

WASHINGTON AND LEE  
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**WASHINGTON & LEE**

**Legal Studies Research Paper Series**

Accepted Paper No. 2005-14  
October 2005

**SOME OBSERVATIONS ON THE  
LAW AND ECONOMICS OF INTERMEDIARIES**

**THOMAS F. COTTER**

**MICHIGAN STATE LAW REVIEW  
FORTHCOMING (2005)**

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# SOME OBSERVATIONS ON THE LAW AND ECONOMICS OF INTERMEDIARIES

*Thomas F. Cotter\**

2005 MICH. ST. L. REV. 1

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## INTRODUCTION

Let me begin by thanking Professor Peter Yu and the faculty and staff of the Michigan State University College of Law for inviting me to participate in, and to prepare this essay in connection with, the law college's April 2005 conference titled "W(h)ither the Middleman: The Role and Future of Intermediaries in the Information Age." Professor Yu hardly could have timed the conference any better, coming as it did less than two weeks after the U.S. Supreme Court heard arguments in the *Grokster* case<sup>1</sup>—and the very week in which the British magazine *The Economist* devoted its cover story to a special report titled *Power At Last: How the Internet Means the Consumer Is Really King (and Queen)*.<sup>2</sup> Predicting which intermediaries will succeed and which will fail in the Internet Age, and determining what approach (if any) the law should take with respect to intermediary regulation, are some of the most pressing issues facing legal policymakers today.

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\* University of Florida Research Foundation Professor, University of Florida Fredric G. Levin College of Law. As of July 1, 2005, the author will be Professor of Law at Washington and Lee University School of Law. I thank Andrea Matwyshyn and Bill Page for useful comments, and Diego Puig for excellent research assistance. Any errors that remain are mine.

1. See *Metro-Goldwyn-Mayer Studios Inc v. Grokster, Ltd.*, 125 S. Ct. 686, *granting cert. to* 380 F.3d 1154 (9th Cir. 2004); see also *Grokster Lawyer Intrigues Court by Arguing About Procedural Effect of Ruling to Affirm*, BNA'S PATENT, TRADEMARK & COPYRIGHT J. (Apr. 1, 2005), at 560 (discussing the oral argument before the U.S. Supreme Court).

2. THE ECONOMIST (Apr. 2nd-8th 2005).

Perhaps the best place to start is with some terminology. Broadly construed, an “intermediary” can be any entity that enables the communication of information from one party to another. On the basis of this definition, any provider of communications services (including telephone companies, cable companies, and Internet service providers) qualify as intermediaries.<sup>3</sup> A growing body of literature addresses the question of whether, or when, these entities should be liable when others use their services to engage in unlawful conduct.<sup>4</sup> Since no one that I am aware of is predicting the complete and utter demise of these types of intermediaries,<sup>5</sup> I surmised that the conference was mostly intended to address (and my focus in the remainder of this essay will center exclusively upon) another type of intermediary, the existence of which is, in some instances at least, potentially threatened by the Internet: namely, the economic agents that help to reduce the costs of buyer-seller transactions, by enabling buyers and sellers to find one another and to sort, classify, and distribute information to one another.<sup>6</sup> Although some observers, as early as the late 1980s, predicted that the digital revolution would lead to the demise of these latter intermediaries (“disintermediation”), others argued instead that intermediaries would still be necessary to perform a variety of services—and that the need for intermediaries might even increase in some settings.<sup>7</sup> As we shall see, the latter view has proven to be the more correct. Although some

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3. For that matter, any tangible artifact—a writing, a painting, a sound recording, a motion picture—is, by itself, an intermediary that facilitates the communication of ideas or expression from the brain of one person to the brain of another. For discussion, see, e.g., Thomas F. Cotter, *Memes and Copyright*, 50 TUL. L. REV. \_\_, \_\_ (forthcoming 2005).

4. See, e.g., Doug Lichtman & Eric Posner, *Holding Internet Service Providers Accountable*, \_\_ S. CT. ECON. REV. \_\_ (forthcoming 2005); Ronald J. Mann & Seth R. Belzley, *The Promise of Internet Intermediary Liability*, 47 WM. & MARY L. REV. \_\_ (forthcoming 2005).

5. Although developments such as Internet telephony will certainly have an impact upon the providers of traditional telephone service.

6. The above is a fairly standard definition of this second type of “intermediary.” See, e.g., BETHANY L. LEICKLY, INTERMEDIARIES IN INFORMATION ECONOMIES: A THESIS SUBMITTED TO THE FACULTY OF THE GRADUATE SCHOOL OF ARTS AND SCIENCE OF GEORGETOWN UNIVERSITY IN PARTIAL FULFILLMENT OF THE REQUIREMENTS FOR THE DEGREE OF MASTER OF ARTS OF COMMUNICATIONS, CULTURE AND TECHNOLOGY 1, 5 (Apr. 30, 2004), available at [http://cct.georgetown.edu/thesis/Bethany\\_Leickly.pdf](http://cct.georgetown.edu/thesis/Bethany_Leickly.pdf):

An intermediary works as an economic agent who helps buyers and sellers find each other and execute a transaction. Equally important, they help to sort, classify and distribute market information and goods. . . . Historically, intermediaries found a niche in markets where transaction costs were high, and they served both the buyer and the seller in reducing these costs.

Leickly’s thesis, which I cite several times herein, is a good source for much of the existing literature on intermediaries.

