

**Reviving the Economic Viability of Newspapers and Other  
Originators of Daily News Content**

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# Reviving the economic viability of newspapers and other originators of daily news content

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# **Reviving the economic viability of newspapers and other originators of daily news content**

## **Crux of our analysis and what we propose**

- In a variety of ways, the federal copyright act allows online competitors of newspapers to commercially exploit newspapers' copyrighted and uncopyrighted news reports without paying the newspapers and without their consent. The copyright law has the same effect on all originators of news reports.
- Called "aggregators," those online competitors offer truncated rewrites of the newspapers' reports to the public via the internet at about the same time that the newspapers circulate them. The aggregators do the same thing with news reports published by other originators of news.
- Aggregators' timely versions of news reports are close substitutes for those that newspaper publishers and others originate. That enables aggregators to attract much the same demographic readership and advertisers that the newspapers' online and print reports attract.
- Although few single aggregators of news rewrites can match the readership of a website operated by the publisher of a large daily newspaper, the combined readership of all such aggregators can have a meaningful impact on the market for advertising associated with news.

- Because the online competitors legally free-ride on the newspapers' substantial news-gathering expenses, they dramatically undercut newspapers in the market for advertising dollars. They can charge advertising rates that the newspaper cannot profitably match because of the newspaper's exponentially higher costs to gather news and craft news reports.
- The newspaper publisher cannot amass enough extra reader traffic to surmount the difference in advertising rates between what the publisher must charge to recover the publisher's substantial journalistic expenditures and what the aggregators can charge by free-riding on those expenditures.
- Even though they rely on newspapers for virtually all of their commercially exploitable news content, competition among aggregators will drive advertising rates below the newspapers' journalistic costs, and can drive newspapers and any other originator of news reports out of business.
- The copyright law will prevent any firm from staying in business that undertakes the substantial journalistic investment required to originate news coverage comparable to the depth and scope of newspapers' coverage.
- In 1918, the United States Supreme Court affirmed an injunction barring a for-profit news wire service from competing with the Associated Press in much the same way. The International News Service allegedly rewrote uncopyrighted AP news dispatches arriving in New York, and sold them via telegraph and telephone to newspapers in the western states. That enabled the INS dispatches to arrive out west at about the same time that AP's

original dispatches got there. Describing INS as misappropriating AP's "quasi-property," the Court decided that INS was unfairly competing with AP by free-riding on AP's substantial journalistic costs. The injunction was not permanent. It lasted only long enough for AP to exploit the highly-perishable commercial value of its own news reports before INS could exploit their substance. That case is *International News Service v. Associated Press*, 248 U.S. 215 (1918).

- When Congress revised the copyright act in 1976, it added a provision -- § 301 -- that abolishes all state laws that function as copyright does. A draft of the statutory revision had preserved the *INS* theory so that it was not subject to the copyright act's pre-emption of state laws. But the Justice Department objected, exaggerating the effect of the *INS* decision by arguing that it gave news organizations a "boundless monopoly" in factual information of public interest that the copyright act placed in the public domain. The House then struck the exception.
- We recommend amending § 301 of the copyright act to make clear that, in the context of unfair competition among direct competitors, the unjust enrichment theory underlying the *INS* decision remains viable as a matter of state law. The copyright act, then, would not preempt state common law or state statutes that afford rights under that theory. Although we endorse unjust enrichment as an unfair competition theory in this context, we do not endorse the "quasi-property" mode of legal analysis.
- We do not recommend a definitive statutory amendment. The fast-changing embryonic environment of delivering news commercially via the

internet demands the flexibility of the judiciary's common law reasoning in adversarial contexts. A statute that tries, by itself, to remedy destructive free-riding on others' news-gathering is bound to replace today's problems with new ones, reflecting compromises that impede what the common law could provide more effectively.

- If used strategically by newspaper publishers and others who originate news reports, our recommended change to the copyright law would pressure aggregators to contract with originators of news reports to avoid the legal consequences of unjust enrichments suits. Doing so would assist markedly that those who spend substantial sums to originate news coverage to stay in business.

***Prelude: 67 years ago, Professor Callman predicted the destructive effect of free-riding on news-gathering.***

At least 50 years before newspapers encountered the internet, one of the nation's top experts in the law of unfair competition presciently warned about the economic dangers of allowing one competitor in the news business to free-ride on another's news-gathering.

In an article published by Harvard Law Review in 1942, Professor Rudolf Callmann agreed with the majority's reasoning in the *International News Service v. Associated Press*, effectively predicting what the newspapers are experiencing today from parasitic free-riders on the internet. Analyzing the effect of the International News Service allegedly competing with the Associated Press by

selling rewritten AP stories, Professor Callmann said:

Had there been nothing to prevent the International News Service from continuing the action complained of, the Associated Press might eventually have been driven out of business by the competition of a rival whose expenses were so much less . . . .

No company could maintain large news-gathering services if it were subject to such competition . . . .

[T]he public will not be benefited by allowing one competitor to profit from the fruits of another's labor and expense. This may be true in other situations as well, but it is particularly so when one competitor enriches himself at the expense of the other.<sup>1</sup>

**The parable of the Little Red Hen explains why today's laws will drive newspapers and other originators of news out of business**

Recall the tale of the Little Red Hen. She asks the other barnyard animals, "Who will help me cut the wheat?" Each of them says, "I won't." After cutting the wheat, she asks, "Who will help me grind the wheat?" Each says, "I won't."

After grinding the wheat into flour, the Little Red Hen asks, "Who will help me bake the bread?" Each of the barnyard animals repeats, "I won't."

Then, after the bread is baked and she removes the warm, aromatic loaves from the oven, she asks, "Who will help me eat the bread?" And each of the barnyard animals says, "I will."

Not only do our laws compel the Little Red Hen to share her bread with the other barnyard animals, they go further. The Little Red Hen decides to sell her bread from a roadside stand. Our laws compel her to allow each of the other barnyard animals to take some of her loaves, open up their own competing roadside stands, and drive her out of business by undercutting her price. Because her labor costs are so much higher than theirs, she can't match their prices without suffering a huge loss. So she goes out of business.

