The Authors Guild, Inc.

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John R. Read, Esq.
Chief, Litigation III
Antitrust Division, United States Department of Justice
Washington, D.C. 20530

Re: *United States v. Apple, Inc., et al.*, 12-cv-2826 (DLC) (SDNY).

Dear Mr. Read,

I'm writing to express the Authors Guild's firm belief that the proposed settlement of the Justice Department's lawsuit alleging that five publishers and Apple colluded to introduce agency pricing to the e-book market is not in the public interest. The settlement is flawed by an astonishing provision, specifically requiring three large publishers to allow e-book vendors to routinely sell e-books at below cost, so long as the vendors don't lose money over the publisher's entire list of e-books over the course of a year.

The proposal, by allowing targeted predatory pricing of e-books, would give governmental sanction to a practice long considered destructive to a free and fair market. It was precisely this practice – selling frontlist e-books at below cost to discourage and destroy competition – that helped Amazon capture a commanding 90% of the U.S. e-book market. Agency pricing, which the Justice Department believes was introduced through collusion, has allowed Amazon's competitors to gain a foothold, driving Amazon's market share down to 60% in two years.

The Justice Department has made clear that it intends to irreversibly reshape the literary market. Allowing Amazon to resume its predatory ways with e-books will likely accomplish that, but not in the way the Justice Department intends. The proposed settlement will almost certainly backfire and harm readers in the long run.

The Justice Department needs to rethink and revise its proposal: it can stop the alleged collusion without requiring publishers to allow Amazon to resume predatory pricing.

The Competitive Landscape: Amazon's in Control

The Justice Department's assessment of the literary market offers but a pinhole glimpse of the genuine competitive landscape. Its competitive impact statement fails to discuss the relationship between the print book market and the e-book market, for example, or the critical distinctions between the online book market and the brick-and-mortar market. Most importantly, it fails to mention Amazon's monopolistic reach and reflexive anticompetitive habits, the dominant features of the current competitive landscape.

Nowhere does the Justice Department's competitive impact statement discuss the components of Amazon's monopolistic reach:

- that Amazon held 90% of the market for trade e-books prior to the introduction of the agency model in 2010, and that its e-book market share still stands at roughly 60%;

- that Amazon has long controlled about 75% of the online market for trade books in print form;

- that Amazon's dominance of the online market for print books gives it control of the market for an estimated 90% of in-print titles, since only a sliver of in-print books (frontlist books and certain backlist titles) have substantial sales in brick-and-mortar stores;

- that Amazon, through its purchase of Audible.com, has control of the fast-growing downloadable audio book market; and

- that Amazon, through a series of acquisitions, has gained control of the online market for used books.

There simply is no growing segment of the book market that Amazon doesn't dominate.

Even more troubling is the competitive impact statement's failure to discuss how Amazon uses its command of the online book market and its deep pool of capital to undermine competition. The statement doesn't point out:

- that Amazon achieved its $9.99 price for e-books from November 2007 through April 2010 (and through today, for many publishers) by selling frontlist titles *at a loss*, a classic anti-competitive tactic;

- that Amazon managed to undermine its brick-and-mortar competitors while maintaining profitability by selling only a select set of e-books at its below-cost $9.99 price point, *focusing its predation on digital editions of the frontlist hardcover books that attract customers to its brick-and-mortar competitors*;

- that Amazon removed buy buttons from thousands of "long-tail" books in 2008, in a successful effort to force author focused on-demand publishers to use Amazon's costly printing service, a maneuver that continues to reduce royalties for thousands of authors, while preventing rivals from effectively competing with Amazon's author-focused CreateSpace;

- that during Amazon's showdown with Macmillan over e-book terms in 2010, it retaliated by removing buy buttons not just from Macmillan's e-books (which would have been fair play in such a business dispute), but from the publisher's print books as well, tying access to Amazon's vital print book market to acceptance of Amazon's preferred e-book terms (the complaint does blandly mention this, without noting the market-tying strategy);

- that Amazon has continuously used its market leverage, in the U.S. and abroad, to dictate terms to its suppliers by removing buy buttons, in at least one instance punishing a recalcitrant British publisher for more than a year;