7. See *infra* notes 24-30 and accompanying text.

of the services traditionally performed by intermediaries can, in the digital era, be performed directly by consumers or producers, intermediaries still perform, and will continue to perform, many useful functions. An important goal of the ideal regulatory system therefore may be to facilitate the reduction of transaction costs that arise from the various transactions to which consumers, producers, and intermediaries are parties. Among other things, this task may involve determining whether, and how, to regulate those intermediaries that remain (or that owe their very existence to the digital revolution); and whether it may be useful in some instances to facilitate further disintermediation (and if so, how). Figuring out how to accomplish these tasks, however, is no mean feat.

I begin in Part I by reviewing some of the existing literature on intermediation, much of which derives from a classic 1995 paper by Mitra Barun Sarkar, Brian Butler, and Charles Steinfield.<sup>8</sup> In Part II, I consider some ways in which law might play a useful role in reducing the social costs of acquiring, evaluating, and managing information, or enabling the reduction of these costs; but I also note how difficult it can be to predict the optimal legal response in a given setting.

## I. ON THE ECONOMICS OF INTERMEDIARIES

Historically, the intermediaries about which I will remark have performed an economically useful function of reducing the transaction costs attendant to buyer/seller transactions. As Leickly observes:

An intermediary steps in to overcome information asymmetry, information impactedness, distrust, and high transaction costs associated with information. An intermediary functions by seeking out suppliers, finding and encouraging buyers, selecting the buy and sell prices, defining the terms of transactions, managing the payments and keeping records of transactions, and holding inventories to provide liquidity or availability of goods and services. Intermediaries provide utility by increasing the chances of a successful match between buyers and sellers, thus the need for an intermediary will come about because of the frictions in the market. . . . The intermediary can be interpreted as a firm that acts to reduce transaction costs. . . . Intermediaries also emerge as information producers because the production of information, the protection of confidentiality, the provision of transaction services, as well as other intermediary services, are naturally complementary activities.<sup>9</sup>

In their 1995 paper, Sarkar, Butler, and Steinfield catalogued a variety of specific intermediary functions, some of which center more on consumers and

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8. See Mitra Barun Sarkar et al., *Intermediaries and Cybermediaries: A Continuing Role for Mediating Players in the Electronic Marketplace*, 1 J. COMPUTER MEDIATED COMM., No. 3 (1995), available at <http://www.ascusc.org/jcmc/voll/issue3/sarkar.html>.

9. Leickly, *supra* note 6, at 25-26.

others on providers. According to their analysis, intermediaries may assist consumers by reducing the cost of product search and evaluation,<sup>10</sup> helping consumers to find the products that best fit their needs,<sup>11</sup> and helping consumers to manage risk.<sup>12</sup> In addition, intermediaries sometimes assist producers with respect to distributing products;<sup>13</sup> by informing consumers about the existence and characteristics of products;<sup>14</sup> by influencing consumer purchase choices;<sup>15</sup> by providing valuable information about consumers;<sup>16</sup> and by assisting with producer risk management.<sup>17</sup> Sarkar and his co-authors also noted that the “[t]ransaction services provided by intermediaries are subject to economies of scale, which are often achieved through the use of IT.”<sup>18</sup> Finally, successful intermediaries may need to balance the conflicting interests of consumers and producers.<sup>19</sup> For example, producers presumably want to inform consumers about their products; but consumers might want some of that information filtered out as part of the product search and evaluation process.<sup>20</sup> Producers also may want information about consumers, whereas

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10. Retailers are one entity that often performs these services. *See* Sarkar et al., *supra* note 8, at 7 (stating that “the quality of the goods expected at a flea market, a discount store, and a specialty clothing boutique is significantly different”). In addition, specialized intermediaries such as Consumers Union, the Better Business Bureau, Good Housekeeping, and Underwriters Laboratories sometimes provide useful evaluation services. *See id.* at 7; *see also* Mark R. Patterson, *On the Impossibility of Information Intermediaries*, Fordham University School of Law, Law and Economics Research Paper No. 13, at 4 (July 2001), *available at* <http://papers.ssrn.com/abstract=276968>. These latter may be regulated by the Lanham Act’s provisions on the use of certification marks. *See* 15 U.S.C. § 1054. On a more informal basis, consider the reviews provided by other consumers on websites such as amazon.com.

11. *See* Sarkar et al., *supra* note 8, at 7. An example is Ace Hardware’s “Helpful Hardware Folks.” *See id.*

12. *See id.* at 8 (stating that intermediaries may help consumers manage risk by, for example, “providing consumers with the option to return faulty products or providing additional warranties,” thereby “reduc[ing] the consumers’ exposure to the risk associated with producer error”).

13. *See id.* (citing Federal Express as “a prime example of how information technology has begun to make it economical to provide services independently that historically have been provided by integrated retail intermediaries”).

14. *See id.*

15. *See id.* (citing as examples product placement, explicit advice from sales agents, and shelf space payments).

16. *See id.* (citing as examples the provision of market research, and of aggregating demand information from local markets).

17. *See id.* at 9 (citing as examples retail and credit intermediaries, and the practice of risk-sharing between intermediaries and producers).