Now the barnyard animals have no bread to sell. So the cow decides to do the same thing that the Little Red Hen did. But the cow encounters the same free-riding that the Little Red Hen encountered, and suffers the same result. The cow goes out of business too.

In the end, the laws effectively will drive out of business every animal who tries to replicate what the Little Red Hen did or who tries to improve upon it. No matter how tasty or unique the bread is, the other barnyard animals can sit back until it's perfected, then take some of the perfected loaves and sell them at low prices, which drives the bread-baker out of business.

That is how our laws work today for the news business, just as Professor Callmann predicted 67 years ago. That is not free-market economics where you

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<sup>1</sup> Rudolph Callman, *He Who Reaps Where He has Not Sown: Unjust Enrichment in the Law of Unfair Competition*, 55 Harv. L. Rev. 595, 599 (1942).

get to reap what you sow. Instead, under today's laws as they apply to the news business, you get to reap what others sow until you drive them out of business.

The next section ("Summary of the factual and legal problems") explains the basic facts upon which we relied in forming our analysis. The facts described are generalities that we gleaned from interviewing personnel who handle advertising for online websites, handle advertising for newspapers and television stations, and have worked in placing online ads. The facts also come from literature about the subject, and from our own knowledge and observations.

### **Summary of the factual and legal problems as we understand them**

#### **I. General overview of where daily news reports originate.**

In the United States, virtually all information of general public interest published daily about current events – popularly called “news” -- comes from journalists whom companies compensate for gathering information and reporting about it in writing. Even radio and television journalists often begin with news that first appears in writing originated by others who incurred the expenses of initially gathering and reporting that news.

Although it is common to describe news reports as “products,” we believe that it is more valid to view what journalists provide as services.

It requires a large staff of paid journalists plus other expenses to chronicle the newsworthy events of the day in a large metropolitan area. Most of the factual information comprising America's daily news has originated from journalists

employed by newspaper publishers. The publisher of a large metropolitan daily newspaper in a mid-sized American city may employ 200 to 400 journalists, most of them devoted to news and information of local or regional significance. By contrast, a television or radio station in the same market may employ fewer than 25 journalists.

Each day, newspapers deliver fresh news to the public in two ways. One is through newspapers comprised of paper (“hard-copy”), which they sell to individuals for a nominal fee (*e.g.*, 75¢) from news stands, newspaper vending machines, or by paid subscriptions through which the publisher causes an edition of each day’s newspaper to be hand-delivered to the subscriber’s home. The other is through newspaper publishers’ websites where, via personal computer or other electronic device, individuals read current but usually shorter versions of what appears in the hard-copy newspaper.

## **II. Overview of how newspaper publishers produce revenue to recoup the substantial journalistic costs of originating news reports.**

Hard-copy newspapers produce revenue through fees that readers pay for hard-copy newspapers and through fees that businesses pay to advertise in those newspapers.

Advertisers pay most of the revenue that hard-copy newspapers produce. Advertising comprises roughly 40% to 60% of the content of daily hard-copy newspapers. Publishers sell advertising in these newspapers by a quantity of

column-inches, and by the page, or some proportion of a page, such as a quarter-page.

Although newspaper publishers could charge a fee to readers who visit the publishers' websites, they usually do not. Newspaper websites typically produce revenue only through selling advertising positions on the publisher's website. Presumably, publishers have found that online readers are more price-sensitive than readers who are willing to pay 75¢ for a hard-copy.

Newspaper websites receive most of their visitors during working hours, Monday through Friday, suggesting that a large proportion of readers visit newspaper websites using their employers' computer systems. Those visitors, therefore, pay nothing to read online news, not even fees to connect to the internet. That also suggests that hard-copy newspapers delivered to homes on Sundays and Saturdays may have more staying power as substitutes for online news than do hard-copy newspapers delivered during the work week.

### **III. Basics about where newspaper publishers place display ads on newspaper websites.**

Newspaper websites rely primarily on display advertisements, which present words, graphics, and pictures in a format that readers recognize readily as advertisements.

The front ("home") page of many newspaper websites have photographs and captions much as front pages of hard-copy newspapers do. But, unlike the front

page of a hard-copy newspaper, the website's home page rarely has news stories. Instead, the home pages list headlines with electronic links. When a reader (called "users" in online jargon) clicks on the link, it takes the reader to the body of the story on an "inside" page of the website.

Each inside page on the website usually has only one article, whereas each inside page of a hard-copy newspaper usually has several. Display ads appear with each website article, whereas ads do not surround each article on the inside page of a hard-copy newspaper.

Home pages of newspaper websites typically have three-to-four positions for display ads. Each inside page typically has three positions for display ads.

Ads on newspaper websites are measured physically in pixels. "Pixel" means picture-element, a combination of the words "pictures" ("pix") and "element" ("el"). A pixel is the smallest item of information on a page. For example, a huge number of tiny dots comprise the image on a television screen. Each dot is a pixel.

Newspaper websites offer display ads in a variety of sizes. For example, a "leader board" is an ad at the top of the page, which may be 728 pixels across x 90 deep. A "skyscraper" is an elongated ad that may be 160 pixels across x 600 deep.

#### **IV. How newspaper publishers price online display ads.**

Online advertisers using display ads typically pay by the ad impression. An ad impression occurs each time someone loads a page containing the ad onto a

personal computer. That occurs whenever someone uses that personal computer to view the page.

Newspaper websites sell ads based on cpm rates – cost-per-thousand ad impressions. They try to sell ad impressions by blocks of a fixed number of impressions. For example, a website may price display ads based on blocks of 100,000 ad impressions. If an advertiser commits to, say, 1 million ad impressions, the website might charge \$10 cpm. If an advertiser commits only to the minimum block - 100,000 impressions in our example -- the cpm is likely to be above \$10 cpm.

