

WINNING THE DIGITAL RACE

Hughes Hubbard & Reed LLP partner Daniel Schnapp and associate Matthew Syrkin examine the current trends and challenges in Latin America's expanding digital media sector

Between 2000 and 2007, the number of internet users in Latin America grew from 18.1 million to an astounding 122.4 million, growing at an annual rate of 32 per cent compared to a mere 12 per cent in the US.

The internet frenzy is catching up with Latin America at a daunting pace. While internet penetration in the region grew modestly during the 1990s, hindered by the lack of infrastructure and high prices for telecoms services, today's numbers for Latin America evidence a different trend. According to comScore, a provider of global internet information, the average Latin American internet user spends 29 hours online per month, compared to a global average of 25 hours. A key driving force behind this figure is Brazil, which has one of the world's most intensive internet user populations, in excess of 42 million, a figure which is expected to more than double by 2011.

The region is in a race to modernise the sector as the world rushes to take advantage of escalating usage.

Typically, the Latin American end user is likely to fall into middle or upper socio-economic groups, and the demographics largely skew towards the younger population. In Venezuela, for instance, internet usage is concentrated among young, educated, male

city residents, with more than 60 per cent of the users coming from Caracas. Such highly defined demographics present prospective advertisers with an extraordinary opportunity for targeted advertising, and online ad spending in the region is poised to grow far more rapidly than advertising on traditional media platforms. In fact, advertising expenditure in Latin America is expected to grow by 13.3 per cent this year to US\$29 billion – over three and a half times more than is estimated for the US ad market.

Despite the unparalleled growth of new media outlets and opportunity in Latin America, the region still faces significant challenges on the road to modernisation. For example, online payment penetration, such as online credit card usage, in Latin America is still extremely low, and the banking system is currently ill-equipped to process and clear large volumes of e-commerce transactions to keep pace with online consumer demand. This lack of confidence among core businesses and Latin American companies regarding the use of internet-based services, as well as the prevalence of deficient technology infrastructure and network readiness in many areas of the region, will remain an obstacle to Latin America's progress in a highly competitive digital global economy.

Emerging convergence in Latin America Such obstacles have not put off mainstream names in the digital media space from approaching. With a market of more than half a billion people and a highly active online community, Latin America has already caught the interest of companies such as Google and Microsoft. Just last year, Google cemented its presence in the region by establishing the headquarters of its Latin American operations in Buenos Aires, in addition to maintaining other offices in Mexico City, Belo Horizonte and São Paulo. Google is betting on Argentina for its expansion in Latin America, and expects its office there to become the third-largest headquarters for Google business development in the world. Indeed, many multinational corporations consider the Latin America market to be their number-one priority and are moving their operations to the region to benefit from the impending boom.

The global trend towards convergence – the use of a single network for the full range of technological services – is reflected in recent M&A activity in the region, which grew to an all time high of US\$107 billion in 2007. Just recently Telemar Participações, owner of Brazil's largest telephone company, agreed to buy the parent of Brasil Telecom Participações for US\$3.5 billion, creating a

carrier that controls almost two-thirds of the country's land lines, which will provide high-speed internet access and cable television to more than 10 million Brazilians.

An extension of the idea of convergence is the use of a single device for multiple services, a movement that is particularly suited for the Latin American market, where internet penetration and network readiness levels are still low, while mobile phone penetration is very high. America Móvil recently secured a much sought after exclusive distribution agreement with Apple to offer the iPhone in 12 Latin America countries. Mobile carriers in the region are engaging in a flurry of activity to capitalise on the increased penetration of mobile services in the region that is further sparking the move towards convergence.

Telefónica, for instance, recently announced a new mobile banking (m-banking) initiative in partnership with the Inter-American Development Bank, targeting the 175 million people in the Latin America region who have mobile phones, but do not currently have banking access. The project's principal aim is to improve financial access in Latin American markets by providing an m-banking solution to those groups that do not currently have access to banks or financial services.

Service providers are also now focusing on migrating to next-generation network infrastructure to keep pace with consumer demand for new media services, products and content. For example, HBO's Latin America Group recently partnered with video-on-demand (VOD) technology provider SeaChange International and digital video specialist Thomson to deploy an advanced content delivery platform using digital watermarking for enhanced security. This will make full-length feature films available in the VOD services of cable network operators throughout Latin America.

The legal challenges

Internet regulation in Latin America now addresses the same concerns and issues seen in North America and Europe. As internet penetration and usage increases in the region, novel legal questions regarding the interpretation and application of the doctrines of defamation, hate speech, copyright and privacy law have been pushed to the forefront. Multinationals seeking to expand their businesses in the digital media space in this region face conflicting laws, a

lack of uniformity in the application of the existing regulations and disparate national sensitivities from country to country.

This veritable legal minefield is perhaps best typified by the two-year internet privacy struggle between Google and Brazilian law enforcement officials over Google's website Orkut, a social networking service that allows users to exchange information and create personal web pages. While still relatively unknown in the US, Orkut is the most popular web destination for Brazilians,

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with more than half its 25 million monthly visitors in Brazil alone. In fact, Orkut far outstrips rivals Facebook and MySpace in the country in terms of popularity and activity and Brazilians account for 27 million of its 60 million members worldwide. In this case, officials in Brazil demanded that Google

deliver information regarding users suspected of posting offensive material on Orkut.

Beginning in 2006, federal prosecutors in São Paulo in charge of human rights, began flooding Google's Brazil office with subpoenas seeking personally identifying information of Orkut users accused of committing crimes online. Google maintained that since the Orkut data was stored exclusively on computer servers located within the US, the permitted use and disclosure of the data was subject solely to US law and the terms and conditions of its privacy policy.