18. *See id.*

19. *See id.*

20. *See id.*

consumers would prefer to keep some such information private.<sup>21</sup> And some producers might prefer to provide biased information about their products, but consumers presumably want truthful information. “Ultimately, in a competitive market for intermediary services, a firm which does not successfully balance these needs will lose their suppliers and/or their customers.”<sup>22</sup> In an imperfect market, on the other hand, there is always some risk that intermediaries will bias or skew information in favor of some producers; or that the intermediary will put its own interests first, and will be able to do so because the cost of monitoring the agent’s conduct more closely is too great.

Where intermediaries are unnecessary to reduce transaction costs or to perform these other functions described above, one would expect a perfectly functioning market to eliminate them. Elimination could result from vertical integration of some or all of these functions within one entity that can perform them at lower cost (the classic Coasean explanation for the firm);<sup>23</sup> or it could result from more direct, unmediated consumer-producer transactions. On the basis of this sort of analysis, some observers predicted that, as a general matter, the Internet would reduce the need for intermediaries, because of lower transaction costs.<sup>24</sup>

Other commentators, however, including Sarkar and his co-authors, called into question the demise of intermediaries on the ground that, in some contexts, social costs would be even higher without intermediaries.<sup>25</sup> In this

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21. *See id.* at 8.

22. *Id.* at 9; *see also* Joseph P. Bailey & Yannis Bakos, *An Exploratory Study of the Emerging Role of Electronic Intermediaries*, 1 J. ELEC. COMMERCE 7, 19 (No. 3, 1997); Leickly, *supra* note 6, at 61-64; Patterson, *supra* note 10, at 14.

23. *See* R. H. Coase, *The Theory of the Firm*, 4 *ECONOMICA* 386 (1937). Leickly notes the connection between, on the one hand, the transaction-cost analysis that began with Coase and has been further developed by Oliver Williamson and others, and the disintermediation hypothesis. *See* Leickly, *supra* note 6, at 20-27.

24. *See, e.g.*, Robert Benjamin & Rolf Wigand, *Electronic Markets and Virtual Value Chains on the Information Superhighway*, 36 *SLOAN MGT. REV.* 62, 62 (1995) (suggesting that “all intermediaries between the manufacturer and the consumer may be threatened as the NII reaches out to the consumer”); Thomas W. Malone et al., *Electronic Markets and Electronic Hierarchies*, 30 *COMMS. OF ACM* 484 (1987).

25. *See* Sarkar et al., *supra* note 8, at 7-9; *see also* LARRY DOWNES & CHUNKA MUI, *UNLEASHING THE KILLER APP: DIGITAL STRATEGIES FOR MARKET DOMINANCE* 151-52 (1998); Judy Scott, *Emerging Patterns from the Dynamic Capabilities of Internet Intermediaries*, 5 J. COMPUTER MEDIATED COMM., No. 3, at 3 (2000), *available at* <http://www.ascusc.org/jcmcl/vol5/issue3/scott.html>. Leickly sums it up well:

while communication and technology advances promote disintermediation in some markets, there are instances in which intermediaries can still add value to business transactions. However, intermediaries can only succeed as differentiated, specialized

regard, Sarkar and his co-authors proposed the following taxonomy. First, they noted that, before the arrival of the Internet, the transaction costs attendant to direct transactions would sometimes be greater than the transaction costs attendant to intermediated transactions.<sup>26</sup> If, however, the post-Internet transaction costs of direct transactions turn out to be less than the transaction costs of intermediated transactions, then a perfectly functioning market should result in the disappearance of intermediaries, as suggested above (the “threatened intermediaries” hypothesis).<sup>27</sup> On the other hand, even after the arrival of the Internet the transaction costs of some direct transactions may continue to be greater than the transaction costs of intermediated transactions; In such cases, one might predict the appearance of what Sarkar and his co-authors refer to as “NII [National Information Infrastructure] Supplemented Intermediaries.”<sup>28</sup>

Alternatively, pre-Internet the transaction costs of some direct transactions may already be less than the transaction costs of intermediated transactions. If, post-Internet, the transaction costs of direct transactions are still lower than the transaction costs of intermediated transactions, one might predict the appearance of an “NII Supplemented Direct Market” (e.g., Internet-supplemented direct merchandising by companies that traditionally have done business by catalogue sales).<sup>29</sup> If, however, post-Internet the transaction costs of some direct transactions remain greater than the transaction costs of intermediated transactions, then intermediation would continue to make sense, as long as intermediaries can reduce the costs of transacting below what they otherwise would be. And this is likely to be the case in many situations; as Leickly points out, technology can *increase* transaction costs under certain

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agents for commerce, not as watchdogs of consumer information and privacy. Thus, the benefit will come from the intermediary’s ability to reduce transaction costs by addressing the problems the information overload associated with the information economy.

Leickly, *supra* note 6, at 6.

26.

27. See Sarkar et al., *supra* note 8, at 6.

28. See *id.*:

The current best example of this is Walmart, a firm which uses an information infrastructure to drastically reduce the producer-intermediary transaction costs and leverage the distribution and real-estate that is required for distribution to individual consumers. Scenario 4 may also arise when the network permits existing intermediaries to create economies of scale, scope, and knowledge that arise for supporting information or risk management services. Examples here include credit card companies who might use an NII to offer money-back guarantees for purchases made over the network.