The most expensive cpm rate, sometimes called the “open rate,” applies to ads sold in a volume below the website’s minimum block. If the minimum block is 100,000 ad impressions, and an advertiser commits only to 20,000 impressions, the cpm rate will be higher than if the advertiser had committed to the minimum block. The open rate, which might be \$16 cpm, is the newspaper website’s highest rate. Open rate display ad sales are rare.

The cpm rates that we use in our example are probably below those charged by newspaper publishers in large metropolitan markets, but may be realistic for small daily newspaper markets.

The least expensive ads on a newspaper website are “remnant” ads, which play an important role in our analysis. They work chiefly like this. An advertising

network, such as advertising.com, sells bulk ad impressions to national advertisers, such as Office Max. Advertising.com then provides “ad tags” to the newspaper publisher. The ad tags are codes that the newspaper publisher loads onto its server. The codes allow advertising.com to place remnant ads directly onto the newspaper’s website for positions that the publisher makes available for those ads.

The newspaper publisher typically receives fees for remnant ads far below the publisher’s standard rates. Rates for remnant ads may be below \$1 cpm.

National advertisers can target local markets, such as Pittsburgh, by buying remnant ads through an advertising network. Those ads, then, may appear on the local newspaper website.

Newspaper publishers offer incentives to advertisers to pay the publisher’s standard rates instead of buying much cheaper remnant ads through an ad network. At the publisher’s higher standard rate, the publisher guarantees that the ads will appear when the advertiser wants them to appear, and at more desirable, prominent positions on the site’s pages. The much cheaper remnant ads fill only leftover ad positions that the publisher could not sell at standard rates. So remnant ads usually appear on newspaper sites in less desirable positions and on less predictable dates.

**V. Websites that aggregate summaries or rewrites of news reports that originate from newspapers.**

Increasingly since the mid-1990s, entrepreneurs have created websites that feature the substance of news reports originating on newspaper publishers' websites and in publishers' hard-copy newspapers, usually without the newspaper publisher's consent. We refer to them as aggregators.

Most aggregators do not provide the full range of topics typically offered on newspaper websites. Many are "vertical" aggregators. They specialize in a discrete topic, such as local basketball or gardening.

An aggregator's site may attribute summarized or rewritten news reports to the originator, and may provide an electronic link to the page on the originator's website that contains the article that the aggregator summarized.

The technology of the internet allows aggregators' rewrites of news reports originated by others to reach the reading public at very nearly the same time as the original reports. So online readers can read *The Daily Bugle's* original news stories on either the *Bugle's* website or on a parasitic aggregator's website, and the stories arrive and remain available on both sites at materially the same time and for roughly the same duration. They also may turn up in the same list of online search results.

We label as "parasitic" those aggregators that subsist on the journalistic services of originators of news reports without the originators' consent, and post

enough of the substance of the originator's report to divert materially more readers away from originators' reports than to the originator's report – essentially making the originator's report redundant. Why read the same story twice, those readers say.

**VI. “Pure” aggregators link readers to a newspaper publisher's website, but do not rewrite or summarize a publisher's original reports.**

Another kind of aggregator, which we call a “pure” aggregator, provides readers with a list of headlines for stories that originate on other sites, maybe a partial or complete lead sentence, and maybe a small “thumbnail” photo that appears with the story on the original site. The headlines on the aggregator's site have electronic links that take the reader to the page on the original site where the story appears.

To qualify as a “pure” aggregator under our lexicon, the aggregator must always link to the originator's site and:

1. send materially more readers to the originator's site than the aggregator would send by offering rewrites of the originator's reports; and
2. send materially more readers to the originator's site than the originator would receive if the aggregator went out of business.

The key is that pure aggregators do not post enough of the originator's content to cause most interested readers to substitute the aggregator's summary for the originator's report. Pure aggregators can help newspaper publishers and

other originators of news reports can more readers in the online world. Parasitic aggregators supply too few new readers to originators of news reports to offset their likely destructive impact on originators. Our analyses explain why.

In its present form, we see Google News as a pure aggregator; a parasitic aggregator might be Newser or The Daily Beast.

#### **VII. Why newspaper publishers voluntarily provide some aggregators with links to publishers' websites.**

Newspaper publishers voluntarily provide Real-Simple-Syndication (RSS) feeds to many aggregators at no charge. RSS feeds are headlines for articles that appear on the originator's site with electronic links to the page on that site where the story appears. The RSS feeds may update throughout the day.

When newspaper publishers voluntarily provide their RSS feeds to aggregators for free, they do so primarily for two reasons. One is that they expect the RSS feeds to increase reader traffic to the publisher's website by bringing in readers that visited the aggregator's site instead of going directly to the publisher's site.

The other reason is that search engines, such as Google, track the number of links to given websites. The more websites that link to the newspaper publisher's site, the higher the publisher's site will appear in a list of results of a search that a potential reader conducts on the search engine using words that appear in an article on the publisher's site. The higher a publisher's site appears in a list of

search results, the more traffic the publisher's site is likely to receive.

### **VIII. How aggregators profit from display ads.**

Launching an aggregator website does not require much capital, so the economic barrier to entry is quite low. Many aggregators – pure and parasitic -- operate their sites with only one or two people.

By relying on content originated by others, aggregators need not undertake the labor-intensive work of discovering the news and distilling and writing about it for the first time. That keeps aggregators' operating costs at only a tiny fraction of the journalistic costs that any firm that originates news reports incurs.

A few aggregators charge readers to visit their sites, but virtually all of aggregators' revenue comes from advertising that appears on their sites. Most aggregators do not have a sales staff to sell advertising positions. Instead, they contract with advertising networks to receive the cut-rate remnant ads.

When a local aggregator wants to receive remnant ads from an advertising network, the network usually checks the content of the aggregator's site to ensure that it is not pornography or something with which a national advertiser, such as Sears, would not want to associate its brand.

Because an aggregator has so little capital investment to recoup and its operating costs are so low, the local aggregator apparently can make an acceptable profit from the revenue received from remnant ads alone.

## **IX. Local broadcaster websites can function as parasitic aggregators.**

Websites operated by local radio and television stations can function as aggregators that compete with newspaper publishers' websites.