Authorities in Brazil threatened Google with criminal and civil lawsuits if it did not comply with opening the restricted online photo albums of users under suspicion of paedophilia. After more than two years of legal wrangling, however, Google finally capitulated, handing over data stored by suspected criminals, including paedophiles, on Orkut to Brazilian authorities, ceding to pressure to lift its confidentiality duty to its users. In addition to delivering the requested information, Google negotiated a wide-ranging deal that requires the US company to systematically provide data regarding suspect Orkut users to Brazilian authorities.

Beyond privacy concerns, the lack of uniformity in the regulatory landscape in the region is often coupled with a level of enforcement that can be generally characterised as insufficient and inconsistent. Thus, one of the objectives of the US government in signing free trade agreements (FTAs) with several Latin American countries was to improve protections for US copyright and trademark holders against piracy and discriminatory or anti-competitive regulation in the region. As a result, the intellectual property provisions of these FTAs are substantially uniform with respect to each treaty and country, and introduce more acutely developed legal doctrines applicable to online conduct, such as secondary liability (both vicarious and contributory) for copyright infringement committed by third parties.

One of the many noteworthy sections included in the intellectual property sections of the FTAs are the provisions regarding anti-circumvention measures that prohibit tampering with technology used to protect copyrighted works and are based on the anti-circumvention provisions contained in the US Digital Millennium Copyright Act (DMCA). Relatively novel to the

region, these anti-circumvention provisions are of particular importance to businesses in the digital space seeking to distribute and syndicate their multimedia content in the Latin American market. As online streaming and download content offerings continue to grow in popularity, businesses will rely on legal protections that support the implementation of digital watermarking, fingerprinting and digital rights management (DRM) protections contained in their content designed to prevent unauthorised use, reproduction and distribution of the same.

The FTAs also offer safe harbours for internet service providers (ISPs) against liability for copyright infringement that occurs over their networks. These regulations are equally crucial to businesses operating in the online space, as they provide effective remedies for the removal of infringing content and procedures for assessing appropriate liability. At a time when social networking and user-generated content sites are attracting unprecedented numbers of end users, the FTAs will prevent signatory nations in the region from enacting inconsistent regulations regarding the display and distribution of copyrighted works by an ISP.

In practice, these regulations would prevent the type of situation that recently occurred in Brazil involving WordPress.com, a blog-based user-generated content service, where a Brazilian judge ordered ISPs to block one blog hosted at there. While the particular blog's name and the reason for the ban have not been disclosed, in order for this decision to be carried out, ISPs would need to block the entire WordPress.com domain, essentially shutting down business operations for WordPress in the country. Similarly, in January 2006, a Brazilian court ordered YouTube to close down its service in the country until it removed all video clips of a celebrity sex video featuring model and ex-wife of Brazilian soccer player Ronaldo. Despite YouTube's attempt to remove the video, it was continually reposted. In January 2007, a Brazilian judge ordered telecoms companies to entirely block access to YouTube until the particular video was removed from the website. Several ISPs, including Brasil Telecom, announced their intention to comply with the court ruling, but days later, the judge revoked his order and lifted the ban on the entire site.

The FTAs' regulations concerning the internet in particular will give overseas



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businesses the ability to more accurately assess the risk and liabilities associated with operating, for example, a user-generated content site and at the same time provide creators and distributors of content, such as movie and television studios, certain enforcement mechanisms and procedures for preventing the continued infringement of their content. On a policy level, the relevant provisions of the FTAs will help strike a balance between the protection of intellectual property in the digital space and the unimpeded proliferation and distribution of new technologies in the region. Indeed, as social networking and user-generated content sites become increasingly popular across the globe, issues relating to copyright protection, such as content filtering or removal by ISPs, will have a profound impact on the prospects for distribution of new media content in Latin America, which will in turn impact the investment in advertising and the viability of countries within the region as consumers of digital content.

Despite the ratification of several FTAs, the operative provisions relating to digital media and intellectual property protections have yet to be implemented, as both the necessary technological infrastructure and legal enforcement mechanisms in most of the region's developing countries are ill-equipped to adhere to the contours of the laws. As a result, the US brokered a compromise during the FTA negotiations whereby all of the participating countries would be afforded lengthy windows for implementation of the technology-related provisions of the FTAs. In some cases, these span more than three years from the date of ratification.

A strong intellectual property regime reassures potential investors that their capital and their technologies will not fall prey to piracy and counterfeiting. Especially when confronting a legal system deeply rooted in the civil law tradition, new purveyors of digital content in the Latin American market require established regulations governing the core of their business. Precedent-setting decisions in North American courts, and even Latin America itself, are insufficient to provide the level of comfort required to adequately assess the liabilities and risk facing multinationals conducting business in the digital media space in the region.

Moreover, as the commercialisation of the internet continues to evolve at a frenzied pace, businesses operating in the digital media space must continually innovate, develop and implement new technological offerings and platforms that account for rapid shifts in end user behaviour, interactivity and tendencies in order to maintain a competitive advantage. Doing so in a region such as Latin America, however, where the technology infrastructure and network penetration are less than robust and regulations and enforcement mechanisms are in a constant state of flux, presents substantial risks.

Indeed, the paramount challenge for multinationals delving into the digital media arena in Latin America is how to effectively mitigate the operational and legal risks associated with the implementation of their initiatives, while the safeguards and infrastructure necessary to conduct business in this area are put in place. One thing that is certain, however, is that Latin America is poised to attract the overwhelming support of multinational corporations in the digital media space, and will undoubtedly become the lucrative online market reflective of its population and potential.