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The Groucho Marx Theorem

An Application to Europe's Collecting Societies

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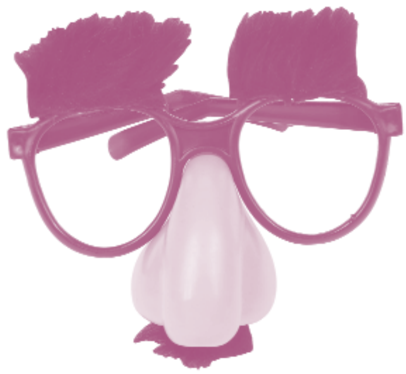
'I don't want to belong to any club that will accept me as a member,' remarked one Julius Henry 'Groucho' Marx (1890 -1977). That same astute self-observation was used to powerful and persuasive effect by Professor Andrew Hughes Hallett in a series of influential economic papers which helped Europe's policy makers understand what it will take to make a Monetary Union work. Here, Will Page - one of the Professor's former students - explains how the theorem can be applied to the dilemma facing Europe's network of collecting society's today.



According to Professor Hughes Hallett's 'Groucho Marx Theorem', no country would - in its own interests - ever want to join a union of other countries who were less reformed than it was. By the same token, any union of countries would want to try to persuade a more flexible or more reformed country to join their union instead.

The reasoning is straight forward enough. The most market flexible country will end up doing the lion's share of adjusting every time there is a shock; suffering the first and strongest upward adjustment of prices in inflationary times, and the bulk of the downturn and unemployment in recessionary times, on behalf of the rest of the union as well as itself. It gets ripped off, in other words, by the ability of the rest of the union to free ride on the flexible economy which, by definition, cannot prevent its market from adjusting first and by most.

Nice theory - but is there any evidence to support it? Well, the key driver in the formation of the Euro zone was the fact that countries wanted to join a club primarily to secure lower (German) inflation that they could not generate themselves. Given that higher inflation countries would join the club, Germany would not be able to prevent their higher inflation (and hence Germany's import prices) having an effect on her economy and her inflation. So why would Germany ever want to join such a club? And if Germany were not to join, why would the second lowest inflation country ever want to join? And so on... Meanwhile the higher inflation countries would always want to join, in order to free ride to lower inflation again.

Of course, Germany did eventually join the Euro in order to take advantage of the political capital of membership, such as the location and governance of the European Central Bank, but that's a different story and certainly does not remove the Groucho Marx effect.

Professor Hughes Hallett essentially highlighted the problem of 'asymmetric incentives' (when two parties share the same task but have opposing goals) when 'free riding' (when one party benefits from a collective activity without participating in it) is possible. So, can we apply the theorem to achieve a similar understanding about what to do with Europe's twenty-seven collecting societies?

Let's apply these two economic concepts to the CISAC club of collecting societies.
Firstly 'free riders' could be those societies whose primary job is to collect another society's money. Their existence - and market insulation via a monopoly status - is technically justified by free riding off the

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Professor Hughes Hallett

economies of scale generated by someone else's repertoire. Point being (had they not been members of the club) that repertoire would not have been theirs to collect. Secondly, 'asymmetric incentives' can occur when a society pays out more into the network than it collects in - or runs a deficit trade balance - as it might have an incentive to apply protectionist trade practices. Put simply, if you're in the business of collecting your own members' royalties, then you behave one way; whereas if the majority of your business is collecting other peoples' money, you behave another way. That's the problem of asymmetric incentives when free riding is possible.

These two economic concepts can help us apply the Groucho Marx theorem to collective rights management. Consider the formation of a completely new 'club' of collecting societies who seek to pool expertise and exploit economies of scale for the purpose of online collective rights management. The question facing potential members of this club is, 'would they want to join the network?', whereas the question facing existing members is 'would they want these potential members to join?' Should this 'more efficient' club threaten the incumbent model, then Groucho's theorem could be turned on its head by observing that any union of societies would want to try and persuade a more efficient society to rejoin their old network.

This observation helps explain the conflicting and contradictory views currently being expressed by some (less efficient) societies, to the Alliance's own online initiative of Alliance Digital and CELAS, along with its continued support for Option Three. For those societies who have been openly critical of these developments, Groucho would have viewed this as a club they would have benefited from had they been allowed to join. From a publisher's perspective, their frustration with the incumbent model and motivation for a new model can also be captured by Groucho when he went onto say: 'Please accept my resignation. I don't care to belong to any club that will have me as a member'.

What else can we learn from Groucho's Theorem and the Professor? Well, going back to how economists created the conditions for a European Monetary Union to work - integration was treated as a 'given', but the Maastricht Criteria enforced tough fiscal rules - or incentives - upon those who wished to join the 'euro club'. Similarly, if we treated the integration (or consolidation) of Europe's twenty-seven societies as a 'given', then a similar set of membership rules could be applied to commission rates, transparency and timeliness of distributions. Rules, when designed properly, can have the desired effect of restoring symmetrical incentives and eliminating the free rider problem.

But, what if societies continued to ignore the economics behind Groucho's Theorem? How might a continuation of the old marriage of twenty-seven institutions, draped in asymmetric incentives and free rider problems, progress into a digital age? This might offer stability in the short term - but paves the way for a more uncertain future of collective rights management as the interests of the society become increasingly asymmetric to those of the publisher and writer, or, as Groucho concluded: 'Marriage is a wonderful institution, but who wants to live in an institution?'