.B.2.

263. Karaganis, *What Everyone Wants*, *supra* note 1. This echoes Raustiala and Sprigman's argument that imitations "may serve as advertising for brands — advertising that is not only free but arguably more powerful." RAUSTIALA & SPRIGMAN, *supra* note 2, at 199 (emphasis omitted).

264. Karaganis, *Forget it, Jack, It's Chinatown*, *supra* note 1.

265. Raustiala & Sprigman, *supra* note 1, at 28.

piracy has aided the growth of an emerging Chinese middle class, which represents a massive potential pool of new customers for Western firms that sell the genuine article In the longer term, open copying may build demand for Western innovations.”²⁶⁶

F. Theme #6: “Foreign Dominance Poses a Greater Threat to China’s Cultural Industries than Piracy Does.”

Karaganis worries that the real danger to Chinese creative industries is not piracy, but rather overexposure to Hollywood through its box office successes. This could cause China’s film industry to become like that of Taiwan, where domestic films have a mere three percent market share.²⁶⁷ The result in China, according to Karaganis, would be

a high-end American-dominated market devoted to hero archetypes, violence, and spectacle (*Titanic* and *Avatar*), [with] a domestic industry bifurcated into a state-subsidized sector producing niche films and documentaries, and a commercial sector producing low-end, localized TV series and movies — the telenovelas and slapstick comedies of 21st century China.²⁶⁸

The following Part responds to and critiques each of the six themes discussed above.

V. DOES PIRACY HELP OR HINDER CHINA’S FILM AND MUSIC INDUSTRIES?

Part IV introduced six themes that have emerged from recent literature arguing that the harms of widespread copying are exaggerated and that piracy has even provided net benefits to China’s creative industries and to Chinese society as a whole. This Part analyzes and responds to each theme in the context of China’s music and film industries.

²⁶⁶ *Id.* at 26, 29.

²⁶⁷ Karaganis, *Forget it, Jack, It’s Chinatown*, *supra* note 1.

²⁶⁸ *Id.*

*A. Responding to Theme #1: “Piracy Has Not Harmed the Chinese Creative Industries, Because Production Continues Apace and Is Even Growing.”*²⁶⁹

Despite rampant piracy in China, Chinese and foreign studios invest millions of dollars in the production of new films with China’s theatrical market in mind. Independent and grassroots filmmakers in China continue to produce films as well, many with no hope of domestic theatrical distribution. Similarly, large domestic and international record companies invest substantial sums in the production of new music, and amateurs continue to write songs, mostly for free distribution on Youku and other Chinese video sites.

Why do people continue to invest in producing these works despite the high-piracy environment? One simple but incomplete answer is that, as demonstrated in Part III, even in China’s suboptimal enforcement environment, theatrical distribution can be lucrative for the right films, and live concerts and product endorsements can be lucrative for music superstars. The question itself, however, assumes an overly simplistic cause-and-effect relationship between copyright incentives and the quantity of creative production. The creative industries exist within a complex system of interacting components and socioeconomic variables,²⁷⁰ in which copyright is just one factor affecting the profitability and quantity of content production.²⁷¹ More to the point, Robert Merges argues that it is fruitless to ask whether or why people create even in the absence of extrinsic motivation.²⁷² Some artists are driven by intrinsic motivations, but that reveals little about whether copyright has social value. Instead, a more pertinent and constructive question is, “[W]hat conditions will surround and shape the work of creative persons, and will those conditions allow the creators to fully flourish — to create works of the highest quality they are capable of?”²⁷³ The question thus phrased assumes that supporting and enabling creators, not just motivating production, is a key copyright objective. The following Section argues that it is.

1. The Importance of Supporting a Professional Class of Content Creators

Myopically focusing on the production volume of creative works unduly narrows the focus of the inquiry. When evaluating the effects of piracy, we should inquire foremost into the health and stability of

269. See *supra* Part IV.A.

270. See generally Michal Shur-Ofry, *IP and the Lens of Complexity*, 54 IDEA 55 (2013).

271. See *id.* at 94–101.

272. ROBERT P. MERGES, JUSTIFYING INTELLECTUAL PROPERTY 247 (2011).

273. *Id.*

the creative industries and their ability to support a professional class of creators. Well-funded creative industries that support a professional creative class are key to assuring abundant production of high quality cultural works. Professor Merges argues that robust IP regimes (and their effective enforcement) ensure to creators two things: *reward* — that is, fair compensation for their efforts, and *autonomy* — that is, the opportunity to develop their craft and pursue a chosen livelihood as creative professionals.²⁷⁴ A copyright system that provides sufficient rewards and autonomy ensures that the most talented creative individuals in society enjoy the economic support and freedom to hone their craft and, in return, spend their professional lives maximizing their creative potential and publicly disseminating the fruits of those efforts. This state of affairs is not only good for creators. It benefits any society that values high quality cultural production and an endless wellspring of high quality works on which to build new works and shared cultural meanings.²⁷⁵ To the extent that a creative work's popularity is a measure of its social and cultural value, then professionally produced content is the most valuable, even in (indeed, especially in) this age of user-generated content and digital distribution.²⁷⁶

An economically robust creative ecosystem also promotes creative flourishing by supporting professionals who perform functions that are necessary but peripheral to creative work, thereby enabling creators to focus on creating. These support professionals are sometimes called “channel partners” because they perform critical channel functions such as administration, provision of financial support and advances, marketing, accounting, distribution, and sales — functions that creators often cannot perform, or cannot perform as well, themselves.²⁷⁷ When piracy erodes the economic support for channel partners, creators must assume the burden of these peripheral functions, and their creative productivity may suffer. Distraction can be costly: even well-known “DIY” creators have ultimately signed deals with major media companies because they found performing channel functions themselves was too difficult or detrimental to their artistic careers.²⁷⁸ This argument is not a defense of the exploitative practices of

274. *Id.* at 195. Of course, autonomy also means that creators are free from having to rely on state patronage — an important consideration in China, as addressed below in Part V.D.

275. *Id.* at 223 (“[W]ithout high-quality contemporary products in accessible form, there would be a lot less material out of which we can construct our shared culture. This is why I see [creative] professionals as so important.”).

276. See ANITA ELBERSE, BLOCKBUSTERS: HIT-MAKING, RISK-TAKING, AND THE BIG BUSINESS OF ENTERTAINMENT 150–64 (2013) (presenting data and case studies that demonstrate that professionally produced blockbuster content is far more popular than niche, “long-tail,” or user-generated content, and that the trend of consumer preference for blockbuster content is intensifying, not diminishing).

277. *See id.* at 191–92.

278. *See id.* at 193–98. Elberse provides case studies, including that of author Amanda Hocking, who achieved fame and fortune by selling independently published e-books direct-

some media companies. It is, rather, recognition that an economically strong creative ecosystem, even if flawed, provides far better conditions for creative flourishing than a creative ecosystem impoverished by piracy.

Advances brought about by digital technologies are unlikely to compensate for the economic losses caused by piracy. While digital technologies increasingly enable creators to produce higher-production-value works more cheaply and to market and distribute them directly to consumers, technology cannot replace all the channel functions and partners that help ensure skilled creators have the time and focus to master their craft and produce high-quality works. Further, while technology can reduce costs, it cannot eliminate the substantial expense of producing and commercializing high-production-value content,²⁷⁹ or the substantial costs of living for those involved.²⁸⁰

2. The Importance of Revenue Stream Diversity

China provides an instructive example of how copyright performs important functions beyond merely incentivizing production. One deleterious consequence of piracy that is often overlooked is its effect on revenue stream diversity. Why are diverse revenue streams important to producers? After all, film is a prime example of an industry that grew for more than half a century on a single revenue stream — box office receipts. Revenue stream diversity through home video formats is a recent phenomenon.

ly to consumers on Amazon. However, she subsequently signed a major publishing deal because performing all the channel functions herself meant “I hardly have time to write anymore, which sucks and terrifies me.” *Id.* at 196. Trent Reznor of the band Nine Inch Nails is another famous artist who employed a high-profile “DIY” strategy for several years before deciding that he was unable to adequately perform the channel functions alone. Marc Hogan, *How Radiohead Inspired Trent Reznor’s Return to Major Labels*, SPIN, Oct. 15, 2012, 9:47 AM ET, <http://www.spin.com/articles/trent-reznor-david-byrne-major-labels-destroy-angels-radiohead/>.

279. See Ted Sichelman, *Taking Commercialisation Seriously*, 33 EUR. INT. PROP. REV. 200 (2011) (arguing that IP regimes should take into account the investment not only in creation of IP but also in its commercialization); Adam Mossoff, *How Copyright Drives Innovation in Scholarly Publishing* (Apr. 12, 2013) (unpublished manuscript) (on file with George Mason University of Law), available at http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2243264 (arguing that current IP policy focusing on incentivizing the production of copyrighted works fails to account for publishers’ significant investment in innovative manners of commercialization and distribution).

280. See Mark Schultz & Alec Van Gelder, *Creative Development: Helping Poor Countries by Building Creative Industries*, 97 KY. L.J. 79, 116 (2008) (“Technology is greatly changing the music business, but . . . [m]usicians still need to earn a living. Production costs have declined, but they will always exist. Distribution and marketing costs have declined, but they will always exist. Food, shelter, and other necessities of life needed by those who produce music . . . are still costly.”).

The answer lies in the non-rivalrous nature of works of authorship. Because creative works can be consumed — and monetized — in a theoretically unlimited variety of formats and locales, the health of a creative industry ultimately depends on its ability to effectively monetize works for each market in which they are consumed. In Professor Paul Goldstein’s formulation, the aim of copyright is to “connect [] authors to their audiences,” and the best prescription for doing so “is to extend rights into every corner where consumers derive value from literary and artistic works.”²⁸¹ The point of this formulation is not to argue that copyright rights should be absolute, or that every use should be monetizable.²⁸² Rather, Professor Goldstein’s approach suggests a general recognition that audience consumption habits and technologies change, and that a core function of copyright is to create economic assets by which creators can derive value from each new market or use. For copyright to effectively support a professional creative class, the law must be able to follow works into the markets in which they are consumed.