29. See *id.*

conditions.<sup>30</sup> Problems can include information overload (e.g., consumers find it hard to differentiate between trustworthy or opportunistic businesses); the exacerbation of information asymmetry;<sup>31</sup> consumer weariness of technical malfunctions, failures, hackers, and increased risk; vertical disintegration leading to outsourcing of unessential activities; and so on.<sup>32</sup> New roles for intermediaries therefore might include sorting, routing, filtering, comparing prices, and vouching for worthiness of products and firms. Indeed, several commentators predicted the appearance of a new type of intermediary, referred to in the literature as the “cybermediary” (or “information intermediary” or “infomediary”), to fulfill these types of roles.<sup>33</sup>

I think it is fair to say that history thus far has borne out Sarkar and his co-authors critique of the threatened intermediary hypothesis. Although consumers rely much less frequently today on the services of some traditional intermediaries, such as travel agents, there are many other intermediaries (such as eBay and Amazon) that didn't exist before the Internet.<sup>34</sup> This is not to say that the rosier predictions of the rise of infomediaries have been completely vindicated, either. For example, Leickly argues that some fledgling infomediaries such as Lumeria and AllAdvantage failed for reasons not adequately taken into account in some analyses—most notably, because they served consumer interests to the exclusion of producer interests, and thus were unsustainable.<sup>35</sup> And in a more theoretical vein, Mark Patterson has noted some of the difficulties of sustaining a competitive market for infomediaries, among them that information is sometimes a credence good,

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31. Online, it is much harder to ensure product quality, or verify the reputation of a business. Information can be counterfeited, forged, or misrepresented, and thus “lemon” markets may ensue

32. See Leickly, *supra* note 6, at 49-59.

33. See Sarkar et al., *supra* note 8, at 6-7 (discussing cybermediaries); see also JOHN HAGEL III AND MARC SINGER, NET WORTH: SHAPING MARKETS WHEN CUSTOMERS MAKE THE RULES 28-29(1999) (predicting the rise of infomediaries); Bailey & Bakos, *supra* note 22, at 8, 19-20; Alina N. Chircu & Robert J. Kauffman, *Digital Intermediation in Electronic Commerce—The eBay Model*, in E-COMMERCE AND V-BUSINESS: BUSINESS MODELS FOR GLOBAL SUCCESS 45, 51-56 (Stuart Barnes & Brian Hunt eds. 2001); Scott, *supra* note 25, at 3.

34. See Chircu & Kauffman, *supra* note 30, at 51; Leickly, *supra* note 6, at 77-83; Sarkar et al., *supra* note 8, at 10-12; Scott, *supra* note 25, at 3-6, 10-12. P2P platforms may facilitate the formation of yet other infomediaries. See Zary Segall et al., *Multishelf: An Experiment in Peer-to-Peer Infomediation*, Proceedings 2002 International Conference on Peer-to-Peer Computing (P2P2002), Linköping, Sweden, available at <http://www.comp.lancs.ac.uk/~kortuem/publications/p2p2002.pdf>.

35. See Leickly, *supra* note 6, at 74-75; see also Bailey & Bakos, *supra* note 22, at 19; Patterson, *supra* note 10, at 14.

and that reputational constraints on infomediaries may be weak.<sup>36</sup> The import of Patterson's analysis is that infomediaries whose purpose is to reduce, say, consumers' costs of evaluating or comparing products may not have a sufficient incentive to provide the truthful information that consumers need to make intelligent evaluations and comparisons.<sup>37</sup> Nevertheless, the persistence of some traditional intermediaries, as well as the creation of new intermediaries, in the digital age suggests that a more productive task might be to predict *which* intermediaries are likely to vanish and which to flourish, and to suggest some ways in which law can either assist or hinder the market in achieving efficiency gains. In the following part, I suggest some ways of approaching this latter task of formulating legal responses. The discussion is illustrative only, however, and is not intended to be an exhaustive treatment of the topic.

## II. SOME POSSIBLE LEGAL RESPONSES

The preceding part culled the existing literature on intermediaries to arrive at three basic propositions: (1) that intermediaries traditionally have served a function of reducing the costs of buyer-seller transactions; (2) that the digital revolution renders some intermediaries superfluous, by reducing the costs of nonintermediated buyer-seller transactions; and (3) that the digital revolution also increases some transaction costs, and thus creates opportunities for new intermediaries to arise and assist in transaction-cost reduction. The question then arises what, if anything, the law can do to facilitate or enable the transaction-cost reduction promised by (2) and made necessary by (3). Put another way, can the law facilitate the reduction of transaction costs, either by enabling private actors to develop transaction-cost minimizing approaches on their own, or by directly intervening to reduce those costs when appropriate?

The answer to this question is not easy to formulate in the abstract. As we have seen, the intermediaries that best reduce transaction costs overall might be those that achieve some optimal balancing of consumer and producer

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37. See Patterson, *supra* note 10, at 15. As Patterson notes, a credence good is one "whose value the consumer will have difficulty evaluating even after consuming it." *Id.* at 5 n.19. Patterson points out that for some "sources of information, which do not offer facts but instead offer, say, search results or product evaluations, the value of the information is uncertain even after it is consumed." *Id.* In the absence of reputational constraints or appropriate private or public countermeasures, this phenomenon could result in a "lemon" market in which bad information drives out good. See George Akerlof, *The Market for "Lemons": Quality Uncertainty and the Market Mechanism*, 84 Q.J. ECON. 488 (1970); see also Leickly, *supra* note 6, at 15-16, 24.

needs, because these are the most likely to succeed in the marketplace.<sup>38</sup> Governmental measures to directly reduce transaction costs (for example, by reducing the sort of information asymmetry that can give rise to lemon markets) may be necessary in some circumstances. But they also can give rise to unanticipated consequences, by undermining incentives to produce or to compete effectively (more on this below). Stated differently, at the very least government needs to enforce contracts, deter fraud, and promote competition; but what this means (or should mean) in a given context is not always clear. Policymakers also need to consider which institutions will best oversee intermediaries, in light of the institutions' own abilities to process information and avoid capture: these institutions may include markets, government, private actors, and entities formed by private actors. I will use two examples below to illustrate some of the aforementioned difficulties, one from the law of copyright, the other relating to the law of unfair competition.