- that when Amazon entered the e-lending market for public libraries in 2011, it struck an unprecedented deal with OverDrive, the leading e-lending service provider, requiring it to redirect borrowers from their local public library websites to Amazon's own commercial website and servers, turning thousands of public library websites into virtual storefronts for Amazon, while compromising library patrons' reading privacy;

- that Amazon, in November 2011, brought its predatory campaign to a new level with its Kindle Owners' Lending Library, offering free e-books to gain a loss-leading competitive advantage for its new tablet, the Kindle Fire; and

- that Amazon has aggressively moved in the past seven months to protect its horizontal control of the online book market through a series of vertical acquisitions, buying exclusive rights to thousands of titles, including Ian Fleming's James Bond books, Avalon Publishing, and Marshall Cavendish Children's Books, leading to an unprecedented and dangerous balkanization of the literary marketplace.

Each of these acts represents behavior that should set off alarm bells in the Justice Department's Antitrust Division. Assessing the effects of the proposed settlement without taking these into account is impossible.

Several of these points merit further description, to illustrate the myriad, creative ways in which Amazon leverages its market power to destroy competition.

Amazon, On-Demand Publishing: Making Room for CreateSpace

For years, the Authors Guild staff had heard whispers of Amazon's buy-button removal tactic as a means of getting publishers to agree to new terms. In January 2008, during the Association of Writers and Writing Program's annual conference, Amazon's market-denying maneuver hit hundreds of Guild members, as it removed the buy buttons from more one thousand books in the Guild's Backinprint.com program.

The Guild had launched Backinprint.com in the summer of 1999, allowing authors for the first time to republish their out-of-print books without incurring any set-up costs. (The Guild had negotiated an agreement with on-demand publisher iUniverse to prepare the books for on-demand printing.) The service was an immediate hit with members; within two years, more than 1,000 titles were available to readers again, including books by Mary McCarthy, Thornton Wilder, William F. Buckley, Jr., and Victor Navasky. The books, all of which had fallen out of print after being published by traditional U.S. publishers, are among the more than one million in-print books that make up bookselling's "long-tail," low sales-volume works that rarely appear on bookstore shelves. Long-tail books, more than any other, depend on virtual bookstores: Amazon largely defines their market.

Sales of all on-demand books grew steadily in the early 2000s. By 2005, sales of on-demand books had reached a new high. Backinprint titles sold 41,000 units that year. Amazon, the storefront for most on-demand sales, took notice. It purchased BookSurge, an on-demand printer, to compete with Lightning Source, the industry-leading on-demand printing service run by Ingram.

Three years later, however, few on-demand publishers had moved their printing to BookSurge. Small wonder, since it charged more for its printing services than Lightning Source and had a reputation of offering lower quality service. So Amazon turned to aggressive tactics to win market share, reportedly removing the buy buttons from all iUniverse titles during the 2008 AWP conference. Author Solutions, which had acquired iUniverse, saw its sales plummet. It quickly agreed to use BookSurge for its Amazon sales, and Amazon restored access to its millions of customers.

While a traumatic event for iUniverse, the episode went unnoticed in the book world, which was focused on Amazon's November 2007 introduction of the Kindle, with its predatory pricing scheme for select frontlist books. Even our members with books in the program took no notice, because when Amazon removes a buy button from a book's sales page, the sales page looks almost identical to a page for an out-of-print or out-of-stock book. Reports of Amazon's strong-arming of on-demand publishers didn't surface for more than a month, in March 2008, with reports in the Wall Street Journal and elsewhere.

Amazon got away with this gambit, suffering barely a scrape. On-demand publisher Booklocker did file a class action lawsuit in Maine against Amazon over the episode. After Amazon's motion to dismiss failed, Amazon quietly settled the suit for a reported $300,000 in attorneys' fees. Amazon has doubtless earned back those fees many times over. Thousands of authors continue to see their on-demand royalties reduced by ten to fifteen percent as a result of Amazon's squeeze. (This wasn't a maneuver justified by efficiencies that ultimately benefit consumers, incidentally. Amazon appears to sell the books at precisely the same price as other online retailers. Amazon just makes more money at it than they do.)

