The Book Subscription Model— A Legal View: An Interview with Attorney David Koehser

Change has been the byword in the world of higher education publishing, also known as college publishing. Cengage will be rolling out in August 2018 its new Cengage Unlimited “All in One Subscription” program, whereby students pay a flat fee of $119.00 per semester for unlimited access to Cengage’s digital database of textbooks. https://www.cengage.com/unlimited

However, authors have said, “Not so fast.” In a class action lawsuit filed in the Southern District of New York, textbook authors David Knox and Caroline Schacht have filed a complaint against Cengage Unlimited. https://bit.ly/2sa20L1

According to *Publisher’s Weekly* (May 15, 2018),

Filed this week in the Southern District of New York by authors David Knox and Caroline Schacht, the suit claims that in introducing its subscription service, Cengage “is systematically dismantling and frustrating the business of selling Plaintiffs’ work" in favor of selling subscriptions to Cengage’s digital products. The authors, the suit states, "expect their royalties to decline substantially" as a result of Cengage Unlimited.

"The fundamental bargain struck between Plaintiffs and their publishers was for the payment of royalties upon the *sale* of their works," the filing states.

To get a legal perspective, I asked David Koehser, my legal advisor, for his initial reaction to the Cengage litigation:

One of the key questions that remains unanswered with respect to subscription models is whether the author’s income will be reduced relative to that of the publisher. For example, under the traditional model, if a publisher sells a copy of a work for $10.00 and the author gets a 10% royalty, that comes out to $1.00 for the author. If the publisher instead leases a copy through a subscription service and gets $1.00 and the author gets a 10% royalty, the result is the same percentage-wise. The author gets 10% of whatever the publisher received, and both parties are in the same relative position. The income to each is much smaller, but each party maintains the same position relative to the other with regard to that party’s share of the total amount received. In other words, both sides suffer, but they suffer equally.

The authors in the Cengage litigation appear to be arguing that Cengage’s switch to a subscription model has altered the relative positions of the parties in favor of the publisher. However, the authors are also arguing that Cengage has refused to provide any information on sales data and royalty calculations, thus making it impossible to determine whether the authors’ position relative to the publisher has been made better or worse. It is possible that the adoption of the subscription model has reduced the income available to both parties, but, depending on the system used to allocate that income, some authors may be in a better position relative to the publisher than was the case with a sales model, while others may be in a worse position (see the discussion below on the alternatives for allocation of subscription revenue among the titles included in a subscription service).

I also asked Dave a few more questions.

JM-What is the definition of the subscription model?

DK- The subscription model is similar to Netflix and other movie subscription services. With Netflix, subscribers get access to all the films and television programs offered by Netflix, and can view those films and programs whenever they wish. The roster of available films and programs changes frequently, as some films and television programs are removed and others are added. However, Netflix and other similar services are increasingly producing their own content, which will presumably remain available through the service indefinitely.

A basic subscription allows for use by one user on a single device, but it is possible to get expanded subscriptions which allow multiple users to access the service at the same time, using different devices.

One question that remains unanswered with respect to book subscription services is how subscription fees will be allocated among the titles included in the service. For example, assume that a user pays a subscription fee of $100.00 to get access for six months to a subscription service that offers 100 titles. Options for allocating the subscription fee among the 100 titles include the following:

- Per title allocation, with $1.00 of the fee allocated to each title, regardless of use.
- Allocation by size of each title, with an amount greater than $1.00 allocated to longer titles and an amount less than $1.00 allocated to shorter titles.
- Allocation by print or ebook retail list price, with higher list price titles commanding a greater share of the subscription fee and lower list price titles receiving a lesser share.
- Per hit allocation, with the fee allocated only among titles that the user views during the subscription period. For example, if the user looks at one title five times during the subscription period and looks at five other titles only one time each during the six-month subscription period, the fee would be allocated at $50.00 to the title viewed five times and $10.00 to each of the one hit titles.
- Per time allocation, with the fee allocated based on the amount of time the user spends viewing each title.
- A hybrid formula combining one of the above with the allocation of a base amount to each title included in the service, regardless of whether that title is or is not accessed by the user during the subscription period.

