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LITIGATION III, ANTITRUST DIV.
U.S. DEPT OF JUSTICE

May 22, 2012

John R. Read
Chief, Litigation III Section
United States Department of Justice
450 5th St NW
Suite 4000
Washington DC 20530

Dear Mr. Read,

As a literary agent for over thirty years, and chair of Writers House LLC, an agency that represents many bestselling authors, I'm baffled by the suit the Justice Department recently filed against Apple and five leading publishers, and by the settlement it's reached with three of them. Though I don't have the expertise to evaluate the case from the point of view of a lawyer, I do know the business, and after reading both the brief and the settlement, I'm outraged that the DoJ, based on a cursory knowledge of book publishing, has decided that the publisher defendants have conspired in a manner harmful to the public.

Whether the publishers conspired is open to question. Whether they stifled competition and caused the public harm is not. Since the advent of the agency model, which gave the publisher defendants control of ebook pricing, the book market has grown considerably: Consumers now have access to more, better and less expensive electronic reading devices, as well as a greater selection of lower-priced ebooks. If the terms of the settlement are not overturned, Amazon will likely return to discounting ebooks well below the price matching ability of any competitor. The DoJ ruling will thus protect one competitor at the expense of others: it has the potential to put many retailers out of business (especially small businesses without access to the kind of capital needed to match loss leading pricing), harm publishers working within unavoidably low profit margins, and harm consumers, who will ultimately have fewer good quality books from which to choose.

To understand why publishers are so concerned about the effect of aggressive ebook discounting, it's important to understand the connection between the print and digital markets, as well as the cost of producing both digital and physical books. Contrary to what Amazon and some journalists have led the public to believe, ebooks are not, as the Justice Department asserts, considerably cheaper to produce than print books. Digitizing a book costs less than printing it,

yes; distributing an ebook also costs less than shipping a physical book. Binding and warehousing create additional costs for print books. But these costs are minimal compared to the unseen costs of curation, editing, marketing, promotion, publicity and last, but certainly not least, the cost of acquiring a manuscript, which can range from thousands to millions of dollars. These invisible costs are substantial and must be factored into the pricing of both digital and physical books. When all the costs of producing a book are considered, not just the more tangible costs of physical production and distribution, ebooks are not significantly less expensive to produce than print books. Another way of expressing this is that at current agency pricing levels, e-books do not provide greater marginal revenue to the publisher than the comparable print editions, despite the absence of costs related to physical production and distribution.

Introducing a new lower-priced format, which appears to cost less than it actually does, into a market with already low profit margins, presents a considerable challenge, especially if the lower-priced format threatens to cannibalize sales of the higher-priced editions. If ebook prices were to barely cover what it costs to publish them, and if they continue to replace rather than supplement the sale of higher-priced physical editions, publishers might not be able to sustain the invisible though critical costs of production and publication. Preserving the market for hardcover and other print editions is thus of critical importance to publishers. Besides yielding a higher profit, print editions contribute to the marketing of ebooks: most successful ebooks are either digitized versions of print books or are released simultaneous with hardcover and other print editions. It's further likely that without physical stores devoted to the display and sale of physical books, Amazon and other solely online retailers would have a harder time selling ebooks. To wit, Amazon's recent ad campaign, which encouraged consumers to browse in physical stores. Such advertising methods suggest that Amazon and other online retailers might not be able to sell as many copies without physical shops, whose displays and employee expertise help consumers determine which books they want to read.