The United States film industry grew for decades on a single revenue stream because the cinema was the only venue at which audiences viewed films. Of course, there was leakage even at that time,²⁸³ but the industry was still able to capture most of the revenue.²⁸⁴ When television began to broadcast movies into the home, a new point of consumption emerged, but copyright owners were able to capture the value through licensing fees. The advent of home video recording threatened to shift the landscape by empowering consumers to record, collect, and share copies of movies. The movie industry responded by seeking to eliminate or control the new technology.²⁸⁵ The industry lost the legal battle, but it figured out how to capture a great deal of the value at this new point of consumption through home video sales.²⁸⁶ The Internet presents a new front, and it remains to be seen how or whether value can be captured at its numerous points of consumption.

What happens when copyright owners are unable to monetize their works at the points where consumers derive value from them? The experience of the film and music industries in China illustrates three ways in which the diminishment of potential revenue streams

281. PAUL GOLDSTEIN, *COPYRIGHT HIGHWAY: FROM GUTENBERG TO THE CELESTIAL JUKEBOX* 216 (Stanford University Press 2003).

282. *Id.* at 214.

283. See generally KERRY SEGRAVE, *PIRACY IN THE MOTION PICTURE INDUSTRY* 25–102 (2003) (canvassing the many ways in which films were pirated from the silent era through the introduction of the consumer VCR).

284. See *id.* at 179 (“By the mid-1970s Hollywood appeared to have piracy under control. Of course, it had not been eliminated but it was seemingly a relatively minor problem.”).

285. See *Sony Corp. of Am. v. Universal City Studios, Inc.*, 464 U.S. 417 (1984).

286. See SEGRAVE, *supra* note 283, at 103–06.

harms producers: (1) monetization opportunities for smaller and independent producers are drastically reduced, (2) market signals sent to producers are reduced and distorted, and (3) producers are disproportionately exposed to the idiosyncrasies of peculiar markets and exploitation by intermediaries.

a. Reduced Revenue Stream Diversity Diminishes Monetization Opportunities for Smaller and Independent Producers

Fewer revenue streams mean fewer monetization opportunities for all market entrants. In the film context, theatrical distribution is a limited resource for which studios compete fiercely because there are no other comparable monetization options. While the Chinese box office may be booming, it is also a winner-take-all market in which a handful of big budget Hollywood and domestic films dominate box office availability and take the lion's share of revenue each year.²⁸⁷ This makes the paucity of well-developed alternative revenue streams that much more damaging to smaller domestic producers who, unlike Hollywood studios, typically cannot soften the piracy blow with substantial revenues from other markets.²⁸⁸ Legitimate online distribution has become an increasingly important source of revenue for filmmakers since major online video portals began to effectively reduce piracy and license videos, providing the first path for filmmakers to capture value from that medium of consumption.²⁸⁹ However, video portal payouts still trail far behind box office revenues.²⁹⁰

It is tautological that a reduction in revenue streams leaves producers with fewer options for monetizing their works. To at least one

287. See *Entgroup Consulting, Top 10 Characteristics of China Film Industry in 2011 I*, ENTGROUP CONSULTING (Dec. 10, 2012, 14:17, Beijing Time), http://english.entgroup.cn/views_detail.aspx?id=1275 (“In 2011 . . . 16% of all movies released [in Mainland China] accounted for 70% of box office revenue. The polarization of the Chinese film market . . . concentrating in well-funded, large-scale domestic movies and imported Hollywood films, result[s] in a severe imbalance in the Chinese film industry.”)

288. Of course, for many Chinese independent films made without state approval, limited foreign distribution is one of the few options for monetization or exposure — along with unofficial distribution outlets in China, such as cafes, small film clubs and societies, and Internet sites offering free downloads of independent films. See Reed Johnson, *China's Cinematic Revolution*, L.A. TIMES, Apr. 3, 2011, <http://articles.latimes.com/2011/apr/03/entertainment/la-ca-china-film-20110403>.

289. See *supra* Part III.B.1.b.

290. See *supra* Part III.B.1.b. The amount film producers can earn from online licensing is still dwarfed by box office revenues. To get a rough sense of online video licensing fees versus box office royalties, assume video websites' aggregate licensing payouts, the amounts of which are not all publicized, totaled \$350 million between 2009 and 2012 — a nontrivial sum, to be sure. See, e.g., YOUKU TUDOU INC., 2012 ANNUAL REPORT, *supra* note 106, at 74 (reporting the online video market leader's content-related expenditures during that period of approximately \$170 million, including licensing fees, personnel costs, and in-house content production costs). That amount equals fifteen percent of copyright owners' likely China box office share during that span.

observer, however, the hundreds of Chinese films each year that never see theatrical release are evidence of *overproduction*.²⁹¹ It is puzzling to conclude that the China film market is saturated when over ninety percent of legitimate film revenue derives from one form of distribution — theatrical — in a nation in which 12,000 screens serve a potential audience of over one billion. If the number of films exceeds available distribution channels, the problem, it seems, is not that there are too many films but rather too few legitimate distribution channels.²⁹² At the very least, there is doubtless a market for more than the three hundred films released in Chinese theaters annually. Indeed, evidence from China's online streaming video market indicates that a new, legitimate distribution channel can support the development of up-and-coming filmmakers and spark the production of new films for which there is a sizable audience.²⁹³

b. Reduced Revenue Stream Diversity Distorts Market Signals Sent to Producers

When Chinese audiences purchase or download pirated works, producers are disconnected from those choices, undermining copyright's market signaling function. When this happens, it “deprive[s] producers of the signals of consumer preference that trigger and direct their investments” in the production of new works.²⁹⁴ In the music industry, the market signals likely skew producers toward producing works that result in popular ringback tones but are not necessarily the best music by any other measure. In the film industry, where box office receipts dominate, the market signals are distorted in favor of one segment of the population — theater-going urbanites, who tend to be relatively young and wealthy — and are only meaningful to the smaller subset of producers that actually achieve theatrical distribution. As a result, feature filmmakers may seek to produce films for that demo-

291. Karaganis, *What Everyone Wants*, *supra* note 1 (“[T]he bigger problem for studios in both China and the US is probably *overproduction* For all the investment in production, only around a third of Chinese films saw domestic release in 2012. For Hollywood, the new 34-film quota may be an optimal solution that keeps attention focused on its big bets.”)

292. See Cecily Liu, *Window of Opportunity on the Entertainment Stage*, CHINA DAILY, Aug. 5, 2013, 7:18, http://www.chinadaily.com.cn/business/2013-08/05/content_16870476.htm (quoting PricewaterhouseCoopers global entertainment and media analyst Marcel Fenez as saying, “In the Chinese market, the demand for foreign films is much higher than 34. There are definitely opportunities for foreign players, but they will have to work with Chinese partners”).

293. See, e.g., Isabella Tianzi Cai, *New Hit Web Movie Marks Chinese Cinema's Online Explosion*, DGENERATE FILMS (Apr. 12, 2011, 6:54 AM), <http://dgeneratefilms.com/critical-essays/new-hit-web-movie-marks-chinese-cinemas-online-explosion> (discussing *Old Boys*, a popular web film jointly presented by China Film Group and Youku and exclusively distributed on Youku.com, which was watched over 31 million times in the first six months after its release).

294. See GOLDSTEIN, *supra* note 281, at 146.

graphic with hopes of achieving theatrical distribution, when but for piracy a far broader market would signal the need to invest in a greater variety of works. Licensed Internet distribution of online video and music is beginning to fill this gap, particularly because views and downloads are tracked and quantifiable. But market signals are only helpful if online videos generate revenue for copyright owners. Signaling is just one half of the equation, after all — there must also be sufficient promise of revenue to secure the financial backing that enables investment in new, high-quality productions.

c. Reduced Revenue Stream Diversity Disproportionately Exposes Producers to the Idiosyncrasies of Peculiar Markets and Exploitation by Intermediaries

While the effects of piracy may be palliated in box office boom times, the fact that the film industry relies almost exclusively on box office revenue renders the industry extremely vulnerable to fluctuations in the performance of that dominant revenue stream. This vulnerability is largely attributable to the high piracy rate, which deprives film copyright owners of significant potential income from aftermarket sales.²⁹⁵ Such sales could insulate domestic filmmakers from inevitable drops in box office attendance (nothing booms forever), thus helping to ensure continued production and the overall health of the industry. It can also help soften the blow of capricious actions by key intermediaries, such as when China Film Group recently decided to stop paying box office revenues to foreign studios pending the resolution of a tax dispute.²⁹⁶

The Nigerian film industry provides an object lesson in the dangers of relying solely on theatrical revenue. In the 1980s, an economic downturn, rampant crime, and problems plaguing celluloid film production forced theaters to close.²⁹⁷ Without revenue the film industry

295. See *supra* Part III.B.1.a.

296. McClintock & Masters, *supra* note 89. It is true that disproportionate exposure to the actions of key intermediaries is as much a result of China's information control regime, which vests China Film Group with exclusive film importation authority, as it is a result of piracy. But different agencies have authority for different segments of the market — DVD importation and distribution is overseen by GAPP, for example. So diversified, robust revenue streams, even in China, would help in this regard.

297. See Patrick J. Ebewo, *The Emerging Video Film Industry in Nigeria: Challenges and Prospects*, 59 J. FILM & VIDEO 46, 46 (2007); Andrew Rice, *A Scorsese in Lagos*, N.Y. TIMES, Feb. 26, 2012, at MM26, available at <http://www.nytimes.com/2012/02/26/magazine/nollywood-movies.html> (“[In] the early 1990s . . . [Nigerian m]ovie theaters were closed because no one wanted to venture into the dangerous streets at night.”). Thanks to Sean Pager for pointing out this instructive example.

collapsed,²⁹⁸ to the point where as few as two Nigerian films were produced each year.²⁹⁹

China's mobile music market throws the piracy and revenue diversity problem into even sharper relief. Recall that ninety percent of the industry's anemic annual revenue derives from a single source: mobile music, which is largely comprised of CRBT revenue.³⁰⁰ On top of that, the dominant mobile music distributor, China Mobile, is a state-controlled monopoly occupying two-thirds of the Chinese mobile market.³⁰¹ To its suppliers — music companies — China Mobile is therefore a monopsonist.³⁰² As is generally the case with monopsonies, the supplier is exposed to a significant risk that it cannot extract the fair value of its contribution to the service. In theory, copyright owners could negotiate higher royalty rates and exclusive licenses with competing service providers. However, this is not a realistic option where one service provider controls a large share of the market. Regardless, copyright owners likely would have little negotiating leverage even among competing service providers because consumers likely deem CRBTs to be a luxury value-add, not a primary consideration when selecting a service provider. It is unlikely that many prospective subscribers would sign up with one mobile provider over another based on CRBT song selection rather than considerations such as price or coverage.