Many broadcasters employ companies to "host" and design the broadcasters' websites. The hosts provide computer servers that allow readers to access broadcaster sites through the internet. Hosts that specialize in local radio or TV websites provide the sites with entertainment news and other content that is not tied to the broadcaster's geographic region. Companies that host local broadcaster sites sometimes advise that local news and information are significant drivers of reader traffic on those sites.

Local broadcaster websites post local news stories that their own journalists originate. Often, those stories report about the same event that the unrelated local newspaper also covered using the newspapers' own journalists.

As they employ far fewer journalists to cover local news than do daily newspapers, many broadcaster websites expand their local news offerings with rewrites of stories that originated on the newspapers' sites. The broadcaster sites may attribute those rewrites to the originating newspaper, but rarely link to the newspaper's site. In that sense, local broadcaster sites can function as parasitic aggregators.

Typically, local broadcaster sites feature display ads. The same staff that sells on-air commercials also may sell the online ads. Local broadcasters price

their display ads using their standard cpm rates together with much cheaper remnant ads much the same way that newspaper sites do. Local broadcasters regularly accept cpm rates that are below the standard rates charged by the local newspaper site.

When local broadcaster sites contain rephrased local stories that originated from a local newspaper publishers' website, the broadcasters' sites may rank above the newspaper publisher's site in a reader's search results.

**X. Reader traffic on a newspaper website vs. reader traffic on aggregators' websites.**

Readers can connect to newspaper websites by searching the name of the newspaper on a search engine such as Google. Those readers get a list of search results that includes the newspaper's site, and they click on the result that links to that site. That may account for 20-30% of reader traffic to the site.

Other traffic comes from word searches that yield a list of results that includes the newspaper publisher's site; links through the newspaper's RSS feeds or other links to the newspaper's site; readers accessing the newspaper's site directly by typing the newspaper's Uniform Resource Locator (URL) web address in the address bar at the top of the screen on the search engine's home page; and readers effectively doing the same thing by saving a link to the site on their internet browsers as a "bookmark" or "favorite" and then clicking on that link when they want to visit the site.

Usually, a newspaper publisher's site gets many times more reader traffic than any single aggregator site containing rewrites of a publisher's stories, including any single local broadcaster's site. When combined, however, all aggregators rewriting a newspaper publisher's content have substantial reader traffic that can more meaningfully rival the publisher's traffic. The ad rates charged by those aggregators combine to influence the overall market rate for display advertising associated with online news. We explain that effect in much greater detail later.

**XI. The federal copyright act allows parasitic aggregators to "free-ride" on others' substantial journalistic investments.**

To commercially exploit the substance of a newspaper publisher's original news report, the aggregator pays nothing to the publisher. Parasitic aggregators typically do not seek or receive the publisher's consent to exploit the substance of the publisher's news.

That is because the federal copyright act does not compel the aggregators to get the publishers' consent to summarize or excerpt the publishers' original news reports, or to link to them. Indeed, the copyright act effectively encourages the aggregators to free-ride on the expensive news-gathering efforts of the publisher.

Copyright protects writings that originate in the mind of the writing's author. Because facts originate outside the author's mind, copyright does not protect facts. Nor does copyright protect an author's investment in time and

resources to discover and document facts. Copyright protects only the author's original language in describing fact, but not the facts themselves.

Even where copyright protects an author's original language, the copyright act allows others to excerpt it verbatim in various contexts – including competitive commercial contexts -- as a “fair use.” A fair use does not infringe copyright.

Also, copyright protects only the *copying* of original expression. When an aggregator links to a newspaper publisher's website, the aggregator is not copying the content of that site. The link merely causes the reader's internet browser to open a new window or tab, which loads the publisher's content page onto the reader's personal computer. That page replaces the aggregator's page.

The copyright act extinguishes all state laws – statutes and caselaw – that would protect expression in ways that equate with providing a copyright. That may imperil state statutes or common law that would protect originators of news reports against parasitic aggregators or others who commercially exploit the substance of others' news reports.

**XII. Newspaper publishers find that they cannot recover their journalistic costs by commercially exploiting their own reports online.**

Many newspaper publishers are discovering that their websites cannot command sufficient advertising revenue to pay for their substantial journalistic expenses. Nor can they recoup enough money in hard-copy display ads to cover those expenses without cutting their journalistic staffs.

## Structure and summary of our analysis

We offer an economic analysis to explain why prevailing law converges with the ready-availability of current online daily news reports to prevent an originator of news coverage from recovering enough money in advertising fees to cover its journalistic investment.

First, we explain why those who rewrote daily newspaper reports for profit did not threaten the survival of newspapers before the internet became a popular vehicle for the public to obtain daily news.

Second, we use a hypothetical to show how basic economic theory works in the context of parasitic aggregators to endanger the survival of daily newspapers and others that originate comprehensive news reports.

Third, we apply the principles of that hypothetical and other economic theory to show how the law allows parasitic aggregators to compete destructively and unfairly with newspaper publishers and other originators of daily news content even though any single aggregators' readership is far below that of the website of a typical metropolitan newspaper.

Fourth, we propose a modest change in the copyright act that we believe would lead to adjusting the economies of originating written daily news reports. If adopted, our proposal should enhance the ability of originators of current news reports to recover their hefty journalistic costs and make a profit through

advertising revenue.

Changing the law should would restore to newspaper publishers and others who invest in news-gathering the legal rights against unfair competition that may be absent today. Originators of daily news reports could leverage those rights to require aggregators to link to their sites without rewriting their stories, or to contract with them on some other terms.

That should curb substantially what we see as destructively unfair competition by parasitic aggregators that commercially exploit summaries of newspaper publisher's original stories in direct competition with the publishers.

Finally, we explain that "pure" aggregators can have an organically different impact on originators of daily news reports. We conclude that the net economic effect of pure aggregators benefits many originators of daily news reports, including newspaper publishers. We explain that it probably would be fruitless if publishers charged fees to Google News or to similar pure aggregators as a condition for those aggregators linking to the publishers' websites. We address Google News in some detail and compare it with Yahoo News, which is not a pure aggregator.