#### A. Copyright

The conventional wisdom is that copyright is a tool for encouraging creators to create and publishers to publish; and that, in the absence of copyright or some other corrective mechanism, the supply of creative expression would be less than some posited optimum, due to the potential for free riders to take advantage of others' creative efforts without having invested in production themselves.<sup>39</sup> In recent years, however, skeptics such as Raymond Ku have argued that maybe this conventional wisdom doesn't hold true in the digital realm.<sup>40</sup> Ku points out that, as an empirical matter, the people who compose and perform musical works often derive little direct financial gain from the copyright system, as it now exists; and he speculates that they might just as easily finance their creative activities by alternative means, such as touring and merchandise.<sup>41</sup> Sound recording producers, on the other hand, may have performed a necessary production-and-publication function at one time. But that is not the case any longer, because musicians can finance the production of their own recordings at relatively low cost, and consumers can finance the publication of these recordings through Internet

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38. See *supra* text accompanying notes 19-22, 32.

39. See, e.g., Cotter, *supra* note 3, at \_\_\_. More technically, if creative works are priced at marginal cost, but marginal cost is below average cost (which is likely), then publishers will be unable to break even. See Christopher S. Yoo, *Copyright and Product Differentiation*, 79 NYU L. REV. 212, 226-29 (2004).

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41. See Raymond Shih Ray Ku, *The Creative Destruction of Copyright: Napster and the New Economics of Digital Technology*, 69 U. CHI. L. REV. 263, 306-11 (2002).

file-sharing, simply by purchasing computer hardware and software.<sup>42</sup> Hence, on Ku's reasoning, copyright as we have traditionally known it is no longer necessary to induce either the creation or the publication of one form of creative content, music.<sup>43</sup>

I'm not sure I agree with this, even with respect to music. For one thing, Ku's reasoning may underestimate the value that producers add in terms of production, editing, and the like. And it's hard to see how Ku's assumption of continued creativity could be true with respect to cost-intensive works such as movies, even if it is true with respect to music and other relatively low-cost works.<sup>44</sup> But let's assume that Ku is right, and that copyright is unnecessary to ensure the creation or publication of (at least some genres of) content. Even so, there would still be a need for filters (evaluators, gatekeepers) to channel people's attention to the content they want—a point made by the philosopher Daniel Dennett in the 1990s,<sup>45</sup> and restated by Yochai Benkler as the “Babel objection.”<sup>46</sup> So perhaps copyright performs a hitherto underappreciated service of enabling publishers to channel consumers' attention to the subset of all possible works that consumers may be interested in consuming. Put another way, perhaps the need for sound recording producers and other publishers to finance publication is gone, but the need for someone to filter that which has been published remains. In the case of music, copyright enables sound recording producers to perform this necessary filtering function.

The obvious question, however, is whether sound recording producers, backed up by copyright law, best serve this filtering function—or whether other intermediaries could do as good or better, at lower cost (in which case, on Ku's reasoning, we could dispense with traditional copyright protections altogether). Benkler and Ku contend that, in the absence of copyright owners serving as gatekeepers, consumers would find other ways to locate the content they want.<sup>47</sup> Consumers could rely on critics, for example, or on recommendations from peers, as with such newly developed services such as MusicMatch and Yahoo's LaunchCast.<sup>48</sup> And maybe these alternative

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42. *See id.* at 301-05.

43. *See id.* at 305-22.

44. A point Ku himself acknowledges. *See id.* at 305; *see also* WILLIAM W. FISHER III, PROMISES TO KEEP: TECHNOLOGY, LAW, AND THE FUTURE OF ENTERTAINMENT 35 (2004).

45. *See* DANIEL C. DENNETT, DARWIN'S DANGEROUS IDEA: EVOLUTION AND THE MEANINGS OF LIFE 350-51(1995).

46. *See* Yochai Benkler, *Siren Songs and Amish Children: Autonomy, Information, and Law*, 76 NYU L. REV. 23, 105-06 (2001).

47. *See* Benkler, *supra* note 41, at 106-09; Ku, *supra* note 36, at 314-15.