The difference between China's music and film industries is one of degree rather than kind. Just as China's film industry's fortunes rise and fall with the idiosyncrasies of theatrical distribution, the recording industry's fortunes are inextricably tied to the idiosyncrasies of the CRBT format. If and when the CRBT format grows stale for consumers, ninety percent of music companies' income is at risk — regardless of the CRBT distributor.³⁰³ The effect of piracy reducing the number of available revenue streams is therefore doubly damaging to the music industry, whose income is tied to the whims of a single revenue-generating format that is controlled by a monopsonist. If music companies could diversify their revenue by effectively exploiting their copyrights in China — through monetized online downloads, sub-

298. See Ebewo, *supra* note 297, at 46.

299. Sean A. Pager, *Folklore 2.0: Preservation Through Innovation*, 2012 UTAH L. REV. 1835, 1853 (2012).

300. See *supra* Part III.C.1.c.

301. Christina Lo, *China's Mobile Subscribers up 1 Pct at 1.13 Bln in Feb*, REUTERS (Mar. 20, 2013), <http://www.reuters.com/article/2013/03/20/china-mobilesubscribers-idUSL4N0BK3J120130320> (reporting China Mobile's subscriber base was 720 million in the first quarter of 2013, approximately sixty-four percent of the total 1.13 billion wireless subscribers in China).

302. A monopsony exists when there is only one buyer of a well-specified good or service. ROGER D. BLAIR & JEFFREY L. HARRISON, *MONOPSONY IN LAW AND ECONOMICS* 41 (2010).

303. See Tan, *supra* note 71.

scription streaming, CD sales, and so on — they might be in a better position to weather fluctuations or downturns in the fortunes of the CRBT format. Equally importantly, diverse revenue streams might provide music companies with the leverage and financial fortitude to negotiate a better deal with mobile service providers or else remove their content altogether. Agreements such as the search engine licensing deals discussed in Part III.C.1.a above are a positive first step toward counterbalancing mobile music revenue, at least for the international major record labels.³⁰⁴ However, to forgo, or credibly threaten to forgo, mobile music revenue, record labels must earn far more from such licensing deals than they presently do.

Finally, there is the fundamental issue of fairness. Why should others derive the vast majority of the benefits of the record label's investment in the production of the music? This highlights the point that a robust copyright system helps ensure that creators reap the fair rewards of their efforts by creating markets for diverse uses of creative works. The varied revenue streams that result not only enable copyright owners to recoup their investment, but also provide insurance and leverage against exploitation.

B. Responding to Theme #2: "Piracy Benefits Creators and Consumers by Lowering Access Barriers to a Wide Variety of Information Goods."³⁰⁵

Piracy doubtless increases public access to creative works, which leads to a short-term increase in welfare for consumers and creators of prospective works. This can be particularly helpful to creators, who draw inspiration, memes, themes, style, and countless other ideas from pre-existing works. There are two problems with the argument that piracy increases creative output in China by increasing access, however: (1) it erroneously assumes that legitimate sources of creative works are not readily available, and (2) it prioritizes short-term but lesser welfare gains over long-term, greater welfare gains.

1. Legitimate Sources of Creative Works Are Readily Available in China.

In reality, legitimate on-demand music and video have been readily available at a reasonable price for several years in China. It is true that censorship limits the availability of musical and audiovisual works through official channels.³⁰⁶ However, even this problem is exaggerated. For several years, online services that often reside in the

304. See *supra* Part III.C.1.a.

305. See *supra* Part IV.B.

306. See *supra* Parts III.B.2 & III.C.2.

interstices of SARFT and MOC content regulations have provided licensed access to a surprisingly broad array of music and audiovisual content.³⁰⁷ On the music front, legitimate domestic music services have been around for years, including Top100.cn, which launched a music subscription service in 2006, and 9Sky, which like Top100.cn had a large catalog of Chinese and international artists and charged a mere \$3 per month for unlimited access.³⁰⁸ Top100.cn eventually partnered with Google China to provide a legitimate ad-supported music download service that was free to consumers. However, neither Top100 nor 9Sky could ultimately compete with free unauthorized downloads, so Top100 was shuttered and 9Sky, while still operational, has become a marginal player in China's online music space.³⁰⁹ Other domestic services have stepped in to fill the void, including domestic MP3 search services Baidu Music and Sogou, and domestic streaming services like QQ Music, Douban.fm, and Xiami,³¹⁰ which was recently acquired by Chinese e-commerce giant Alibaba.³¹¹ While there is still some ambiguity about how much of the music in their catalogs is fully licensed, these sites are continuing to strike deals with music content owners and so at the very least are moving in the direction of legitimacy.³¹² On the independent music front, since 2008 WaWaWa has made licensed music available from a vast catalog of

307. See *supra* Parts III.B.2.d. & III.C.2.

308. See Eric Priest, *Why Emerging Business Models and Not Copyright Law Are the Key to Monetising Content Online*, in COPYRIGHT LAW, DIGITAL CONTENT, AND THE INTERNET IN THE ASIA-PACIFIC 119, 133 (Brian Fitzgerald et al. eds., 2008). Even digital rights management ("DRM") has rarely been a sticking point for online content in China. For example, 9Sky reportedly did not generally wrap its digital music files in DRM, although its agreements with the international major labels apparently required it to do so. *Id.* at 10.

309. See Michael Kan, *Google Yanks Free Music Service in China*, PCWORLD (Sept. 21, 2012, 6:54 AM), <http://www.pcwORLD.com/article/2010313/google-yanks-free-music-service-in-china.html> (reporting that Google ended its partnership with Top100.cn because their music download service "wasn't popular enough"); Tracey Xiang, *How's the Reconstruction of China Digital Music Market Going?*, TECHNODE (Sept. 17, 2013), <http://technode.com/2013/09/17/hows-the-reconstruction-of-china-digital-music-market-going/> (reporting that Top100.cn shut down one year after Google pulled out of the partnership); Ed Peto, *Music Ally Report 337 — China's Great Digital Leap Forward*, MUSIC ALLY (Mar. 5, 2014), <http://musically.com/2014/03/05/music-ally-report-337-chinas-great-digital-leap-forward/> (discussing the emergence of "a handful of strong, ad-supported streaming services" in the Chinese online and mobile app music space, listing QQ Music, Kugou, Kuwo, Baidu Music, Xiami, Douban, NetEase, and Nokia's MixRadio, but failing to list 9Sky among the major players in this space).

310. See *supra* Part III.C.1.a.

311. See Alexander C. Kaufman, *Alibaba Buys Xiami, Major Music Streaming Site, in Next Step To Take Over China's Music Industry*, INT'L BUS. TIMES (June 4, 2013, 9:43 AM), <http://www.ibtimes.com/alibaba-buys-xiami-major-music-streaming-site-next-step-take-over-chinas-music-industry-1290331>.

312. See *supra* Part III.C.1.a.

Chinese and foreign independent artists and labels for a mere \$0.03 per song.³¹³

On the video front, more recently thousands of licensed domestic, regional, and international films and TV shows have been made available on Chinese video sites such as Youku, Tudou, Tencent Video, and Sohu, some under an ad-supported model and others as “premium” content behind a paywall that charges as little as 5 RMB (less than \$1) per view.³¹⁴ Youku alone has licensed more than 3,600 television shows, and more than 4,500 domestic and foreign films.³¹⁵ Since the websites’ licensing deals for foreign content do not involve theatrical distribution, these films are not subject to the thirty-four-film import quota.³¹⁶ In addition, websites such as Youku feature many user-generated videos of increasingly high quality.³¹⁷ In short, the argument that piracy is required to provide reasonable access to a large amount of video and music content in China is wrong. While plenty of content remains available through piracy, over the past decade Chinese creators have had access to a multitude of legitimate, reasonably priced sources.

313. See Erik Rostad, *WaWaWa*, EPR CREATIONS (Aug. 5, 2008), <http://www.eprcreations.com/wawawa/>; WAWAWA, <http://www.wa3.cn/home.htm> (last visited Feb. 10, 2014).

314. See Jonathan Landreth, *Youku.com Buys Online Rights to 'Inception' for China*, HOLLYWOOD REP. (Jan. 24, 2011, 6:34 PM), <http://www.hollywoodreporter.com/news/youkucom-buys-online-rights-inception-68345> (“[Youku is charging] customers of its paid, advertisement-free video-on-demand service 5 yuan (\$0.75) each to see the global blockbuster [Inception].”); SOHU.COM, SOHU.COM 2012 ANNUAL REPORT 8–9 (2013) (reporting that the company’s “extensive and comprehensive content library comprises licensed high definition popular television dramas, variety shows, in-house produced content, and user-generated content,” and that while its “online video revenues are primarily derived from advertising services,” it offers “selected premium content such as high definition movies, educational content, and documentaries on [an] advertisement-free paid channel”); TENCENT, TENCENT HOLDINGS LIMITED 2012 ANNUAL REPORT 9, 18 (discussing monetization of the company’s video platform through advertising and the “significant” content costs the company incurred in 2012); Steven Millward, *Tencent: Our Video Site Is Now China’s Biggest, Ready To Charge for Hollywood Movies*, TECHINASIA (Dec. 21, 2012, 11:15 AM), <http://www.techinasia.com/tencent-video-site-hollywood-content/> (noting Chinese web giant Tencent’s investment in video content licenses and its experimentation with a premium video-on-demand service).

