



MADLINE MCINTOSH
SENIOR VICE PRESIDENT & PUBLISHER
RANDOM HOUSE AUDIO GROUP

February 21, 2008

Dear Publishing Partner,

Last fall, Random House Audio launched a test of DRM-free distribution with eMusic.com. Based on the successful results of that test, and on the similar results from recent tests in the music industry, we are now comfortable broadening this type of distribution. **Beginning March 1st, we will no longer require that our retail partners use DRM when selling audiobooks via digital download.** We believe that this move will allow for healthy competition among retailers targeting the iPod consumer, without posing any substantive increase in risk of piracy. **At the same time, this is not an all-or-nothing proposition: we will still have the ability to maintain DRM restrictions for those authors who still feel it is necessary.**

Testing DRM-free Sales

Since our decision has been based in part on our experience with eMusic, I would like to share those results with you. eMusic started selling audiobooks mid-September, and their program has been a success, with strong sales every month since launch. Since they sell content only in the MP3 format (in other words, without DRM), our goal was to find out if allowing them to sell our content would lead to any increase in illegal filesharing. For tracking purposes, we watermarked all of the eMusic files and then hired a piracy watchdog service to monitor and report back to us if any of our titles appeared on the major filesharing networks. We tracked a mix of popular titles, including some that were not available through eMusic. Because piracy is already a fact of life in the digital world, what we were interested in finding out was not *whether* piracy exists, but rather whether there is any correlation between DRM-free distribution and an *increased* incidence of piracy.

The results: we have not yet found a single instance of the eMusic watermarked titles being distributed illegally. We did find many copies of audiobook files available for free, but they did not originate from the eMusic test, but rather from copied CDs or from files whose DRM was hacked. **It is worth noting that these results are entirely consistent with what the music industry has found in the last six months.** After conducting their own tests with Amazon, Walmart.com and others, the major labels have reached the conclusion that MP3 distribution does not in itself lead to increased piracy, they are now moving their entire catalogs to this approach.

MP3 Distribution Approach

Because of these results, and because we believe that the future health of the audiobook category will depend on allowing a competitive retail marketplace, we will now allow our retail partners to sell in the MP3 format (in other words, without DRM). **This means that we will be able to sell not only through existing partners such as iTunes, Audible and Amazon, but we will also be able to foster new audio sales through any of our CD retailers who have web sites, and through emerging partners such as eMusic.**

Moving to MP3 distribution does not mean that we will be any less vigilant in guarding the security of our content. On the contrary, we are setting in place a stringent set of operational and technological requirements that any retailer must meet and be able to sustain before we will consider selling through them. If at any point we do not like the direction our download business is taking, we can move to take down our MP3-formatted files.

Furthermore, as an everyday part of our business operation, we will continue to monitor the filesharing sites and move on a daily basis to have any illegal files removed.

Impact on Individual Authors

While the growth of the download market may cause anxiety, please keep in mind that our digital royalty structure insures that **author earnings will rise as sales shift from CD to download**. As a reminder: our digital royalty is 15% of the digital list price; the CD rate is 10% of net receipts. This means that on an average 6-hour-long program, an author earns \$2.25 per download as compared to about \$1.50 per CD.

But despite that good news, and despite our own comfort as a publisher that MP3 distribution is the best way to proceed, I know from our conversations with some of you over the past year that there is a range of opinion regarding this issue. In deference to the concerns that you and your authors may have, I want to emphasize several points:

- We would never want to distribute your authors' content in a way that causes any discomfort. As a result, we will continue to take a moderate approach to rolling back DRM from individual titles. **We have the ability to keep DRM in place for those authors who do not yet feel comfortable selling without it. If an author is willing to forego the potential for increased sales through DRM-free retailers, we will be able to support that option.**
- **We are not making any changes at all to our library digital download program.** That marketplace operates under very different conditions than retail. In the library environment, DRM is used not just to prevent copying, but also to control the limited borrowing privileges attached to the digital library edition. **To be clear: all titles distributed in download form from our Books on Tape and Listening Library lists through our two existing library distribution partners, OverDrive and NetLibrary, will continue to have DRM.**

Moving Forward

PLEASE NOTE: Our expectation is that you will contact us if you wish to have your titles withheld from MP3 distribution. We have the ability to test individual titles for you and then retract them at a later date if you feel it is necessary. We will be as flexible as possible.

For Random House, allowing sales via MP3 is part of an aggressive digital growth strategy that also encompasses our significant investment in a state-of-the-art audio archiving and distribution system and sales personnel dedicated to the digital channel. I look forward to continuing the conversations we have been engaged in, not only about protecting ourselves from piracy, but even more about the ways we can work together to ensure the future health of our category and of your authors' royalties for years to come.

I can be reached at any time, as can Editorial Director Amy Metsch (ametsch@randomhouse.com).

All the best,



Madeline McIntosh
mmcintosh@randomhouse.com
212-782-9497