48. *See The Music Match Discovery Engine*, [http://musicmatch.com/download/music\\_discovery\\_intro.htm](http://musicmatch.com/download/music_discovery_intro.htm); *LAUNCHcast Help*, <http://help.yahoo.com/help/us/launch/cast/cast->

gatekeepers would do a better job at matching consumers with content than does today's recording and publishing industry. To be sure, if members of the industry do not satisfy consumer tastes, a competitive market will penalize them. But, copyright critics argue, there are a variety of reasons to question whether the copyright system as it currently exists adequately satisfies consumer preferences for diverse fare, including (1) the difficulty of determining whether tastes are satisfied, when tastes themselves are in part a function of consumers' previous exposure to similar content;<sup>49</sup> (2) the cost advantages that copyright confers upon the owners of large copyright portfolios, which can be used to create a stream of derivative works against which smaller competitors may have difficulty competing;<sup>50</sup> and (3) so-called "solidarity effects," which may put smaller producers at a further disadvantage when they compete against the owners of blockbusters.<sup>51</sup> And there may be other unintended negative consequences of strong copyright protection (e.g., it enables content owners/intermediaries to leverage control of content to control of distribution technology and of follow-up improvements).<sup>52</sup> Furthermore, intermediaries themselves may collude; antitrust may not always detect collusion. On these grounds, critics might assert, there is a strong theoretical case for allowing the market to delegate the channeling function to some other intermediary, *if* it is feasible to do so without impinging upon the incentive to create and publish.

Of course, that's a big "if." But there probably is no good reason to delegate the gatekeeping function to publishers and producers, *unless* this delegation is a necessary byproduct of copyright, and copyright itself remains necessary to ensure creation and publication. Unfortunately, we don't really know whether this is true, even with respect to music, and intuitively it seems even less likely with respect to some other art forms (which is not to say, however, that copyright needs to be quite as strong, in terms of scope and duration, as it currently is, in order to achieve its positive effects). Still, the analysis is useful in that it explicitly separates out the channeling function

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37.html.

49. See C. Edwin Baker, *Giving the Audience What It Wants*, 58 OHIO ST. L.J. 311, 320-21 (1997).

50. See Yochai Benkler, *Intellectual Property and the Organization of Information Production*, 22 INT'L REV. L. & ECON. 81, 95-98(2002); Yochai Benkler, *Free as the Air to Common Use: First Amendment Constraints on Enclosure of the Public Domain*, 74 NYU L. REV. 354, 407 (1999).

51. See Mark S. Nadel, *How Current Copyright Law Discourages Creative Output: The Overlooked Impact of Marketing*, 19 BERKELEY TECH. L.J. 785, 800-02 (2004); Guy Pessach, *Copyright Law as a Silencing Restriction on Noninfringing Materials: Unveiling the Scope of Copyright's Diversity Externalities*, 76 S. CAL. L. REV. 1067, 1077-84 (2003).

52. For discussion of relevant sources, see Cotter, *supra* note 3, at \_\_\_.

from the other functions served by copyright, and thus invites consideration of alternative ways of fulfilling that function. Perhaps the law can move us toward a more efficient channeling system, if adequate creation and publication incentives can be preserved in other ways.<sup>53</sup>

## B. Truth in Advertising

Another problem, however, to which alternative channeling mechanisms might give rise relates to the reliability of critical opinion itself. If one is to rely upon critics and peers as evaluators, then critics and peers must have an incentive to give their honest opinions and to identify themselves in some fashion. If, on the other hand, opinion can be bought, or the identity of reviewers are hidden from view, then critical opinion risks becoming debased and hence unreliable. Hence there might still be a role for trademark law, false advertising law, laws against fraud, and consumer protection laws to safeguard the integrity of whatever alternative system is put in place. (For example, consumers need to be sure that someone who is providing an opinion really is who he or she purports to be, and is not falsely attributing the opinion to some other, more credible source.<sup>54</sup>) More generally, if Patterson is correct in classifying information as a credence good, then infomediaries that provide search results or product evaluations (for example) may sometimes have an incentive to provide biased information, and thus the law may need to step in with appropriate corrective measures.<sup>55</sup>

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53. For an interesting recent analysis of how recording “mentors” could, under some plausible scenarios, replace the “labels”—and possibly result in greater empowerment of recording artists—see Maija Halonen-Akatwijuka & Tobias Regner, *Digital Technology and the Allocation of Ownership in the Music Industry*, available at [http://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=603461](http://papers.ssrn.com/sol3/papers.cfm?abstract_id=603461).

54. Perhaps the above overstates the need for accountability, however. For one thing, the sheer number of peer recommendations and reviews may provide a sufficient diversity of viewpoints so that consumers are able to make reasonably informed decisions, even if the identity of specific reviewers, or their ties to a given supplier, are unknown. Alternatively, if the number of recommendations and reviews is small, perhaps consumers will take this fact into account in deciding how much weight to accord them.

55. See Patterson, *supra* note 10, at 5-6:

Consider search engines or price-comparison sites, for example. When a user seeks a web site with information about, say, eyeglass prices, the user might want to find a seller that offers low prices. The user probably does not, however, have a good sense of low and high price levels. Therefore, the user will find it difficult to judge whether a search engine has provided a link to a site that meets his or her needs. It might be the case instead the search engine’s selection criteria have been exploited by high-eyeglass-price sites, or even that the search engine has sold such sites prominent placements in its search results.