315. See YOUKU TUDOU INC., 2012 ANNUAL REPORT, *supra* note 106, at 40.

316. See Ross, *supra* note 121 and accompanying text.

317. See Press Release, Youku Tudou, Inc., Mobile Video Contest Co-Hosted by China Mobile and Youku Tudou Breaks New Records, Generating More than 100 Million Yuan in Mobile Box Office Sales (Jan. 8, 2014), <http://ir.youku.com/phoenix.zhtml?c=241246&p=irol-newsArticle&id=1888991> (discussing amateur filmmaking competitions hosted by Youku Tudou that receive tens of thousands of submissions annually and hundreds of millions of views, designed to identify and nurture high quality user-generated content).

2. Piracy's Long-Term Harms to Creators Outweigh Its Short-Term Benefits.

More importantly, if this Article's contention in response to Theme #1 above is correct — that the key inquiry concerning the role of copyright should be whether or not the creative industries are positioned to support a professional class of creators — then the social welfare gains from piracy-enabled access are short-lived. The more meager the returns on a creative industry's investment in new works, the lower the likely number of high production value, high quality works the industry will produce.

The respective trajectories of the Chinese movie and music industries are instructive in this regard. A decade ago, piracy plagued both industries and neither had the means to monetize their works on a large scale. Revenues from both industries at that time were roughly similar — about \$200 million for the music industry in 2003,³¹⁸ compared to about \$250 million in annual box office revenues.³¹⁹ Then the film industry's fortunes began to change dramatically. More investment in distribution infrastructure — modern theaters — coupled with an increase in the disposable income of Chinese consumers led to the box office boom discussed in Part III.B.1, above. Now film industry revenue stands at more than \$3 billion annually.³²⁰ By contrast, over the same decade, Chinese music industry revenues have declined by more than \$100 million.³²¹ In fact, the only reason that recorded music revenue has not collapsed altogether is that by happy circumstance, Chinese consumers like ringback tones — unlike their American counterparts³²² — and mobile companies direct a tiny percentage of CRBT revenue to the content owners.³²³ The key difference between the film and music industries is that the former benefits from theatrical distribution, a scalable, exclusion-based monetization model that is moderately resistant to piracy, while the latter does not. As argued in Part V.A.2.c, above, a film industry dominated by theatrical revenue fails to capture a great deal of value from non-theatrical consumption, to the long-term detriment of the industry. But the rapid simultaneous growth of theatrical revenue and the film industry does demonstrate the direct link between increased monetization and increased investment in production.

318. IFPI, THE RECORDING INDUSTRY COMMERCIAL PIRACY REPORT, *supra* note 171, at 8.

319. See Priest, *supra* note 9, at 798.

320. McClintock, *supra* note 84.

321. *Recording Industry in Numbers 2012*, *supra* note 173, at 62.

322. See, e.g., Sandhva Raman, *Ringback Tones a Failure in the United States — But Why?*, FIERCE MOBILE IT (June 6, 2011), <http://www.fiercemobilecontent.com/special-reports/ringback-tones-failure-united-states-why>.

323. See Yang Yang, *supra* note 212.

The increase in Chinese box office revenue has been a boon for Hollywood, but the biggest beneficiary has been the domestic film industry. With resources to invest, China's movie industry is putting out more films of higher quality than ever before in its history.³²⁴ In 2011, 791 domestically produced films were officially released in China, earning a total of \$1.11 billion — 53.6% of 2011 ticket sales — with twenty films earning more than \$16 million.³²⁵ This total included many smaller domestic productions, a number of which competed well against foreign blockbusters.³²⁶ One locally-produced hit, *Love Is Not Blind*, cost a mere \$1.6 million to produce, but grossed \$43 million.³²⁷ Another low-budget comedy, *Lost In Thailand*, trounced numerous Hollywood blockbusters, including *Skyfall* and *The Hobbit: An Unexpected Journey*, at the Chinese box office.³²⁸ In the first quarter of 2013, domestically produced films earned twice as much as imports.³²⁹ Given the extraordinary popularity of online music in China,³³⁰ China's domestic music industry could have the potential to experience a similar boom but for the lack of a similar exclusionary monetization model. Because the music industry's principal means of monetization, other than the CRBT model, is through exploitation of copyrights, piracy is almost singularly to blame for the industry's present woes.³³¹

*C. Responding to Theme #3: "Piracy Incentivizes Copyright Owners To Adopt Innovative Business Models."*³³²

Regarding the claim that piracy is driving business model innovation in China, current circumstances do not present a ringing en-

324. See, e.g., Julie Makinen, *China's Movie Box Office Surges 27% to \$3.6 Billion in 2013*, L.A. TIMES, Jan. 1, 2014, <http://articles.latimes.com/print/2014/jan/01/business/la-fi-ct-china-box-office-20140102> (quoting Asia film industry expert's observation that "[a]s Chinese filmmakers continue to refine their craft, local audiences are finding relatable stories packaged together with high-production-quality content").

325. Coonan, *supra* note 84.

326. See *id.*

327. *Id.*

328. See Clarence Tsui & Karen Chu, *China Box Office: Local Films Rule First Quarter of 2013*, HOLLYWOOD REP. (Apr. 1, 2013, 9:19 AM), <http://www.hollywoodreporter.com/news/china-box-office-local-films-431967>.

329. *Id.*

330. See *supra* notes 163–164 and accompanying text (noting that music is the third most popular network application in China, with more than seventy-seven percent of Chinese netizens consuming music online).

331. It is worth noting that music executives decry several factors besides piracy that have led to stagnation and decline in the Chinese music industry, such as the inequitable distribution of profit by distributors, including mobile operators, to copyright owners. See Yang Yang, *supra* note 212. As this Article shows, however, piracy is the primary root of these evils as well, since it strips music copyright owners of the economic leverage to renegotiate and enforce their deals with distributors. See *supra* Part V.A.2.c.

332. See *supra* Part IV.C.

dorsement of piracy. There is scant business model innovation in the movie industry, which relies almost entirely on its oldest form of monetization: box office revenue. While copyright owners are licensing their works to online streaming services, there is little evidence that these deals are driven by piracy. Indeed, this form of monetization is made possible because the major online video portals have increasingly shunned piracy and purchased licenses for the films and television programs they distribute.³³³ Perhaps piracy has hastened the transition to online streaming for many copyright owners, but the shift was inevitable as TV distribution is far more restricted than online distribution and Chinese are increasingly consuming their content online.

Piracy has forced record companies worldwide to scramble in an attempt to diversify their revenue streams. So far, however, the results have been underwhelming in China. Music copyright owners have experimented online with free, ad-supported MP3 downloads. The experiment failed in its first incarnation, a music service operated by Google and Chinese online music retailer Top100.cn.³³⁴ Record labels have also supported online streaming, which is growing in popularity but is not generating significant revenue.³³⁵ Labels did embrace mobile music and CRBTs early on, but it is unlikely that piracy was the reason. CRBTs are provided through a paid service that charges recurring monthly fees,³³⁶ so the labels would have embraced this promising, steady revenue stream even in a low-piracy environment. Labels also routinely employ “360 deals” to partake in artists’ live performance revenue and sponsorships.³³⁷ As with box office revenue in the film industry, however, live performance and patronage are the oldest forms of music revenue and hardly smack of innovation.³³⁸

In short, there is little evidence that piracy has driven the adoption of new business models in the film and music industries, save perhaps hastening the inevitable move to cloud-based distribution. This benefit is hardly worth the harsh toll that piracy has exacted on China’s creative industries. Indeed, it is because of piracy that labels have had so little leverage to enforce their agreements with mobile providers and maximize the CRBT revenue stream opportunity.

333. See *supra* Part III.B.1.b.

334. See Kan, *supra* note 309, and accompanying text.

335. See *supra* Part III.C.1.a.

336. See *supra* note 207 and accompanying text.

337. See *supra* note 258 and accompanying text.

338. See Schultz, *supra* note 72, at 750.

*D. Responding to Theme #4: "Piracy Is Especially Important for Political Discourse in China Because It Helps Information Goods Circumvent Heavy-Handed State Censorship Policies."*³³⁹

Because of China's pervasive media censorship rules, many foreign and domestic films and songs have no legitimate distribution channel in China. The only way these works can be accessed in China is through illegitimate channels — in other words, piracy. Moreover, because both copyright and censorship rules limit access to information goods and involve questions of their "legality," the line between copyright enforcement and censorship often blurs. It is not uncommon, therefore, for official raids under the auspices of anti-piracy to target banned works as well.³⁴⁰ The nexus between censorship and copyright raises profound issues of free expression and social welfare, and is the strongest argument that piracy improves social welfare in China.

However, copyright skeptics overestimate the role of piracy as a vehicle for free expression. Piracy does provide the public with access to a far greater variety of works and thematic content than official media sources. But piracy is far from a censorship-free safe zone. One is unlikely to find the average DVD street vendor selling hardcore pornography or video documentaries of the Tiananmen massacre, for example. Chinese websites that host unlicensed copyrighted content are even more likely to avoid or remove banned or overtly sensitive political content.³⁴¹ Purveyors of pirated works are not free speech activists; they are businesspeople.³⁴² Pirates are bound to self-censor as much as anyone who wants to stay in business.

More importantly, copyright skeptics underestimate the positive effect of the market on free speech in China. An inherent tension exists in China's efforts to privatize sectors of the economy once dominated by state enterprises,³⁴³ including the media sector.³⁴⁴ On the one hand, state information control remains a bedrock principle of Chinese Communist Party rule. On the other hand, as the media sector

339. See *supra* Part IV.D.

340. See, e.g., Stephen McIntyre, *The Yang Obeys, but the Yin Ignores: Copyright Law and Speech Suppression in the People's Republic of China*, 29 PAC. BASIN L.J. 75, 125 (2011).

341. Clifford Coonan, *China's Censors Clamp Down on Booming Internet Video Sector*, HOLLYWOOD REP. (Mar. 20, 2014, 12:48 PM PDT), <http://www.hollywoodreporter.com/news/chinas-censors-clamp-down-booming-689865> (noting that Chinese officials are strengthening the censorship review process for video content distributed online, and that to date video websites have been "doing their own internal censorship").