More importantly and profitably to Amazon, by forcing iUniverse and other author centered on-demand service providers to use BookSurge, Amazon severely constrained effective competition for its own author centered on-demand service provider, which became known as CreateSpace in 2009. Amazon's vertical integration of on-demand printing eliminated the ability of iUniverse, PublishAmerica, XLibris and others to offer authors better royalties when selling through Amazon. CreateSpace appears to have thrived ever since.

Amazon's Exercise of Its Buy Button "Nuclear Option"

In June 2008, Doreen Carvajal of the New York Times called buy-button removal "the literary equivalent of a nuclear option for rebellious publishers who balk at [Amazon's] demands." Ms. Carvajal was discussing Amazon's removal of buy buttons in the United Kingdom from hundreds of Bloomsbury titles while in negotiations with the publisher.

The Authors Guild began preparing for the next incident, which everyone in the industry knew would come. Since stealth appeared to be a significant weapon for Amazon (authors may not notice, if the incident is over quickly enough, and publishers are fearful of blowing the whistle), the Guild hired developers to build a tool to e-mail authors when Amazon removed one of their buy buttons. When Amazon removed the buy buttons from Macmillan's print and digital books in January 2010, the Guild launched the tool through a dedicated website, WhoMovedMyBuyButton.com.

Amazon's buy button removal campaign persists unabated. Independent Publishers Group markets and distributes titles from independent publishing houses to the book trade at large. When IPG's Amazon contract came up for renewal in 2012, Amazon pressured IPG for more favorable terms. When IPG resisted, Amazon took down all IPG e-books from its site. After X months, IPG came to terms, etc.

Amazon and E-Lending by Public Libraries

In September 2011, Amazon entered an arrangement with OverDrive, the largest supplier of e-books and audio books to public libraries, making possible e-book library lending through the Kindle device. OverDrive's implementation of the Kindle lending program, pursuant to its agreement with Amazon, required it to redirect patrons to Amazon's servers. A columnist for the *Los Angeles Times* compared it to "walking into your public library then finding yourself at the Target checkout counter." No other e-book vendor has such an arrangement.

**Amazon Pursues Its Own "Monopoly Over Its Titles:"
the Balkanization of the Literary Marketplace**

Since its e-terms battle with Macmillan in January 2010, during which Amazon protested that it had to "capitulate" due to Macmillan's "monopoly over its titles," Amazon has turned toward pursuing its own monopoly. With the launch of the Kindle Fire, Amazon's drive to acquire exclusive rights to books, by acquiring publishers with substantial backlists and other arrangements, has taken on a new urgency.

In September 2011, Amazon's acquired the exclusive digital rights to one hundred popular DC Comics graphic novels. If a customer wanted to read any of these on an e-device, it had to be on a Kindle Fire. Barnes & Noble, trying to break into the e-device market with its Nook, retaliated by pulling all print copies of DC Comics titles from its shelves. Books-a-Million, the third largest bookseller, followed suit. "As Amazon seeks over the next few years to expand its tablet line," predicted the *New York Times*, "these collisions over content are likely to become routine."

Amazon is moving quickly. In December, Amazon entered the children's book market, acquiring more than 450 titles of Marshall Cavendish Children's Books. In April, Amazon announced it had acquired the exclusive North American rights to publish Ian Fleming's James Bond novels -- in both digital and print formats. Earlier this month, Amazon expanded its holdings of genre fiction, purchasing the publisher Avalon Books and the exclusive rights to its 3,000-title backlist of romance, mystery and Western fiction.

Balkanization of the literary market is something new and deeply troubling. "Bookstores used to pride themselves on never removing any book from their shelves," reported the *Times*, "but that tradition—born in battles over censorship—is fading as competitive struggles increase." Awful as it is for our literary culture, the balkanization of the book market is but a logical extension of Amazon's no-prisoners approach to competition.