The complications created by the low price of ebooks beg the question: Why did publishers initially accept Amazon's pricing policies? Why didn't they object to Amazon's promise to its customers that they would be able to buy e-book bestsellers at the low price of \$9.99? Since Amazon paid publishers the full wholesale price regardless of discount, and since the introduction of the Kindle into the marketplace promised to increase sales of ebooks and perhaps the size of the entire marketplace for books, the publishers did not object. What could be wrong with low prices that motivated consumers to buy more ebooks, especially if publisher and author earnings were not affected? As the market matured, however, and it became clear that ebook sales were not incremental, publishers were forced to ask themselves some harder questions: What would happen if content was devalued as a consequence of aggressive discounts? And what would happen if Amazon then decided not to subsidize the losses incurred by such low prices? In confronting these questions, publishers began to believe that a new model for selling ebooks was essential. Apple's offer to use agency was therefore enormously

appealing. It was a model already used by Apple to sell other products, and not one, as the DoJ implies, designed to stifle competitive pricing in the e-book market. In the short term, it offered publishers considerably less profit. In the long run, it promised to preserve the viability of the marketplace.

By neglecting to investigate the nuances of the publishing business, the DoJ has failed to look beyond the fallacious assumption that ebooks are much less expensive to produce than print books, and they have failed to understand the complexities involved in ebook pricing. Ignoring publishers' real and valid concerns about the viability of the marketplace, they came to the facile conclusion that the publishers' primary reason for replacing the wholesale model, which generated more profit for them than the agency model, was solely their fear of Amazon's hegemony in the ebook market. Publishers, according to the DoJ, "feared that their competitive advantages, which they held as a result of years of investment in print books, would erode and eventually become irrelevant as e book sales continued to grow." Amazon's entry into the book business provided the Justice Department with a convenient rationale to explain why publishers seemed to be acting against their self-interest: the DoJ asserts that publishers feared Amazon "would ultimately supplant publishers as intermediaries between authors and consumers."

Though not germane to this suit, the DoJ, perhaps to lend credibility to its point of view regarding what motivated publishers, asserts that Amazon paid a higher royalty rate to authors than the publisher defendants offered. Yes, Amazon was offering a substantially higher share of revenue to self-publishing authors, 70% (so long as the price was between \$2.99 and \$9.99, otherwise the revenue percentage offered to the author dropped to 35%) vs. 25% of net as a royalty, but of course self-publishing authors weren't being published by a third party and specifically were receiving no guaranteed advance, as they do when published by traditional publishers. It is thus illogical to suggest that Amazon was offering authors a better deal than the five publisher defendants and irresponsible to conclude that the publishers conspired to undermine the agency model simply because their role as gatekeepers had been threatened. Publishers are well aware that most professional authors, those that take a year to write a commercial novel as well as those that take ten years to write a biography, rely on advances both to finance their careers and mitigate risk, as large corporations with access to significant capital that own large portfolios of intellectual property are far better positioned than individual authors to absorb the risk associated with individual book publication. While it's true that publishers may have been irked by a customer providing market access to a new kind of competitor, they were far more concerned about the effect of Amazon's practice of loss leading bestselling titles than they were about the revenue splits Amazon was offering self-published authors.

Antitrust law recognizes the dynamic nature of markets influenced by frequent and momentous technological change. In evaluating a potential breach of the law, past, present and future

markets must all be taken into consideration. It's true that the market for ebooks has grown considerably since Amazon introduced the Kindle. It's true that consumers may have had to pay a few extra dollars for a few bestselling ebook titles, and that for a brief period of time consumers may not have enjoyed the benefits of the competition the agency model has since engendered. But it is also true that the ebook market continued to grow, and explosively at that, after the agency model was adopted by the publisher defendants. The adoption of agency has led to a more competitive marketplace, which has benefited consumers in numerous ways. Interfering now in a functioning market will do nothing to protect consumers and will risk disturbing an intricate ecosystem that depends on many factors, not simply the preservation of one competitor's ability to provide deep discounts on ebooks. Without the competition that the agency model has engendered for new retailers and ereading devices, publishers have reason to fear that physical bookstores will not survive and that the price of bestselling books will be reduced to a point at which the quality and quantity of books offered will no longer be sustainable. I do not see how this is in the best interests of the public, and I respectfully implore you to reject the proposed settlement or to consider alternatives that are not as potentially harmful to the pro-competitive environment currently in place.

Yours,

A handwritten signature in cursive script that reads "Amy Berkower". The signature is fluid and elegant, with a prominent initial "A".

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