342. See MONTGOMERY, *supra* note 1, at 54 (observing that commercial piracy in China is "wholly driven by profit").

343. See generally BARRY NAUGHTON, *THE CHINESE ECONOMY: TRANSITIONS AND GROWTH* 91–98 (2007).

344. See Creemers, *Explaining Audiovisual Media Piracy*, *supra* note 9, at 109–13.

becomes increasingly privatized, it becomes more profit-centered and market-oriented.³⁴⁵ Copyright and First Amendment scholar Neil Weinstock Netanel argues that copyright has a “structural function” in democratic societies that is central to its role as an “engine of free expression”:

Copyright does not serve merely to attain a desired quantity of creative expression. It also underwrites a particular type of speech and speaker. Copyright supports a market-based sector of authors and publishers, those who look to paying audiences (and advertisers) [rather than to government subsidies or elite patronage] for financial sustenance. It fosters those sustained works of authorship that would unlikely be created if not for the opportunity to market copies and other forms of access.³⁴⁶

According to Netanel, this function persists even in an era of highly commercial mass communication.³⁴⁷ China is far from a democratic society, but even in the shadow of authoritarianism, public exposure to commercial media “tends to erode passive acceptance of authoritarian power relations.”³⁴⁸

To see how the shift toward media privatization can soften censorship around the edges, one need only look to the impetus for instituting the foreign film quota in the 1990s. Most Westerners focus on the limiting effects of the quota, but it is interesting to consider why an authoritarian state would have established a quota to ensure Western blockbusters are screened in theaters where the usual fare had been propaganda films. Unsurprisingly, blockbusters were imported to increase cinema attendance, bolstering China’s film sector.³⁴⁹

The development of an economically robust and increasingly private media sector undergirded by copyright has expanded demonstrably the limits of officially tolerated speech in China. Since Chinese consumers have proven to like much of what censors aim to expurgate, media content producers and distributors continually push the envelope of permissible content, and they have been successful at

345. See generally DANIELA STOCKMANN, MEDIA COMMERCIALIZATION AND AUTHORITARIAN RULE IN CHINA (2013) (examining the effect of increasing marketization of newspapers on the production of news media and credibility of news sources in China).

346. NEIL WEINSTOCK NETANEL, COPYRIGHT’S PARADOX 89 (2008).

347. *Id.* at 92–94; see also Mark P. McKenna, *Intellectual Property, Privatization, and Democracy: A Response to Professor Rose*, 50 ST. LOUIS U. L.J. 829, 841–42 (2006) (arguing that IP rights play a valuable role in promoting democracy, and providing examples of how IP can favor “the little guy[]” as much as powerful companies).

348. Neil Weinstock Netanel, *Asserting Copyright’s Democratic Principles in the Global Arena*, 51 VAND. L. REV. 217, 253 (1998).

349. See Creemers, *Explaining Audiovisual Media Piracy*, *supra* note 9, at 113.

moving the goal posts. Consider the SARFT rule excerpted in Part III.B.2.b, above, prohibiting graphic violence, murder, and excessively horrific images. There is a yawning gap between what is officially proscribed in the rule and what has actually been permitted to screen in China. For example, several recent American films have screened in China despite containing generous amounts of ostensibly verboten horror and violence, including *Resident Evil: Retribution*; *The Hobbit: An Unexpected Journey*; and *Django Unchained*. True, such films are frequently altered before they receive final SARFT approval. The bloody Quentin Tarantino western *Django Unchained*, for example, was approved for release in China, then yanked from Chinese theaters on opening day before being re-released a month later with three minutes of violence and nudity excised.³⁵⁰ Nevertheless, even the sanitized versions are a far cry from pre-reform-era propaganda films and the kinds of sanctimonious socialist fare that SARFT regulations envision. The approval of violent time-travel drama *Looper* for co-production and distribution in China, SARFT time-travel bans notwithstanding, is another instructive example.³⁵¹ Piracy is an important tool of free expression in China for its ability to deliver uncensored, unsanctioned works to a mass audience. However, the real aspiration of free speech proponents in China is expanding the boundaries of *officially* tolerated expression.

Both piracy and copyright currently play important roles in advancing free expression in the shadow of China's pervasive state information controls. To maximize the creative industries' potential to pressure and change censorship policy, however, the desired trend should be toward empowering and expanding China's creative class — a goal profoundly impeded by the economic harm and exploitation wrought by piracy.³⁵² In the context of audiovisual works, Internet distribution could aid this trend by establishing a middle ground between monetized, official theatrical distribution and unremunerated piracy. SARFT's relatively light-handed approach to online distribution of original video content, illustrated in the micro movie trend discussed in Part III.B.2.d, allows space for independent filmmakers to openly distribute unsanctioned works and even monetize them through ad revenue-sharing arrangements with online video platforms.³⁵³

350. Clarence Tsui, 'Django Unchained' Reopens in China with Nudity and Screenings Reduced, HOLLYWOOD REP. (May 13, 2013, 2:51 AM PDT), <http://www.hollywoodreporter.com/news/django-unchained-reopens-china-nudity-521650>.

351. See discussion *supra* Part III.B.2.

352. See Jingying Li, *supra* note 1, at 556 (acknowledging that the relationship between copyright pirates and Chinese independent filmmakers is "no honeymoon" and reporting that "many filmmakers have complained about the exploitative nature of the pirate industry").

353. It appears that Chinese officials are taking a stronger position toward censoring online content, including a new requirement that online video sites employ government-

*E. Responding to Theme #5: "Piracy Benefits Foreign Rights Holders in China by Providing Free Advertising and Branding for Their Works."*³⁵⁴

The reasoning here seems straightforward. Even if consumers are only enjoying pirated copies of your product, the product is still gaining critical exposure, and surely you can monetize the resulting mind share and consumer path dependence. Unfortunately, there are serious flaws in this logic.

Entrenched stakeholders are hard to dislodge, and piracy itself can shape consumption habits. Weaning long-time users off of inexpensive pirated goods is difficult. Raustiala and Sprigman, as well as Karaganis, highlight Microsoft as an example of a company that employs a piracy-as-branding strategy.³⁵⁵ Raustiala and Sprigman use it to illustrate how "[i]n the longer term, open copying may build demand for Western innovations."³⁵⁶ They note Bill Gates's candid revelation in 1998 that "[a]s long as [Chinese users are] going to steal [software], we want them to steal [Microsoft's]. They'll get sort of addicted, and then we'll somehow figure out how to collect sometime in the next decade."³⁵⁷ More than a decade after Gates's remark, however, not much has changed for software producers in China, including Microsoft. Software industry trade group BSA: The Software Alliance estimates that seventy-seven percent of software in China is still pirated.³⁵⁸ China's entire legitimate software market remains just one-fifteenth the size of the United States market.³⁵⁹ Microsoft recently reported that it generates more revenue in the Netherlands than in China, leading a CNN columnist to write that "China has been a piracy trap for Microsoft" where "profit has proved elusive."³⁶⁰ As consumers migrate from PCs, where Microsoft is dominant, to newer

approved censors to review content. Coonan, *supra* note 341. While it is too early to tell whether this signals a policy of far stricter online video censorship akin to that employed for film production and importation, the odds are that the proverbial cat is out of the bag with respect to online video, and censors will continue to be more permissive with respect to online content distribution.

354. See *supra* Part V.E.

355. Raustiala & Sprigman, *supra* note 1, at 29; see also Karaganis, *Forget It Jack, It's Chinatown*, *supra* note 1 (noting that "some software executives . . . can be indiscreet about the role piracy plays in their business strategies" and linking to a news article about Microsoft's acknowledgement that piracy "helps the company establish itself in emerging markets and fend off threats from free open-source programs" (quoting Charles Piller, *How Piracy Opens Doors for Windows*, L.A. TIMES, April 9, 2006, <http://articles.latimes.com/2006/apr/09/business/fi-micropiracy9> (internal quotation marks omitted))).

356. Raustiala & Sprigman, *supra* note 1, at 29.

357. *Id.*

358. BUSINESS SOFTWARE ALLIANCE, SHADOW MARKET: 2011 BSA GLOBAL SOFTWARE PIRACY STUDY 4 (9th ed. 2012).

359. *Id.*

360. John Foley, *Microsoft Stages Nebulous Chinese Comeback*, CNN MONEY (May 29, 2013, 10:58 AM ET), <http://tech.fortune.cnn.com/2013/05/29/microsoft-china-piracy/>.

mobile devices and cloud-based computing services, where it is not,³⁶¹ Gates's piracy-to-profit strategy in China increasingly looks like a losing bet. The music industry's experience in China has been even worse. Ubiquitous music piracy has only begotten more piracy, and industry revenue is half of what it was a decade ago.³⁶²

Professors Mark Schultz and Alec Van Gelder highlight the implicit caveat to the piracy-as-branding rationale: In order to benefit the copyright owner, "any giveaway must serve as advertising for *some* revenue producing product or service."³⁶³ Piracy-as-branding does not solve the systemic causes of piracy in China, and copyright owners still face the challenge of somehow monetizing their works. This is an especially difficult challenge when the primary revenue-generating product — the item being advertised — is also the item being pirated. Of course, there are monetizable services for which piracy can serve as advertising. In the music industry, some pirated songs can heighten interest in their artists' live performances. The argument that live performance income is a reasonable substitute for recorded music revenue has serious shortcomings, however.³⁶⁴ Only a small percentage of Chinese artists can make a living from live performances in China, and any advertising benefit that Western artists derive from piracy in China is not helping to fill seats at many concerts.³⁶⁵ There are other major shortcomings in this model as well: increasing the number of

361. Liam Tung, *Windows Phone Growth Plateaus in Europe, Xiaomi Beats Samsung in China*, ZDNET (Jan. 27, 2014, 12:57 GMT), <http://www.zdnet.com/windows-phone-growth-plateaus-in-europe-xiaomi-beats-samsung-in-china-7000025613/> ("In China, [Microsoft] Windows Phone's [operating system] market share is 1.1 percent, behind iOS at 19 percent and Android at 78.6 percent.").

362. See *supra* notes 171–173 and accompanying text.

363. Schultz & Van Gelder, *supra* note 280, at 115.

364. See Schultz, *supra* note 72, at 750–54; Jiarui Liu, *supra* note 9, at 636–37 ("It is somewhat ironic that when Chinese artists are finally able to directly distribute their works to consumers free from the physical constraints of compact discs and record shops, they end up having to depend more on other forms of physical constraints, such as theaters or stadiums, to earn a decent living.").