The allocation question becomes more complicated if titles are added to or removed from the service during a subscription period, and if subscribers can sign up at different times for different subscription terms.

The allocation question may be less complicated if subscriptions are tied to a limited number of works. For example, if a subscriber can buy a limited term subscription with access to the five titles required for a course, it may be easiest to allocate the subscription fee equally among the five titles.

JM- *What types of publishers use the subscription model?*

DK-The subscription model would seem to be best-suited to the educational textbook market, where there would be a fixed number of titles for a course and a fixed term for a subscription. Each student enrolled in the course would purchase a subscription and would get access to the books assigned for that course, for the term of the course. The subscription fees could be allocated on a per title basis or by the length or list price of each title. Since all the titles would be required for the course, any one of these methods of allocation would essentially mirror what would happen if print copies were purchased by each student for the course.

The subscription could also work in other contexts, but there may be some question as to whether it would be wise for a publisher to implement the model in these contexts. For example, a publisher could set up a subscription service that includes all the adult novels published by that publisher, but this may result in a substantial loss of revenue over what could be earned if the publisher only sells print and ebook copies of its novels.

JM-What are the advantages to the publisher? Disadvantages?

DK-As between printing and shipping print books versus making books available by a digital subscription service, the subscription service obviously offers a cost advantage. However, the same may not be true when comparing ebooks offered for sale versus ebooks offered through a subscription service. A publisher could most likely charge more for the purchase of an ebook than it would be able to charge for a subscription that includes the right to rent a book for a defined term.

As noted above, subscription services may result in a drop in publishers' income. However, they may become a marketing necessity. If a few publishers adopt a subscription service, it is likely that consumers will come to favor those publishers, and other publishers will need to adopt the same subscription model in order to remain viable in the marketplace. Just as the market for music and films in the form of CDs and DVDs (or, in the case of movies, theater tickets) is dwindling, publishers may find that consumers will be less willing to buy books in print or ebook form if they can get access to and "rent" hundreds or thousands of books for a single subscription fee, or if, in the case of college courses, they can "rent" the titles they need for the duration of the course without having to buy and later, attempt to re-sell, print copies.

JM-What are the advantages to the author? Disadvantages?

DK-The rise of subscription services may mean lower prices for access to books. If this happens, it will not work to the advantage of publishers or authors, unless the drop in revenue per book is offset by a substantial increase in the number of purchasers. Unlike the music industry, most authors do not have the ability to sell hundreds or thousands of tickets for club or arena performances. If the pool of revenue shrinks there will most likely not be other avenues to make up for that lost revenue, and in that case questions as to the allocation of that shrinking pool between publishers and authors will become more important. Even with a more "author-friendly" method of allocation, receiving a larger share of a smaller pie is not likely to sit well with authors. A larger question is what this may mean for the culture as a whole, as at some point it may become unprofitable for some publishers and authors to remain in business.

JM-Many college textbook authors signed contacts before technology made possible the digitization of content. For example, as an acquisitions editor I signed a number of authors with a company in the 1980s who are now part of Cengage because of subsequent mergers and acquisitions. How do the contracts these authors signed during the pre-digital age play out in this litigation?

DK-This harkens back to the early days of ebooks. When ebooks first came on the scene, there were many old contracts that granted the publisher the right to "print, publish and distribute" the work and which calculated royalties in terms of the number of print units sold. The general consensus came to be that, since these older contracts were signed at a time when no one knew about ebooks and since the contracts did not include any mention of ebooks or any mechanism for calculating royalties from sales of anything other than print copies, ebook rights were not included. As a result, most publishers went back to their authors to get amendments to add ebook rights to these contracts, and they started expressly including ebook provisions in their new contracts.

The same arguments are likely to apply here. Even though the Copyright Act defines "publication" as being "the distribution of copies of a work by sale or other transfer of ownership, *or by rental, lease, or lending*," authors are likely to argue that an agreement that only grants the right to "print, publish, distribute and sell" does not include the right to rent a work via a subscription service. Furthermore, many older agreements do not have any provision for determining the royalty for the inclusion of a work in a subscription service, thus supporting the argument that the right to rent the work through a subscription service was not contemplated and is not included in the rights granted under the agreement.