Our recommended change in the law would give originators of news the flexibility to preserve the benefits of pure aggregators while trying to snuff out parasitic aggregators.

## Economic analysis

### I. Why the copyright act's protection of those who rewrite newspaper stories for profit did not endanger the survival of newspapers before now.

Until the internet became available and popular as a medium through which the public obtains daily news reports, the highly perishable commercial value of news posed a formidable barrier to those who wished to accomplish what the aggregators accomplish now on the internet.

Suppose, for example, that, in 1920, an entrepreneur contracted with a printer to publish a new daily newspaper – *The Crier* – which would devote most of its content to rephrased news reports originally appearing in the unrelated *Daily Bugle*, a morning newspaper. By the time the rewritten *Bugle* stories appeared in *The Crier* – maybe very late that day or the next day -- they would be old news.

Even if advertisers could buy space in *The Crier* at rates substantially below the *Bugle's* rates, *The Crier's* readership probably would be too small to attract enough money from advertisers to cover the cost of producing and distributing *The Crier* as a belated rewrite of *The Bugle*. Except in history books, old news commands few readers.

So even though copyright laws allowed printers to sell paraphrased news reports originated by other publishers, the commercial value of the originally-reported news dissipated too quickly and the time to print and circulate rewrites took too long to allow the printer to exploit the economic advantages that the

copyright act provides to those who copy or rewrite others' news reports.

Then came commercial radio. Radio newsrooms have been rewriting newspaper stories for years and reporting the rewrites in their newscasts – often with a modest update -- around which they sell advertising. Unlike a rewrite in *The Crier*, a radio broadcaster's rewrite of a *Bugle* newspaper story can be as fresh as the *Bugle's* report.

But the ability of one product or service to impinge on the market for a different product or service depends on how closely a buyer can substitute one for the other in the marketplace.

For example, a baseball fan either can buy a ticket to attend a major-league game or read a newspaper account of the game published later. A ticket to attend the game is far more expensive than buying a newspaper. Although the availability of the much cheaper newspaper report may cause a few fans to forego buying a ticket to see the game, the newspaper account arrives after the game is over and cannot replicate the excitement of witnessing the game in person.

The availability of a newspaper account is a remote substitute for attending the baseball game and likely would not jeopardize the professional baseball club's survival.

Broadcast radio news is a remote substitute for newspapers. Radio broadcasts the news only during fixed time slots selected by the broadcaster.

Listeners can't replay what they missed, or select only the sports report at the moment when they want to receive it. Because radio reports are oral, they convey little detail because it is hard to for listeners to grasp much detail when delivered orally.

Undoubtedly, radio cut into the newspapers' advertising revenue stream, but radio did not provide a close enough substitute to jeopardize the newspaper industry. Newspapers can thrive with large staffs of journalists despite the law giving radio a free ride on newspapers' costly journalistic services.

But the internet is far different.

## **II. Online rewrites of daily news reports are close substitutes for the original news reports.**

The speed and technology of the internet allows aggregators to overcome the practical obstacles that barred radio and printers from taking full economic advantage of copyright's limits.

Web technology allows people to read aggregators' rewrites of newspaper stories at about the same time and through the same medium as they can read the newspaper's original stories, and they can select which stories to read and the time when they want to read them.

By combining the fresh timing of radio with the convenience of being able to choose which reports to read at any given time, online news has become a close substitute for newspapers – hard-copy or online.

Obviously, online rewrites of originators' online news reports are close substitutes for one another. Evidence that online news also is a close substitute for hard-copy newspapers is the rather abrupt change in how large metropolitan newspapers use their own reporters to cover national and global news.

The publishers of many large daily newspapers in cities outside of New York and Washington, D.C. used to have bureaus in the nation's capital from which the publishers' full-time journalists covered news generated by the activities of the federal government. During the past two years, publishers of daily newspapers in Philadelphia, Cleveland, Pittsburgh, San Diego, Houston, Newark, Hartford, San Francisco, Des Moines, and Atlanta stopped employing full-time reporters in Washington, D.C. to cover federal government.

The ready availability of current online reports of national and world news originating from the "top brands" for that kind of news – The New York Times, The Washington Post, the television and cable networks, USA Today, and others – apparently has supplanted the local hard-copy newspaper as many local readers' chief source for written national and global news. That would not happen to the same degree if online news were only a remote substitute for hard-copy newspapers.

**III. An analogy illustrating basic economic theory explains how the copyright law imperils all originators of written daily news reports available on the internet.**

To understand how the federal copyright law interacts with aggregators that commercially exploit rewrites of originators' news reports to prevent the originators from recovering their substantial journalistic investments, consider this hypothetical analogy.

Suppose that a company hires a workforce, buys fabric, and buys equipment to make white t-shirts. The company sells those shirts to retail stores. If that company enjoys profits, those profits will attract competitors.

Each competitor will hire its own workforce, buy fabric, and buy equipment to make t-shirts. The t-shirt makers will undercut each others' prices to attract purchases by the retailers. Ultimately, that competition will drive the price of each t-shirt down to a level that covers the cost of making each shirt plus a profit acceptable to the t-shirt makers.

Now suppose that some other firms decide to buy t-shirts from the t-shirt makers, but they apply dyes to give the t-shirts a beige color. Assume that dyeing each shirt is an added cost and that the dyeing firms compete with each other to sell beige t-shirts to retail stores. That drives the dyers' prices down to reflect the costs of acquiring the t-shirt and dyeing it, plus a modest profit. The price of beige shirts, therefore, will exceed the price of the white shirt.

If enough consumers prefer beige shirts over white shirts, the dyers might

stay in business despite the higher price.

Now suppose that a change in the law requires each maker of white t-shirts to allow dyeing firms to take some proportion of shirts from the t-shirt maker's inventory at no charge – say, 50 out of every 100 -- so long as the dyeing firms alter the color of the shirts.