365. See *China Wests Steve Sybesma: An Interview*, CHINA MUSIC RADAR (Jan. 17, 2009), <http://www.chinamusicradar.com/china-west/china-wests-steve-sybesma-an-interview> ("Most foreigners in China's live music game (including those in the industry) would have assumed that a megastar like Kanye [West] would be a big draw here in China; hip hop is one of the most popular genres amongst the kids in first tier cities [But] Kanye didn't approach the realm of selling out the 9,000-capacity Shanghai Grand Stage, and . . . not even the cheap seats sold out Even Avril Lavigne — the second most played contemporary international artist on Chinese radio — didn't manage to shift tickets on her Fall '08 tour."); see also *Money Money Money — 2013's State of the Union*, CHINA MUSIC RADAR (July 31, 2013), <http://www.chinamusicradar.com/live-music/money-money-money-2013s-state-of-the-union/> ("[T]he overwhelming preference [in China] is still for domestic (Mandarin Chinese speaking) talent Chinese media is still relatively disinterested in all but the hottest international celebrity talent . . . so fan acquisition is an incredibly expensive exercise.").

live performances can take a serious physical toll on artists,³⁶⁶ many artists do not perform live at all, and some records would be poor advertisements for the live show even if the artist were to perform.³⁶⁷ To the last point, Professor Schultz observes that the Beatles' *Sgt. Pepper's Lonely Hearts Club Band* album "was an artistic and technological masterpiece, not an advertisement for a touring band," especially since the Beatles never toured again.³⁶⁸

The piracy-as-branding theory has more purchase in the context of the film industry, whose dominant revenue stream in China derives from an excludable service — theatrical exhibition — that in theory could benefit from piracy-as-branding. Piracy doubtless has exposed Chinese audiences to a broader array of genres and films than would have been possible in China but for piracy, as Karaganis suggests.³⁶⁹ Still, the notion of "branding" entire filmmaking styles and genres is at best nebulous; it is difficult to measure whether piracy provides tangible marketing or branding benefits to foreign copyright owners. Is it reasonable to assume that fewer Chinese viewers would watch Hollywood movies in theaters today had previous Hollywood films not been available via piracy? Even if film piracy served to introduce Hollywood's brand of filmmaking to Chinese audiences in the 1980s and 1990s, the argument no longer has force. Chinese film audiences are now well acquainted with international films. In fact, piracy may even be *overexposing* Hollywood films to Chinese consumers, potentially contributing to genre fatigue.³⁷⁰ There is simply little reason to

366. Paul Resnikoff, *Let's Add 'Burnout' to the List of Artist Problems . . .*, DIGITAL MUSIC NEWS (Apr. 24, 2013), <http://staging.digitalmusicnews.com/permalink/2013/04/24/artistburnout>.

367. Schultz, *supra* note 72, at 754.

368. *Id.*

369. Karaganis, *What Everyone Wants*, *supra* note 1 ("[P]iracy has a secondary function as a channel for brand development, educating Indians and Chinese in the norms and values of Hollywood. Enforcement in this context is double-edged. Would Hollywood have benefited in the past decade from stronger enforcement and diminished exposure of its films outside the few legal theatrical venues?").

370. See Michael Cieply, *U.S. Box Office Heroes Proving Mortal in China*, N.Y. TIMES, Apr. 21, 2013, <http://www.nytimes.com/2013/04/22/business/media/hollywoods-box-office-heroes-proving-mortal-in-china.html> (discussing "a rapid evolution in the tastes of Chinese audiences, which are quickly turning away from the spectacles American companies have assumed they crave"). Overexposure via piracy may be a real concern for IP owners. Raustiala and Sprigman argue that "[i]n a huge but largely untapped market such as China, exposure, and the prospect of growth tomorrow, can trump greater market share today. And although shanzhai [imitation] products are celebrated, those Chinese who can buy the original products generally do." Raustiala & Sprigman, *supra* note 1, at 28. In fact, however, luxury goods bearing brand logos such as Louis Vuitton's "LV" that seem almost ubiquitous in China are therefore increasingly viewed as commonplace, turning off wealthy Chinese consumers. Surely the great abundance of counterfeit luxury products on the market and in use by average Chinese consumers is not helping luxury brand owners in this regard. See Sonia Kolesnikov-Jessop, *Toning Down the Bling Factor*, N.Y. TIMES (Sept. 10, 2012), <http://www.nytimes.com/2012/09/11/business/global/toning-down-the-bling-factor.html> (reporting that while luxury brand revenues continue to increase in China, increasingly sophisticated wealthy consumers "don't want Louis Vuitton any more because it's become

believe that copyright owners would be missing out on a golden branding opportunity in China if effective copyright enforcement were within their grasp.

*F. Responding to Theme #6: “Foreign Dominance Poses a Greater Threat to China’s Cultural Industries than Piracy Does.”*³⁷¹

This theme rings of broader anxiety over “cultural imperialism” expressed by many sovereigns over the importation of large quantities of foreign content, particularly Hollywood movies.³⁷² The underlying concern is that “big markets,” such as the United States, leverage their wealthy “home base” audience to fund bigger, more attractive productions that ride their competitive advantage over local content to widespread popularity.³⁷³ The foreign works, cultural protectionists argue, encroach on the “cultural sovereignty” of the importing state and pollute the process of national cultural development.³⁷⁴ As described in Part III, above, China’s cultural protectionism is second to none.

There is great cause to doubt the validity of the cultural imperialism thesis in general,³⁷⁵ however, and there is little evidence that foreign content, even Hollywood content, poses a greater threat to China’s creative industries than piracy does. In fact, if anything, the evidence points in the opposite direction: domestic creative industries that can successfully monetize their works are in a better position to compete with foreign productions.³⁷⁶ High piracy rates that hurt the ability to monetize creative works tend to hurt domestic productions more than imports, particularly if no other significant domestic monetization models exist. This is because smaller domestic producers are in a far worse position to withstand the effects of piracy than international producers, who can often subsidize runs in high-piracy markets with earnings from copyright-friendly markets.³⁷⁷

The Chinese music and film industries both suffer from high levels of piracy. Nevertheless, both have been able to compete well against foreign content in recent years notwithstanding high rates of

too common” as “[t]hey are trying to differentiate themselves and not have the same logos and the same brands that have been so popular for the last ten years” (quoting China consumer market analyst Shaun Rein)).

371. See *supra* Part IV.F.

372. See Sean A. Pager, *Beyond Culture vs. Commerce: Decentralizing Cultural Protection To Promote Diversity Through Trade*, 31 NW. J. INT’L L. & BUS. 63, 69–72 (2011) (noting that many governments perceive cultural imports from large markets as a threat to their “cultural sovereignty”).

373. *Id.* at 69.

374. *Id.* at 71.

375. See generally *id.* at 74–97.

376. See Jiarui Liu, *supra* note 9, at 657–58; Schultz & Van Gelder, *supra* note 280, at 121.

377. See Jiarui Liu, *supra* note 9, at 658; Schultz & Van Gelder, *supra* note 280, at 121 (making the same argument in a generalized, not China-specific, context).

piracy. The film industry has experienced growth and increased investment in new productions because it enjoys stable and substantial theatrical revenue, and has been able to compete well with foreign films as a result. Total box office revenue from domestic films is about equal to that of foreign films.³⁷⁸ Of the ten all-time highest-grossing films in China, six are domestic productions.³⁷⁹ The quality of domestic films continues to improve as increased revenue allows the industry to invest more in production and benefit from gains in experience and professionalism.³⁸⁰ This, in turn, should help the local industry become even more competitive. There are, of course, many factors contributing to the competitiveness of local films. Censorship rules that limit market access and screen time for foreign films, for example, doubtless create space for local industry.³⁸¹ But financial health is the biggest factor contributing to the Chinese film industry's competitiveness.

A 2010 empirical study suggested that in recent years piracy has substantially and negatively affected the Chinese music industry's ability to compete with foreign productions. The study showed that as physical format revenue sales decreased and online piracy increased in the early 2000s, the market share for foreign music increased, including songs from Taiwan and Hong Kong, while the share of the market occupied by Mainland producers decreased.³⁸² The study found that from 2000 to 2007, the physical format piracy rate remained constant, around eighty-five to ninety percent,³⁸³ but sales dropped by twenty-five percent, likely due to the onset of unauthorized downloading.³⁸⁴ During this decline, domestic music productions fell from a fifty-five percent market share to thirteen percent as recordings from Hong Kong and Taiwan dominated the market.³⁸⁵ While the reported drop is steeper than this Author would have predicted, a significant drop in domestic market share during that period is conceivable. Although there are no reliable current statistics for domestic versus foreign share of the popular music market in China, indications are that domestic music has rebounded to a majority market share despite continued high piracy rates.³⁸⁶ This rebound for

378. See Melanie Lee, *supra* note 92 and accompanying text.

379. Clarence Tsui, *China Box Office: 10 Highest-Grossing Movies of All Time*, HOLLYWOOD REP. (Feb. 28, 2013, 5:13 PM, PST), <http://www.hollywoodreporter.com/gallery/china-box-office-10-highest-425083#1-avatar-james-cameron-2010-2219-million>.

380. See generally Coonan, *supra* note 84.

381. See *supra* Part III.B.2.

382. Jiarui Liu, *supra* note 9, at 658.

383. *Id.* at 631.

384. *Id.*

385. *Id.* at 635, 651–52.

386. More than two-thirds of the songs on Baidu Music's monthly top 20 downloads charts for June through August 2013 were recorded by Mainland artists. All of the foreign artists on these charts hail from Hong Kong, Taiwan, South Korea, or the United States. See

Mainland artists appears to result in part from a new variable — their greatly increased TV exposure on enormously popular talent shows such as *The Voice of China*.³⁸⁷ In any case, the key point is that there is simply no evidence that piracy helps insulate domestic content producers from foreign content owners who allegedly threaten to dominate the film and music industries in China.