There are reasons, however, to be cautious in jumping to the conclusion that an expansion or further tweaking of unfair competition or consumer protection laws is necessary or desirable to fix these potential problems. To cite one example, critics of false advertising law have argued that the overly aggressive enforcement of false advertising laws can be socially wasteful or even anticompetitive, particularly in light of the other methods consumers have at their disposal to protect themselves.<sup>56</sup> (These “other methods” might include actions for breach of contract, breach of warranty, and fraud,<sup>57</sup> as well as public enforcement actions by governmental agencies such as the Federal Trade Commission (FTC),<sup>58</sup> as well as a variety of self-help measures<sup>59</sup> and

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In theory, even if some buyers are not able to evaluate the information they receive, the information provider’s need to serve other buyers, better informed, may cause it provide high-quality information. This possibility is not as likely to constrain intermediaries like search engines, though, because many of their users are uninformed; informed users are less likely to need a search engine. Other information providers could also, again theoretically, provide information about low-quality information, but if the principal sources of profits for search engines are advertising and payments for placement, other search engines are not likely to have the incentive to provide such information.

In some instances, there are information intermediaries *for* information intermediaries. . . . One might think that these intermediaries could solve this problem by directing users to those search engines that best provide useful, objective information. In fact, though, these intermediaries may not cater so much to users as to the information intermediaries about which they provide information. . . .

*See also id.* at 14 (discussing possible intersection of the law of false advertising, on the one hand, and certification and screening intermediaries, on the other).

56. *See* Lillian R. BeVier, *Competitor Suits for False Advertising Under Section 43(a) of the Lanham Act: A Puzzle in the Law of Deception*, 78 VA. L. REV. 1 (1992); Ellen R. Jordan & Paul H. Rubin, *An Economic Analysis of the Law of False Advertising*, 8 J. LEG. STUD. 527 (1979). Analogous problems might result from overly aggressive antitrust enforcement, but I will not address that topic here.

57. A justification for false advertising law would be that these more conventional claims are likely to be underenforced, and therefore may not provide the optimal amount of deterrence, because a consumer who is defrauded of only a small amount of money may not find it worthwhile to file suit. A variety of legal reforms other than false advertising law, however, could in theory come to the assistance of the aggrieved consumer. These reforms might include greater use of small-claims courts, the wider availability of punitive damages and awards of attorney fees, and greater use of class actions. Of course, all of these reforms have their potential downsides too. *See* Jordan & Rubin, *supra* note 51, at 542-44.

58. The FTC has jurisdiction to investigate and file suit against persons who engage in deceptive trade practices, *see, e.g.*, *FTC v. Gill*, 265 F.3d 944, 950 (9th Cir. 2001); and many states have enacted statutes authorizing public agencies, or consumers or other parties, to litigate these types of claims too, *see, e.g.*, *Guyana Tel. & Tel. Corp. v. Melbourne Int’l Comms. Ltd.*, 329 F.3d 1241, 1246-47 (11th Cir. 2003) (discussing application of the Florida Deceptive and Unfair Trade Practices Act).

59. Self-help may occur either *ex ante* (e.g., sampling a product before buying it) or *ex*

reliance upon the protections afforded by trademark law.<sup>60</sup>) One problem is that, to the extent the content (and not merely the existence) of advertising conveys information to consumers, it may convey a variety of messages.<sup>61</sup> Because different consumers may derive different meanings from the same ad (or even the same consumer may derive different meanings at different times), difficult factual questions necessarily arise concerning *how* consumers interpret a given ad. Difficult policy issues also arise, concerning whether the law should focus exclusively upon majority perceptions only, or also the perceptions of substantial pluralities.<sup>62</sup> The less robust the showing of actual or potential deception must be, the more costly the system is to administer—and the greater is the potential for other negative consequences, including both socially inefficient self-censorship<sup>63</sup> and the creation of barriers

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*post* (e.g., resolving never again to buy a particular brand that has proven disappointing, *see infra* note 55). It also may be implicated in one's reaction to advertising. For example, consumers may discount the content of much advertising, recognizing that producers often engage in "puffery" or state unverifiable opinions. Moreover, much of the content of advertising has little to do *directly* with the inherent quality of the product advertised. The fact that Tiger Woods endorses Wheaties doesn't really tell you much about Wheaties, *except* that the company that makes Wheaties must sell enough of the product to fund an expensive advertising campaign. But this may be an important fact in and of itself. Consumers may have a rational interest in knowing which products are the most popular, to the extent this knowledge enables them to conserve search costs. Also, intensive advertising may signal that a firm expects to remain in the marketplace for a long time (it will need to do so to recoup the cost of its advertising), and it can expect to remain in the marketplace a long time only if it expects people to continue buying its product. Seen in this light, much advertising is relevant not for what it actually says, but rather for what its mere existence signals to the consumer. *See* BeVier, *supra* note 51, at 8-13; Benjamin Klein & Keith B. Leffler, *The Role of Market Forces in assuring Contractual Performance*, 89 J. POL. ECON. 615, 629-33 (1981); Phillip Nelson, *Advertising as Information*, 82 J. POL. ECON. 729, 740-43 (1974); Phillip Nelson, *The Economic Consequences of Advertising*, 48 J. BUS. 213, 214-15 (1975).

60. In other words, even though consumers do not have standing to litigate trademark infringement actions on behalf of trademark owners, consumers benefit from trademark owners' own actions to protect and police the use of their marks. Consumers can usually be confident that a good bearing a trademark is genuine, and if they do not like the way the good performs they can retaliate by not purchasing that particular brand again.

61. *See* BeVier, *supra* note 51, at 31-36.