Many publishers are already addressing this issue in their house agreements by acquiring the right to "make available" the work by any means now known or hereafter developed and by providing a mechanism for calculating a royalty if the work is "made available" through a subscription service. Others are including language stating that the publisher can make the work available through a subscription service if the author agrees.

JM-Textbooks in some disciplines, such as accounting, engineering, taxation, computer science, and health science, to name a few need frequent revisions to be competitive. How do you envision the subscription model working in this scenario when authors who signed pre-digital contracts revise their books?

DK-The subscription model allows for more flexibility in terms of revisions. Since a book will reside on a publisher's server rather than with a buyer, the publisher will be able to make frequent and instant changes to the book. The standard revisions paragraph in most publishing agreements will still apply – that is, the author will be contacted if a revision is desired, and if the author refuses or fails to participate in the revision the publisher will be able to revise the work and either charge the cost against the royalty earned by the author from the revision or reduce the author's royalty by some pre-determined percentage.

Authors may be concerned with how frequently the publisher can request a revision. As noted above, with a subscription service a publisher could theoretically revise a book on a rolling basis, and thus have the author working almost constantly on revisions. Accordingly, authors who are negotiating contracts for new books may want to be more conscious about placing limits on the frequency with which the book can be revised. (This was already a recommended practice for authors for print books, but it becomes even more relevant for books distributed through a subscription service.)

JM-Which party do you think will prevail in this litigation?

DK-I have not seen the response from Cengage or the contents of the original contracts with the authors, and in any case I am generally reluctant to speculate on how any particular case might be decided. It is possible that the parties will reach a settlement, and if that happens the terms will probably be confidential and thus we will not get much in the way of guidance as to how these issues might be handled by Cengage or other publishers in the future. The bigger issue is what the subscription model means for the industry going forward, and whether the model can be made to work for both publishers and authors or whether it will result in reduced income for both.

JM-I want to end my interview with Dave with my own observations. I started my career as a college sales representative for Richard D. Irwin and then for many years I was an acquisitions editor with companies such as Houghton Mifflin, Charles Merrill, and Wadsworth. From that experience, I learned one thing: without authors there is no product and nothing to sell. Authors and their good will are the most valuable asset of an educational publisher. One wonders if the unilateral switch to the subscription sales model and potentially lower royalty payout to authors will damage long-standing publisher/author relationships.

Thanks to ***McHugh Advisor Harvey Kane*** for his review of this interview.

Disclaimer

About David Koehser, Attorney-at-Law

David Koehser is a Minneapolis-based lawyer who practices in the areas of copyright and trademark law. Dave's website contains articles on the topics of: Publishing Law, Merchandise Licensing, Copyrights and Trademarks, and Theater and Performing Arts. Request a copy of Dave's informative quarterly e newsletter*, Publishing and Merchandise Licensing Law Update*. Dave has a B.A. from the University of Iowa and a J.D. *cum laude* from the University of Minnesota Law School. You can find his website at www.dklex.com.

Contact Information: dklaw@cognisinc.com; 612-910-6468

About John B. McHugh

John B. "Jack" McHugh is a 40-year veteran of the publishing business. Jack has worked as an executive for Houghton Mifflin, Wadsworth, and Saint Mary's Press. Jack is also an experienced association publishing executive. For seven years, he was Publisher and Director of Programs at the American Society for Quality and for a two-year period, he served as the Interim Publisher at the Project Management Institute. He is a member of the ASAE Advisory Board for Publishing, Communications, and Media Issues and Practices.

Jack's specialties include association/nonprofit publishing, book publishing, executive recruiting, journal publishing, rights and permissions, new ventures, organizational design, and social media strategy and policy. Mc Hugh is also the manager of the LinkedIn™ group, ***Association*** and ***Nonprofit Publishing***.

Contact Jack McHugh, 414-351-3056

Email jack@johnbmchugh.com,

Website http://www.johnbmchugh.com.

LinkedIn https://bit.ly/2JL0r06

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