The competition among the dyers to sell their shirts will force them to undercut each other in price. Because the dyers acquired their t-shirts for free, their competition will drive the price of dyed shirts down to the cost of dyeing the t-shirts plus a modest profit. Their prices will not reflect the cost of making the shirts. The price of a dyed shirt will be below the price of the foundational white shirt upon which the dyers rely.

The companies that make the white t-shirts will not be able to compete by dyeing their own shirts. To be profitable, those companies must price their dyed shirts to reflect both the cost of making the shirt and the cost of dyeing it. The dyeing firms' prices need cover only the cost of dyeing. By matching the market price established by the dyers, the company that makes the shirts will be driven out of business.

If the makers of white t-shirts go out of business, the dyeing firms will have no shirts to color and therefore none to sell. Even if some dyeing firms enter the business of making white t-shirts, the fatal spiral will recur. The law will allow

other dyeing firms to help themselves to 50% of the new t-shirt makers' inventories for free and then to compete directly against the new shirt makers with cheaper dyed shirts. They eventually will drive the new shirt makers out of business, too.

Although the dyers have a vested incentive not to price the suppliers of white t-shirts out of business, competition among dyers invariably will force them to set prices that reflect only their own dyeing costs plus acceptably modest profits. Those low prices will drive the originators of the t-shirts out of business because the originators cannot match the dyers' prices profitably.

Obviously, the makers of white t-shirts in our hypothetical are the newspaper publishers who invest in journalistic services to originate daily written news reports, and the dyers are the parasitic aggregators that commercially exploit rewrites of those news reports. The t-shirt prices are advertising rates, and the hypothetical law is a rough analogy to the federal copyright act.

**IV. The federal copyright law converges with the unique qualities of the internet to imperil the economic viability of originating written daily news reports.**

Because the internet enables parasitic aggregators to provide the public with rewritten versions of the originators' reports nearly as quickly as the originators can provide them, the aggregators can exploit those reports before they lose their short-lived commercial value.

Because the aggregators and the originators use the same news reports, they

will attract readers of similar demographics, and therefore the same kinds of advertisers. As parasitic aggregators enter the market, they will compete for advertising dollars by undercutting each other's ad rates, which drives market ad rates downward.

If those aggregators were like newspaper publishers – bearing the costs of disseminating the news and the journalistic costs of gathering the news – the competition among them and with the newspaper publishers for advertising would cause rates to fall to a level that would cover the journalistic costs to originate news reports, the costs to disseminate the reports, plus modest profits.

But because the parasitic aggregators do not bear the labor-intensive journalistic costs, they will compete by pushing market rates for advertising down until the rates reflect the lower costs incurred by the aggregators plus a modest profit. The publishers that originate those news reports, however, cannot profit at those rates because they must bear the journalistic costs of producing the original news reports.

Advertising firms that specialize in placing ads on newspaper websites have found that some national advertising clients have decided to shift ad dollars away from the newspaper sites to remnant ads on a range of aggregator sites. “Why pay 10 times more for only double the audience,” those clients say. If the newspaper publisher then tried to recapture those ad dollars by lowering its rates to only

double the aggregators' rates, the publisher might recapture that business but likely at a loss.

That is analogous to the dyers in our hypothetical driving down the price of t-shirts until they reflected only the costs of dyeing the shirts, which the makers of the shirts could not profitably match.

The aggregators' effect on advertising rates would be less acute if the capital investment required to become an aggregator was steep. But because startup costs are quite low, entry into the online market for readers and advertising is relatively easy, which attracts more aggregators seeking low-cost profits. The greater the influx of those aggregators, the greater the market pressure to reduce ad rates to levels that sustain the aggregators, but not the originators.

Similarly, if parasitic aggregators could not exploit the substance of originators' news reports lawfully without the originators' consent, the originators and the aggregators could stay in business. Competition among aggregators for the right to carry the stories to attract ad revenue would drive up prices for the right to do so.

Meanwhile, competition among the originators of the stories to sell those rights to aggregators would counteract the effect of the competing aggregators. It would drive those same prices down. The market prices eventually would settle at a level that leaves both aggregators and originators with adequate profits,

regardless of whether the source of those profits is ad revenue, the sale of rights to use the stories, or some combination of both.

Normally, the free market system benefits when competing, more efficient producers drive prices down to a level that puts inefficient producers out of business. In the online news scenario, however, the aggregators are not more cost-efficient than the newspaper publishers in gathering and discovering current news. Rather, the copyright act effectively compels the newspaper publishers to subsidize the aggregators by supplying those competitors with the journalistic services that produce the core of the commercially valuable news reports.

A newspaper publisher exploits its journalistic services commercially by publishing the reports that result from those services. But once published, the publisher's entire news "inventory" instantly is supplied at no charge to every other purveyor of ad space associated with online news. They need only summarize or rewrite the reports to avoid copyright's interference.

Remarkably, copyright law protects the parasitic aggregator's feeding off of the journalistic investment of the originator, but it does not protect the journalistic investment itself. And, as our legal analysis later shows, the copyright act may block other laws from protecting that investment.

**V. Transfer-pricing policies of vertically-integrated firms offer a real-life example of how a firm that relies on a supplier can unintentionally drive the supplier out of business.**

That aggregators could drive the newspapers out of business, despite needing newspapers to supply current news content, is not mere speculation. Firms that are vertically-integrated – they own both the maker of finished goods and the supplier of components for those goods -- have standard safeguards to prevent exactly that kind of problem.

In vertically-integrated firms, a parent company controls a separately-managed firm that makes goods in their finished form and sells them to customers – call it the assembly-firm. The parent company also owns a separately-managed firm that makes or procures components used in making those finished goods – call it the supplier-firm.

If the parent company allowed the supplier-firm to provide components at no charge to the co-owned assembly-firm, the assembly-firm might endanger the survival of the supplier-firm. Price competition from unrelated competitors will limit how much the assembly-firm can charge for the finished goods. Within those limits, the assembly-firm will price the goods to maximize its apparent profit based on the costs that it incurs. The assembly-firm's self-interest may provide an incentive to charge a price that is not high enough to cover the supplier-firm's costs of supplying the component.