VI. IMPLICATIONS BEYOND CHINA

China is trotted out with increasing frequency as a counterfactual to the standard narrative that copyright is central to the health of creative industries.³⁸⁸ Part V argued that the alleged “benefits” of piracy to creative industries — that piracy increases access to creative works, encourages adoption of innovative new business models, provides free advertising and branding, and protects local industries from foreign dominance — are exaggerated or simply wrong. So what lesson should the rest of the world really draw from China’s experience with piracy?

Many of the arguments in Part V, above, have relevance beyond China, but the most salient lesson is the consequence of diminished revenue stream diversity when pirates, not copyright owners, capitalize on all but a few of the ways in which audiences consume works. As discussed in Part V.A, this harms creative professionals in a number of ways: First, it drastically reduces monetization opportunities for smaller and independent producers. Second, it disconnects copyright owners from consumer choices and therefore distorts market signals concerning the types of works in which to invest. Finally, it disproportionately exposes producers to the idiosyncrasies of peculiar markets and exploitation by intermediaries.

In the United States, creative professionals have already felt the first of these effects as a result of piracy, and particularly as a result of online file sharing.³⁸⁹ For example, independent filmmakers in the United States who do not have access to monetizable “controlled spaces” — that is, theatrical distribution — must rely almost exclusively on various direct-to-consumer copyright-exploitation-based revenue streams, such as online DVD sales and video-on-demand streams, to recoup their production costs. In a recent op-ed, a United States distributor of independent LGBT films asserted that online pi-

Yuebang (月榜) [Monthly Ranking], June 2013–August 2013, Baidu XINGEBANG (百度新歌榜) [Baidu Top New Songs], <http://music.baidu.com/top/new/month/>.

387. See ‘Voice of China’ Returns as King of Ratings, ENGLISH.NEWS.CN (July 17, 2013), http://news.xinhuanet.com/english/china/2013-07/17/c_132548309.htm.

388. See discussion *supra* Part IV.

389. See, e.g., Kathy Wolfe, *Piracy Profiteers: Time To Walk the Plank*, HUFFINGTON POST (Jan. 17, 2012, 8:37 AM), http://www.huffingtonpost.com/kathy-wolfe/piracy-profiteers-time-to_b_1210132.html.

racy “has undermined the careers of many talented aspiring filmmakers.”³⁹⁰ LGBT filmmakers are often forced to self-finance their works because their films are not viewed as “box office winners.”³⁹¹ When unlicensed copies of their films become freely available online, filmmakers lose the ability to monetize their works and “their investment can disappear in an instant.”³⁹² In this environment, fewer filmmakers will invest in producing a second or even first project, and as a result “these stories of diversity will cease to be told and this ‘Freedom of Speech’ will be compromised.”³⁹³

United States creative industries are also experiencing the second effect of diminished revenue streams — market signal distortion. As online piracy has increasingly broken the connection between content provider, licensed distributor, and consumer in the United States, creative industries have increasingly focused their investment decisions on fewer, safer blockbuster bets.³⁹⁴ In her sweeping study on creative industry business and investment strategy, Harvard Business School professor Anita Elberse argues that piracy has played a significant role in major content producers’ decisions to substantially narrow the number and types of creative works they produce:

The threat of piracy, the lower perceptions among consumers of what price is reasonable [for entertainment goods — also partly an effect of online piracy], the unbundling of content packages, and the increased concentration in retailing put tremendous pressures on existing [entertainment industry] revenue models. The bets made by content producers are becoming riskier — only those titles in greatest demand have a shot at earning back their production and marketing costs, with the remaining products more likely to fall by the wayside One way content producers can react to this new reality is by doubling down on blockbuster investments and focusing even less on smaller bets. Such a trend is already underway in several markets.³⁹⁵

Content producers feel compelled to invest in mass-market spectacles that they know in advance have the best chance of being monetized given pressured copyright revenue streams. This creates a self-reinforcing feedback loop: As producers increasingly feel compelled

390. *Id.*

391. *Id.*

392. *Id.*

393. *Id.*

394. See ELBERSE, *supra* note 276, at 236.

395. *Id.* at 236–37.

to forego riskier bets on unconventional or smaller productions, formulaic blockbusters make up an increasingly large share of high-profile content offerings and thus a larger share of the revenue pie. This shift biases monetizable consumption patterns toward blockbusters, which triggers an even greater share of investment in formulaic blockbusters at the expense of experimentation and diversity.

Lastly, trends in the digital content distribution space give global salience to the third effect of diminished revenue streams — the potential for exploitation by monopsonist intermediaries. Influential music and technology blogger Bob Lefsetz is fond of saying that for each type of distribution platform, there is “only one winner on the Internet.”³⁹⁶ Amazon is the king of Internet retail and e-book retail,³⁹⁷ iTunes the king of digital download retail, Google the king of Web search,³⁹⁸ YouTube the king of free online on-demand streaming video and music,³⁹⁹ Netflix the king of subscription streaming video,⁴⁰⁰ Pandora the king of Internet radio,⁴⁰¹ and so on. And some formats will win out over others; for example, in the United States, subscription video streaming by services such as Netflix are already outpacing and outmoding video downloading from services such as iTunes.⁴⁰² China’s experience with monopsony intermediaries that pay miniscule royalties to copyright owners provides a glimpse into our own possibly dystopian future, in which a few legitimate digital distribution platforms become dominant while piracy remains unchecked online.⁴⁰³

396. See, e.g., Bob Lefsetz, *Google Set To Launch Streaming-Music Service as Early as This Week — Report*, LEFSETZ LETTER (May 14, 2013), <http://lefsetz.com/wordpress/index.php/archives/2013/05/14/google-set-to-launch-streaming-music-service-as-early-as-this-week-report/>.

397. See Laura Hazard Owen, *Apple: We Have 20 Percent of the U.S. Ebook Market*, PAIDCONTENT (June 12, 2013, 11:40 AM EDT), <http://paidcontent.org/2013/06/12/apple-we-have-20-percent-of-the-u-s-ebook-market/> (noting that Amazon commands fifty to sixty percent of the United States ebook market).

398. Kevin Bostic, *Apple’s iTunes Rules Digital Music Market with 63% Share*, APPLE INSIDER (Apr. 16, 2013, 12:59 PM PT), <http://appleinsider.com/articles/13/04/16/apples-itunes-rules-digital-music-market-with-63-share>.

399. See NIELSEN, *THE HYPER-FRAGMENTED WORLD OF MUSIC: MARKETING CONSIDERATIONS AND REVENUE MAXIMIZATION* 7 (2011); Ben Sisario, *A Stream of Music, Not Revenue*, N.Y. TIMES, Dec. 13, 2013, at B1, available at <http://www.nytimes.com/2013/12/13/business/media/a-stream-of-music-not-revenue.html>.

400. Netflix reportedly has a ninety percent market share for subscription streaming video. Brian X. Chen, *Apple and Netflix Dominate Online Video*, N.Y. TIMES BLOGS: BITS (June 19, 2013, 4:09 PM), <http://bits.blogs.nytimes.com/2013/06/19/apple-and-netflix-dominate-online-video/>.

401. Cameron Fuller, *Apples iTunes Radio Debuts on the Infinite Dial Survey, People Still Prefer Pandora*, INT’L BUS. TIMES (Mar. 11, 2014, 4:22 PM), <http://www.ibtimes.com/apple-itunes-radio-debuts-infinite-dial-survey-people-still-prefer-pandora-1560833>.

402. *Id.* (“For all the movies watched at home in the first quarter of 2013, 19 percent of consumers watched a movie using a subscription-based service like Netflix, and 5 percent downloaded a movie rental from an on-demand service like iTunes . . .”).

403. See *supra* Part V.A.2.

Portents of such a future are already emerging. Professor Elberse observes that “[b]ecause companies like Amazon, Apple, and Google dominate the sectors in which they operate, they have amassed the power to influence — and sometimes dictate — how and at what price entertainment goods are sold. This, in turn, is putting tremendous pressure on the business models of established [content] producers.”⁴⁰⁴ Developments in the online music streaming space provide an instructive example. While the space is still fragmented, there are already a few identifiable key players: YouTube is the market leader, followed by Pandora and Spotify.⁴⁰⁵ Numerous high profile musicians protest that these services’ royalty payments are unacceptably low and derive from non-transparent royalty calculation processes.⁴⁰⁶ For example, Raymond Pepperrell, guitarist for the acclaimed punk band Dead Kennedys, publicly criticized YouTube for low royalty payments, claiming that a Dead Kennedys video with over fourteen million YouTube views netted the band a mere few hundred dollars in YouTube royalties.⁴⁰⁷ Moreover, he claimed, “I don’t know — and no one I know knows — how YouTube calculates the money.”⁴⁰⁸ Pandora, the leading Internet radio service, pays statutory royalty rates for digitally broadcasting recordings in the United States as a non-

404. ELBERSE, *supra* note 276, at 235.

405. See Glenn Peoples, *How Spotify’s First Year Compares to Pandora, Vevo, YouTube and Others*, BILLBOARD (July 23, 2012, 8:42 PM EDT), <http://www.billboard.com/biz/articles/news/1084519/business-matters-how-spotifys-first-year-compares-to-pandora-vevo-youtube> (reporting that after Spotify’s first year of operations in the United States, YouTube led all music streaming platforms in streams delivered, followed by Pandora and Spotify); Victor Luckerson, *Spotify and YouTube Are Just Killing Digital Music Sales*, TIME (Jan. 3, 2014), <http://business.time.com/2014/01/03/spotify-and-youtube-are-just-killing-digital-music-sales/> (noting that, “[t]he most popular platform for listening to music among young people is YouTube, which is almost entirely free”). *But see* Philip Elmer-DeWitt, *iTunes Radio Overtakes Spotify, Gaining on iHeartRadio in U.S.*, CNNMONEY (Mar. 11, 2014, 6:05 AM ET), <http://tech.fortune.cnn.com/2014/03/11/apple-itunes-radio-pandora-spotify/> (citing study finding that Pandora “dominates” the online music streaming field in the United States market, followed by online radio services iHeartRadio, iTunes Radio, and Spotify, but failing to mention YouTube presumably because it is an on-demand video service and not a dedicated music streaming service).