62. To prevail on a false advertising suit under § 43(a) of the Lanham Act, for example, a plaintiff must prove, *inter alia*, that the defendant has made a false or misleading statement of fact about the defendant's own goods, services, or commercial activities; that the statement deceives or has a tendency to deceive a substantial portion (not necessarily a majority) of its intended audience; and that the plaintiff has been or is likely to be injured as a result. *See, e.g., Am. Italian Pasta Co. v. New World Pasta Co.*, 371 F.3d 387, 390 (8th Cir. 2004).

63. Although some falsity is clearly intentional, or the product of reckless behavior, not all of it is. Some falsity may simply be the expected byproduct of providing information without having sufficient time to verify all of it. Thus, while there may be no value in false information,

to entry, with incumbent firms using the threat of potential legal sanctions (and fees) as a sword to deter aggressive competition on the part of newcomers.<sup>64</sup> Critics also contend that many of these suits dissipate judicial resources on disputes that often are of relatively little social importance.<sup>65</sup> The potential for analogous problems to arise in the context of intermediary regulation are worth considering, before any particular solution is adopted.

That said, one needs to be critical in evaluating the critics too. Some of the aforementioned critiques may apply with much less force in cyberspace. It may well be that if consumers can sample a good extensively before the point of purchase, they have less need to rely upon trademarks *or* any other representations of quality, and so false advertising law is largely a waste; but these sampling options may not be available in many of the situations that infomediaries serve. Indeed, one of the purposes served by infomediaries is to reduce consumers' need to compare and sample products in the real world prior to the point of purchase. The specific representations (and not merely the fact of advertising) made may be highly relevant too. And if Patterson is correct in asserting that competition among providers would not suffice to drive the unscrupulous from the market, or that the market for infomediary services will tend to monopolization due to the presence of high fixed costs and low marginal costs,<sup>66</sup> competition may not provide sufficient deterrence against the purveyors of false statements. None of these observations necessarily suggests a greater role for unfair competition law or other government oversight, but they do counsel in favor of nuanced, fact-intensive consideration of these options. If the market is not an adequate force in favor of infomediary accountability, a governmental response (one that is, at the

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if the standard of liability is too strict producers may provide not only less false information but also less truthful information. *See* BeVier, *supra* note 51, at 30-42; Jordan & Rubin, *supra* note 51, at 540, 552; *see also* Nike, Inc. v. Kasky, 539 U.S. 654, 676-82 (2003) (Breyer, J., dissenting from dismissal of writ of certiorari as improvidently granted) (questioning whether false advertising should receive no First Amendment scrutiny at all). Similarly, the ease or burden of proving the elements of the tort will also affect how many cases are brought and how many succeed. Contemporary law under the Lanham Act departs from the common law in no longer requiring the plaintiff to prove that it *actually has been harmed* by the defendant's false statement; instead, it is sufficient to prove a likelihood of (future) harm, as in trademark infringement cases. *See* Johnson & Johnson v. Carter-Wallace, Inc., 631 F.2d 186, 189 (2d Cir. 1980). Moreover, depending on the facts, some courts are willing to presume some of the other elements of the tort, such as materiality and deception. *See* Johnson & Johnson Vision Care, Inc. v. Ciba Vision Corp., 348 F. Supp. 2d 165, 178, 179 (S.D.N.Y. 2004).

64. *See* BeVier, *supra* note 51, at 42-47; Jordan & Rubin, *supra* note 51, at 548-49, 551.

65. *See* BeVier, *supra* note 51, at 2-3, 48; Jordan & Rubin, *supra* note 51, at 548.

66. *See* Patterson, *supra* note 10, at 3-4.

same time, sensitive to government's limitations too)<sup>67</sup> may be the only practical choice.

#### CONCLUSION

Intermediaries are not dead, at least not all of them. Some old-economy intermediaries have adapted, and some new-economy intermediaries have entered the market to peddle their services. To the extent that government can clear the way for the elimination of unnecessary intermediaries, and for the remaining intermediaries to better serve consumers through the reduction of transaction costs, it should do so. But this may be easier said than done. Sharply reducing the scope of copyright law, or sharply increasing the scope of unfair competition and consumer protection laws, are two possibilities I have briefly considered above; but the jury is still out on the merits of these proposals. Even if these measures were politically feasible, it is not clear whether they would be desirable, or whether policymakers could efficiently calibrate the law so as to avoid the unintended consequences of stifling competition and undermining creative incentives. Developing the optimal response is a daunting task indeed—and one that should be continually revised in the light of further experience. But the specific ways in which technology develops may be too complex for any one person to predict, and in this sense law may always be involved in a game of catch-up. Unfortunately, matching solutions with desired policy preferences and outcomes is a feat that no intermediary to date, academic or otherwise, is likely capable of doing with perfect accuracy.

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67. Given the difficulties that regulators face in responding quickly and effectively to changing technology, and given the potential for regulatory responses to be captured by special interests, it may be the case that self-help measures will become the principal vehicle for inducing honesty. See, e.g., Paul Markillie, *Crowned at Last*, THE ECONOMIST, *supra* note 2, at 5 (noting Microsoft's hiring of its "own celebrity blogger, Robert Scoble, even at the risk that he might be scathing about the company's products," and describing this as "a clever move," because "[t]he less control a company has over its marketing message, the greater its credibility"); see also Joshua Goodman et al., *Stopping Spam*, SCI. AM. (Apr. 2005), at 42 (discussing a combination of technological measures which, the authors predict, in the coming years will reduce the flow of junk e-mail—a phenomenon that the law has found virtually impossible to halt, despite numerous legislative efforts).