The Kindle Owners' Lending Library

Amazon lagged Barnes & Noble by a full year in developing an e-reading tablet. While Barnes & Noble prepared to roll out its second-generation tablet, Amazon prepared to introduce its first, the Kindle Fire. To gain an advantage, Amazon proposed to do something Barnes & Noble couldn't afford to do: give away e-books, including front list e-books, for free.

So in November 2011, shortly before Amazon began shipping its Kindle Fire, Amazon also introduced its Kindle Owners' Lending Library, which allowed Amazon Prime members to download onto their Kindles any of more than 5,000 titles, at the time of it was announced. Customers are limited to one book per month and one book at a time -- when a new book is downloaded, the old one disappears from the Kindle.

Amazon approached the six largest U.S. trade book publishers to seek their participation in the program. By all accounts, each refused. Publishers weren't eager to allow Amazon to undermine the economics of the e-book market, representing the lone bright spot for the industry. So books from the six largest trade publishers were not in the Lending Library program.

Amazon's attempts to enlist the next tier of U.S. trade book publishers, major publishers that are slightly smaller than the Big Six, fared no better. Many, perhaps all, also refused. No matter. Amazon simply disregarded these publishers' wishes, and enrolled many of their titles in the program anyway. Some of these publishers learned of Amazon's unilateral decision as the first news stories about the program appeared.

The use of publishers' books without permission was due to a tortured reading of its boilerplate contracts with publishers. Amazon decided that it didn't need the publishers' permission, because, as Amazon saw it, its contracts with these publishers merely required it to pay publishers the wholesale price of the books that Amazon Prime customers download. By reasoning this way, Amazon claimed it could sell e-books at any price, even giving them away, so long as publishers are paid.

From our understanding of Amazon's standard contractual terms, this is nonsense -- publishers did not surrender this level of control to the retailer. Amazon's boilerplate terms specifically contemplate the *sale* of e-books—not giveaways, subscriptions, or lending. Amazon can make other uses of e-books only with the publishers consent. In other words, Amazon was boldly breaching its contracts with these publishers. This was an exercise of brute economic power: Amazon knew it could largely dictate terms to non-agency publishers, and it badly wanted to launch the Lending Library program with some notable titles.

So Amazon did just that, conscripting publishers into a predatory pricing business model that substituted cash for genuine innovation, further undermining the economics of brick-and-mortar bookstores along the way.

The Justice Department, through this settlement, would deliver the lists of three large publishers into Amazon's predatory scheme. Unless competitors are willing to forego nearly all profits from these publishers, the Kindle will likely have an unmatchable competitive advantage.

Conclusion

Of all the possible remedies to the collusion the Justice Department alleges, requiring three large publishers to allow Amazon to sell e-books at a loss is among the most destructive of competition that one could imagine.

Amazon's tactic of selective predatory pricing of frontlist e-books was far more anti-competitive than the Justice Department has acknowledged. It effectively cut brick-and-mortar retailers – logical participants in a bricks-and-clicks, showroom approach to marketing e-books – out of the game. The retailers would need a partner willing to invest substantial amounts to develop and market an e-reader, e-commerce site, and accompanying software. What partner would dare invest, with Amazon plainly willing to earn little or nothing from e-books? (Google's commitment to independent bookstores always seemed half-hearted, and now it's backing out.) From Amazon's perspective, the best competitor is one that never dares enter the field.

Amazon has engaged in baldly anticompetitive practices for years. Its approach to destroying competition is sophisticated, data-driven, and endlessly creative. What other company would have thought to arm smart-phone users with a price-checking app then reward them for turning on their phones' geo-location function and report pricing data to Amazon in the height of the holiday season? (Up to five dollars from Amazon, every time you deny your local retailer a sale. One Saturday only; limit three per Amazon customer.) It's utterly brilliant, and a game only the richest of corporations can play.

Amazon really doesn't need the Justice Department's help. For the sake of free and fair competition, for the sake of readers who would like many companies to invest in better e-reading devices, software, and even in bookstores that one can visit on a weekend, please find another way to address the collusion you believe you've uncovered.

Respectfully,

Paul Aiken
Executive Director

cc: Scott Turow

Attached: Selected References

Authors Guild Tunney Act Letter
Selected References
June 25, 2012

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