406. See, e.g., Paul Resnikoff, *16 Artists That Are Now Speaking Out Against Streaming*, DIGITAL MUSIC NEWS (Dec. 2, 2013), <http://www.digitalmusicnews.com/permalink/2013/12/02/artistspiracy>; Charles Arthur, *Thom Yorke Blasts Spotify on Twitter as He Pulls His Music*, GUARDIAN (July 15, 2013, 3:09 EDT), <http://www.theguardian.com/technology/2013/jul/15/thom-yorke-spotify-twitter>; Paul Resnikoff, *Pink Floyd Blasts Pandora for “Tricking Artists Into Signing Their Own Paycuts . . .”*, DIGITAL MUSIC NEWS (June 23, 2013), <http://www.digitalmusicnews.com/permalink/2013/06/23/pinkfloyd>; Laura Sydell, *YouTube Shares Ad Revenue with Musicians, But Does It Add Up?*, RECORD: MUSIC NEWS FROM NPR (Sept. 27, 2012, 12:01 AM), <http://www.npr.org/blogs/therecord/2012/09/27/161837316/youtube-shares-ad-revenue-with-musicians-but-does-it-add-up>.

407. Sydell, *supra* note 406.

408. *Id.* Similarly, the band OK Go, whose music video featuring the band members’ antics on treadmills became a viral sensation garnering upwards of 200 million views on YouTube, claimed that if their YouTube earnings (which they would not reveal) were their only source of income, “it would be time not only to not quit your day job but time to get a night job to supplement it.” *Id.*

interactive music streaming service.⁴⁰⁹ Nevertheless, some musicians have criticized the payouts as intolerably low,⁴¹⁰ especially when Pandora lobbied Congress for even lower rates to remedy what it argues is an “astonishingly high royalty burden.”⁴¹¹ The reasons for the low rates are complex and beyond the scope of this Article. The point is that music streaming royalties in the United States are alarmingly low for delivery platforms that are emerging as the new consumption paradigm for legitimate content.⁴¹² If, or when, the “winning” platform or platforms in this space emerge, become ubiquitous and reach monopsony status, they will have little incentive to maximize royalty payouts and it will be difficult for copyright owners to withhold content and reject their terms.⁴¹³ While no United States service provider, even a monopsony, is ever likely to pay out the absurdly low percentages that the Chinese mobile companies pay, the potential for unfair treatment of and harm to creative industries exists.⁴¹⁴ This result

409. See John Villasenor, *The Strangely Tilted Playing Field of Music Copyright Royalties*, FORBES (May 22, 2012, 6:50 PM), <http://www.forbes.com/sites/johnvillasenor/2012/05/22/the-strangely-tilted-playing-field-of-music-copyright-royalties/>.

410. Musician and copyright activist David Lowery, for example, claims that his band Cracker’s 1994 hit *Low* earned a mere \$42 in performance royalties for 1.15 million plays on Pandora over a three-month period in 2012, which compared unfavorably to payouts from other services such as Sirius XM. David Lowery, *My Song Got Played on Pandora 1 Million Times and All I Got Was \$16.89, Less than What I Make from a Single T-Shirt Sale!*, TRICHORDIST (June 24, 2013), <http://thetrichordist.com/2013/06/24/my-song-got-played-on-pandora-1-million-times-and-all-i-got-was-16-89-less-than-what-i-make-from-a-single-t-shirt-sale/>.

411. Steve Knopper, *Pandora Clashes with Musicians over Song Payments*, ROLLING STONE (Dec. 3, 2012, 4:10 PM, ET), <http://www.rollingstone.com/music/news/pandora-clashes-with-musicians-over-song-payments-20121203>. On-demand music streaming service Spotify, for its part, has recently made efforts to be more transparent about royalty payments. See *Spotify Explained: How Is Spotify Contributing to the Music Business?*, SPOTIFY ARTISTS, <http://www.spotifyartists.com/spotify-explained/> (last visited May 7, 2014). The company claims that it pays out nearly seventy-five percent of total revenues in royalties, which comes out to \$6000–\$8400 per one million streams of an artist’s music and has amounted to over \$1 billion in total royalties paid to labels, artists and publishers since Spotify’s founding in 2008. *Id.* Still, Radiohead front man Thom Yorke recently pulled his solo music from Spotify to protest what he sees as unsustainably low payouts, tweeting, “Make no mistake, new artists you discover on Spotify will not get paid. Meanwhile shareholders will shortly be rolling in it.” See Arthur, *supra* note 406.

412. See Sisario, *supra* note 399 (“The buying habits of music lovers are changing,” Doug Morris, chairman of Sony Music Entertainment, told investors last month at a conference in Los Angeles. “Rather than buying physical records, or even digital downloads, consumers are starting to prefer buying music on demand from streaming services.”).

413. See BLAIR & HARRISON, *supra* note 302, at 43–48.

414. Indeed, some copyright owners and music executives allege that Pandora, already a market leader, could be doing far more to monetize its service and pay more in royalties now, but that its incentives are presently misaligned with the interests of copyright owners. Claire Suddath, *Should Pandora Pay Less in Music Royalties?*, BLOOMBERGBUSINESSWEEK (July 1, 2013), <http://www.businessweek.com/articles/2013-07-01/should-pandora-pay-less-in-music-royalties#p2> (quoting John Simson, co-creator and former executive director of the performing rights organization SoundExchange, as alleging that “Pandora has made a conscious choice not to monetize”); Lowery, *supra* note 410 (commenting “Why doesn’t Pandora . . . get an actual business model instead of asking for a handout from congress [*sic*]”).

seems likely if we reach a point where a very limited number of monetization models co-exist with widespread piracy.

VII. CONCLUSION

Examine China's film and music industries, and the picture that emerges is less sanguine than some scholarly narratives suggest. The alleged benefits of piracy in China are exaggerated or illusory, and do not outweigh piracy's substantial harms. Creators and creative industries persist in China despite extreme levels of piracy, and for some observers this fact might raise doubts about the social value of strong copyright. But the mere fact that some producers have adapted to a high-piracy environment says little about the value of copyright in society, just as the existence of extremophile organisms adapted to severe living conditions tells us little about the optimal conditions for thriving biological diversity.

As Professor Merges argues, for creators to thrive, conditions must be right to afford them the two things they need most to incentivize creativity *and* support their ongoing creative development and efforts: reward and autonomy. This, in effect, means that the optimal environment for cultivating high quality creative production is one that supports a stable, economically robust professional creative ecosystem. In China's high-piracy environment, the film and music industries' monetization models have evolved to rely almost entirely on physical and technological exclusion, respectively. The resulting industries are neither robust nor stable—certainly not to the extent that they could and should be. Instead, because piracy has usurped most revenue streams, both industries are hyper-dependent on a single revenue stream — box office revenue in the movie industry and ringback tone revenue in the music industry.

This lack of revenue stream diversity distorts and undermines the creative ecosystem in at least three ways. First, the scarcity of monetization options creates a winner-take-all market dominated by big producers. The paucity of other revenue sources seriously undermines financial support for smaller, independent producers.

Second, rampant piracy and concentration of revenue streams distorts market signals to producers. For example, film producers are incentivized to invest in a relatively narrow range of works that attract

and artists? For instance: Right now Pandora plays one minute of commercials an hour on their free service. Here's an idea! Play two minutes of commercials and double your revenue!"); Paul Resnikoff, *How Artists Are Subsidizing Pandora's Lack of Profitability*, DIGITAL MUSIC NEWS (June 18, 2013), <http://www.digitalmusicnews.com/permalink/2013/06/18/pandoras-profitability> (discussing a study by economist Jeffrey Eisenbach that concludes that Pandora has sacrificed profitability and revenue growth in order to grow market share and thereby increase the value of the company but not the royalties paid).

the audience whose tastes are most easily monetized — young, urban cinemagoers. Music producers likely are incentivized to produce music that will make the most marketable ringtones.

Third, and perhaps most importantly, reduced revenue stream diversity disproportionately exposes producers to the whims of peculiar markets and exploitation by gatekeeper or monopsonist intermediaries. China's music industry provides an especially vivid example, as ringback tones gross more than \$4 billion annually, but the mobile operators who control ringback tone distribution keep more than ninety-eight percent of that revenue for themselves. The meager two percent that goes to copyright owners amounts to ninety percent of those copyright owners' total income from recorded music. So, if ringtones lose their appeal with consumers, the recording industry will collapse. Without other viable revenue streams to leverage, musicians, producers, and record labels have little choice but to grin and bear it while a state telecommunications monopoly enjoys the great bulk of the rewards of their artistic efforts.

The broader takeaway from the adaptive evolution of China's creative industries is that we can expect to see their counterparts elsewhere evolve similarly if copyright enforcement weakens. In the United States, where widespread online infringement plays a significant role in pressuring revenue streams, we already see evidence of this trend: niche and independent producers face severe challenges monetizing their works and recouping their investments; major producers concentrate investments on a narrowing range of highly monetizable blockbuster content; and market-dominating gatekeeper intermediaries dictate and drive down the prices content producers can charge.

As for the claims of piracy's benefits in China, there is either little evidence to support them or else the evidence points in the opposite direction. There is little to suggest, for example, that piracy leads the music and film industries to adopt innovative business models in which they would not otherwise have engaged. There is also little evidence that piracy is substantially benefitting copyright owners from a branding perspective. As regards the suggestion that foreign copyright owners pose a bigger threat to local industries than piracy, the evidence points in the opposite direction in China — the greater the financial health enjoyed by the local music and film industries, the better they are able to compete with foreign content that is subsidized by foreign sales. Even piracy's most pronounced benefit — enhancing free expression by providing access to banned and uncensored works — comes paradoxically at a significant cost to free expression by weakening the private media sector.

Ultimately, the persistence of China's creative industries confirms what we intuitively know: some creative people will create regardless

of the circumstances. The key question is: Does the ecosystem in which creators are working afford them the conditions in which they, and the nation, can *maximize* their creative abilities and potential? Piracy is not the only constraint on the potential of China's creators — strict state content regulations are also a limiting factor. The success of some creators in China shows that these limitations can be largely overcome. But that success mostly serves as a reminder of how much more China's creative professions and professionals would thrive in an environment more respectful of copyright, and less exploitative of creators and their works.