The assembly-firm has only an "apparent" profit because, if the assembly-

firm's managers treat the free component as costing the assembly-firm nothing, sales revenue that exceeds only the costs that the assembly-firm counts as expenses appears to be profit. From the perspective of the parent company, however, it is not profit because the supplier-firm incurred real expenses to procure or make the "free" component, and those expenses are not recouped in the assembly-firm's price.

To protect against that happening, vertically-integrated companies require their finished-goods firms to *pay* for the components that the co-owned supplier-firms provide. That forces the people who operate the assembly-firm to charge a price for the finished good that reflects the cost of the supplied component. That practice, called transfer pricing, keeps the parent company's finished-goods manufacturer from driving the co-owned supplier out of business.

If co-owned vertically-integrated firms need transfer pricing to ensure the survival of the supplier-firm, newspapers require what amounts to the same thing. They need the functional protection of transfer pricing to ensure their survival in supplying unrelated aggregator-competitors with daily news. Current law compels them to supply that news for free, which enables the aggregators to drive down the market price for advertising – endangering the newspapers' survival.

**VI. “Public goods” theory multiplies the magnitude of the threat to originators of news reports.**

The parasitic aggregators may argue that our t-shirt hypothetical is inapt because news stories are what economists call “public goods.” Public goods are those where consuming one good does not reduce the quantity of goods that the producer can make available to other customers.

A t-shirt is not a public good because, if Dyer-X takes or buys a shirt from the t-shirt maker, the t-shirt maker cannot sell that shirt to another dyer.

Although primarily a service, a news story functions as a public good because, if an aggregator paraphrases or excerpts a news story, that does not deplete the publisher’s supply of that story. The publisher still has its original “supply” to exploit commercially.

The “public-goods” quality of news reports, however, accelerates the economic dilemma that originators of daily news coverage face. If Aggregator-A takes the substance of a *Daily Bugle* report and sells ads around it, that does not reduce the available supply of that report for Aggregators B, C, D, E, and others. They, too, can take the same story, rewrite it, and sell ads around it, undercutting each other and Aggregator-A in price. Each additional free rider plays a role in driving advertising rates down to a level too low to sustain the publisher that originated the news reports.

Compare that with our t-shirt hypothetical. In our hypothetical, the law

allowed the dyers to take 50 out of every 100 shirts for free. If Dyers A, B, and C took a combined 50 shirts, there would be no free t-shirts left for Dyers E, F, G and others. The potential influx of competing free-riders would be smaller in our hypothetical than in the newspaper business.

Ultimately, original news reports will be underproduced unless the supplier of the underlying journalistic services can exclude others from free-riding on those expensive services – at least for enough time to allow the supplier to recoup the investment.

The legal system must provide a brief window during which aggregators cannot freely exploit others' original news reports in near-simultaneous direct competition with them. Absent that window, our t-shirt hypothetical will become reality for the news business.

We explain the underproducing of news next.

**VII. If the law does not change, newspapers continually will diminish their journalistic resources until they can subsist only by underproducing news or until they go out of business.**

Large metropolitan dailies have shifted their journalistic resources to covering news that is local to the geographic areas where their hard-copy newspapers primarily circulate and where they have strong brand recognition for conveying local news, which the top national news-brands do not carry.

Because shifting away from originating news reports of national import and focusing on originating news reports of regional import requires fewer journalists,

most large city dailies have reduced their staffs of full-time journalists.

But that shift does not account for the continuing economic pressure on daily newspapers to reduce their journalistic staffs further. More powerful economic forces – largely promoted by the federal copyright act -- are responsible for that.

Nearly all of a newspaper's journalistic costs are fixed in the sense that the costs to produce one issue of a newspaper does not vary with the number of copies of that issue that the publisher sells. The same is true of any enterprise – online or otherwise -- that originates news reports.

A newspaper publisher requires the same number of journalists at the same level of wages and expenses to produce the stories that appear in one copy of one issue of the newspaper as it does to produce 200,000 copies of the same issue. But the publisher can command substantially more advertising revenue by producing and circulating 200,000 copies of that issue than by producing and circulating only one.

So, when a newspaper's advertising revenue drops, it does not experience an automatic and corresponding drop in journalistic costs. Those costs stay the same if the publisher employs the same number of journalists. A sustained decline in ad revenue, therefore, quickly threatens a newspaper's viability.

When free-riding aggregators divert ad revenue from newspaper publishers

at rates the publishers cannot match, and because most of the newspaper's journalistic costs are fixed, a newspaper publisher has little recourse but to reduce its news gathering costs to avoid sustaining significant losses. Typically that means laying off journalists.

But reducing the number of journalists also reduces the actual and perceived quality and scope of the newspaper's news coverage. That may reduce the number of readers, which attracts fewer advertising dollars, leading to more layoffs of more journalists, and so on.

Ultimately, that downward spiral will reduce the overall quality and scope of daily news coverage in the marketplace – regardless of who originates it. It likewise will reduce the perceived or actual value of what the aggregators can offer. In the end, news will be underproduced.

Changing the law can stop that spiral.

## **Legal analysis and proposed change to the copyright act**

### **I. Summary of *International News Service v. Associated Press*.**

In 1918, the United States Supreme Court decided a case about competition in the news business that presented essentially the same economic problem for the Associated Press that the aggregators now present for originators of news reports.

The Associated Press employed correspondents in Europe covering World War I, and sent their news dispatches to New York City. There, New York newspapers that contracted with AP published the dispatches in the newspapers'

early editions. AP also posted its dispatches on bulletin boards available to the public. AP did not claim a copyright in those news reports.

According to the Supreme Court's opinion, journalists in New York working for the International News Service, a smaller for-profit competitor of AP, copied or rewrote AP's dispatches from the bulletin boards and early editions of New York newspapers. INS then sold the copied or rewritten dispatches to newspapers in western U.S. time zones. INS transmitted them by telegraph and telephone.

That resulted in western newspapers reporting the INS dispatches at the same time that other western newspapers reported the identical dispatches originating from AP, and sometimes the INS dispatches appeared before those from AP.

AP sued in federal court in New York City to enjoin INS from continuing that practice. The federal court enjoined INS, but did not bar INS from selling copied or rewritten AP dispatches at all times and under all circumstances. Instead, the court enjoined INS from doing so only for the brief, but indefinite, period while AP's dispatches had commercial value.

The case went to the United States Supreme Court, which affirmed the injunction, 6-2. Applying what is today called federal common law, the majority ruled that INS engaged in unfair competition. The Court recognized that allowing INS to continue its practice would drive originators of news reports out of

business. The Court realized that INS would incur disproportionately low costs in competing against AP, using AP's own journalistic services.

The Court characterized INS as misappropriating the "quasi-property" of AP, a legal framework with which we disagree. But we concur with the Court's underlying reasoning, which largely mirrors a more modern legal theory under state common law now called "unjust enrichment." Separated into digestible parts, the Court's long passages explained:

The right of the purchaser of a single newspaper to spread knowledge of its contents gratuitously, for any legitimate purpose not unreasonably interfering with complainant's right to make merchandise of it, may be admitted;

but to transmit the news for commercial use, in competition with the complainant – which is what defendant had done and seeks to justify – is a very different matter.

In doing this defendant [INS], by its very act, admits that it is taking material that has been acquired by the complainant [AP] as the result of organization and the expenditure of labor, skill, and money, and which is salable by complainant for money,

and that defendant in appropriating it and selling it as its own is endeavoring to reap where it has not sown, and by disposing of it to newspapers that are competitors of complainant's members is appropriating to itself the harvest of those who have sown.

*International News Service v. Associated Press*, 248 U.S. 215, 239-240 (1918).

The Court added:

Stripped of all disguises, the [INS pirating] amounts to an unauthorized interference with the normal operation of complainant's legitimate business precisely at the point where the profit is to be reaped,

in order to divert a material portion of the profit from those who have earned it to those who have not; with special advantage to defendant [INS] in the competition because of the fact that it is not burdened with any part of the expense of gathering the news.

*International News Service v. Associated Press*, 248 U.S. 215, 240 (1918).

If the Supreme Court's ruling and analysis in the *INS* case were powerful legal precedent today, the parasitic aggregators of news on the internet would not be able to sustain their current practices. Newspaper publishers and other originators of news content would have enough legal leverage over those practices that the aggregators would seek contracts with the originators to commercially exploit the original news reports. They would abandon their free-riding on the newspapers' resources, which allows aggregators artificially to drive down the market rate for online advertising to levels below the newspapers' journalistic costs.

Largely because of the copyright act, however, the *INS* case has lost much of its juice.

## II. The weakening of the *INS* case.

Oliver Wendell Holmes and Louis Brandeis, two of the most respected jurists in our history, dissented separately in the *INS* case. Justice Holmes argued that only legislators – not judges -- could create the legal theory for unfair competition upon which the majority relied.

Justice Brandeis agreed, but also forcefully argued that, because copyright did not protect AP's dispatches, no other existing legal theory could protect them. He expressed concern that the majority opinion would allow news-gatherers to monopolize factual information of public interest that the copyright act placed in the public domain. Justice Brandeis noted:

To appropriate and use for profit, knowledge and ideas produced by other men, without making compensation or even acknowledgment, may be inconsistent with a finer sense of propriety; but . . . the law has heretofore sanctioned the practice [except in copyright].

*International News Service v. Associated Press*, 248 U.S. 215, 257 (1918) (Brandeis, J., dissenting).

Over time, many scholars and judges thought that Justice Brandeis had the better analysis. For that and some other technical reasons, courts generally have treated the *INS* ruling as weak, unreliable precedent.

Congress further confined the *INS* case when it revised the copyright act in 1976. It enacted a new section, 301, that abolishes any rights under state common law or state statutes that protect rights in expression if functionally the same as

granting a copyright.

A draft of § 301 had included a clause that listed examples of state-law rights that resemble copyright, but function differently, and therefore would survive despite the copyright act. The clause specifically listed “rights against misappropriation” as among those preserved state rights. Senate and House committee reports specifically cited the *INS* decision as an example of common-law misappropriation that the copyright act did not pre-empt.

But in July 1976, just before the final House debate on the copyright bill, the U.S. Justice Department sent a letter to the chair of the House subcommittee overseeing the bill. The Department objected to preserving the misappropriation theory of *INS*. It mischaracterized the *INS* decision as affording a boundless monopoly over uncopyrighted factual information of public interest that deserves to be in the public domain. In fact, the *INS* decision gave AP only a brief head start over *INS* in commercially exploiting AP news reports.

The House then struck the bill’s reference to misappropriation during the final House debates. While expressly abolishing all state statutes and common law that afford the functional equivalent of copyright, § 301 now says that it does not preempt state-law rights that “are not equivalent to” federal copyright. It does not identify those surviving state-law rights.

A few federal courts have decided that the *INS* theory does not equate with

copyright, ruling that § 301 does not preempt the *INS* theory. The question remains murky, however, and for that reason is expensive to litigate and too unpredictable.

### **III. Our recommendation to change the law.**

We recommend amending § 301 of the copyright act to make clear that, in the context of unfair competition among direct competitors, the unjust enrichment theory underlying the *INS* decision remains viable as a matter of state law. The copyright act, then, would not preempt state common law or state statutes that afford rights to competitors under that unjust-enrichment theory.

For various analytical reasons, however, we do not endorse the “misappropriation” of “quasi-property” that *INS* describes. We endorse only the underlying unjust enrichment rationale as applied to direct competitors.

Unjust enrichment theory in unfair-competitor contexts would entitle the originator of news reports to two kinds of remedies against competing parasitic aggregators. One would be to require those aggregators to disgorge revenues received from advertising associated with the substance of the originator’s news reports.

The other would be to obtain an injunction against parasitic aggregators similar to that affirmed by the Supreme Court in *INS*. In effect, the injunction would bar those aggregators from commercially exploiting the substance of the originator’s news reports in direct competition with the originator, but only for a