

On the Edge

Napster's Lost Revolution

When 18-year-old Shawn "Napster" Fanning, then a freshman at Northeastern University, founded Napster, Inc. in 1999, he started a property revolution. In college, Fanning developed software and a website through which users could connect to each other and then download for free the copyrighted music they had to pay for in stores. Many students felt the music they downloaded belonged to everyone and that copying was okay because it did not affect the original. Two music industry groups sued Napster, however, claiming that through its website Napster was helping others steal their property and that if music property rights were not respected, musicians would have no incentive to produce music. On February 12, 2001, the courts ruled that Napster's website actively contributed to copyright infringement and in 2002, the company was forced to block users from downloading copyrighted music.

But Napster had paved the way for the development of decentralized peer-to-peer file-sharing software that let users connect to each other and download music files directly from each other; some entrepreneurs that have carried out this mission are Grokster, StreamCast, Freenet, Gnutella, eDonkey, Kazaa, Poisoned, Morpheus, BitTorrent, and LimeWire.

Several music companies sued Grokster and StreamCast. In 2004, a federal district court ruled that because Grokster and StreamCast programs let users connect directly to each other without going through their website, neither Grokster nor StreamCast could control what users did with their program. The music companies now turned to suing individual downloaders. One victim remarked, "It scares me. You have no power against these people."

Moreover, the music companies appealed the Grokster/StreamCast decision to the U.S. Supreme Court. On June 23, 2005, the Supreme Court ruled that both Grokster and StreamCast had created their peer-to-peer software with the "intent" of "inducing" consumers to download copyrighted materials and so violated the laws protecting copyrights. In 2007, StreamCast was ordered to distribute new software that blocked users from downloading copyrighted material. Nevertheless, people continued to download copyrighted materials by turning to other providers of peer-to-peer software such as BitTorrent, Gnutella, and LimeWire. But record companies sued LimeWire in 2006, and on May 12, 2010, a Manhattan District Court ruled LimeWire had committed copyright infringement and induced others to do so as well. BitTorrent, anxious to change its business model, announced on February 25, 2007, that it would sell legal video material on its website. But on November 7, 2008, BitTorrent fired half its employees, and said it would now concentrate on distributing video games. The company to this day (2016) continues to distribute its BitTorrent client software from its site at BitTorrent.com. PirateBay, a file-sharing website in Sweden, also continued to hold out, although on April 17, 2009, its founders were sentenced to prison for a year and fined \$3.6 million for assisting in illegal copying. Other members of

the PirateBay community, however, stepped in and continued to operate the site. In spite of being hassled by periodic police raids, thepiratebay.org is still operating today.

WRITING PROMPT

Musical Ethics

1. Even if what Napster, Grokster, StreamCast, LimeWire, and PirateBay did was illegal, was it unethical? Explain why or why not.
2. Should we treat digitized entertainment like online music, movies, or games in the way that Locke said property should be looked at, or like Aquinas said property should be looked at, or like the collectively owned property that many socialists advocate? How does the kind of free downloading that Napster, Grokster, StreamCast, LimeWire, and BitTorrent made possible fit with each of these three views on property?

The response entered here will appear in the performance dashboard and can be viewed by your instructor.

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3.6.3: The End of Marxism?

Defenders of free markets were greatly encouraged by what some called the complete abandonment of communism in several formerly communist nations, particularly the countries of the former Soviet Union. On September 24, 1990, the Soviet legislature voted to switch to a free market economy and to scrap 70 years of communist economics that had led to inefficiencies and consumer shortages. Then, during the summer of 1991, the Communist Party was outlawed after party leaders botched an attempt to take over the Soviet government. The Soviet Union broke up, and its reorganized states discarded their radical Marxist-Leninist ideologies in favor of worldviews that incorporated both socialist and capitalist elements. The new nations embarked on experimental attempts to integrate private property and free markets into their still heavily socialist economies. Some observers, Francis Fukuyama in particular, hailed these developments as indicating "the end of history."¹¹ What Fukuyama and others were suggesting is that, with the end of communism, there will be no more so-called progress toward a better or more perfect economic system: the whole world now agrees that the best system is capitalism.

Those historic communist reforms, however, did not signal the complete abandonment of Marxism or socialism. Without exception, all of these reforms have been aimed at moving communist systems toward economies that are based on the best features of both socialism and capitalism. They have, in short, been aimed at moving the communist countries toward the same kind of mixed economy system

that dominates Western nations. The debate today in the formerly communist world as in the United States is over the best mix of government regulation, private property rights, and free markets, and not over whether a pure market system is better or worse than a pure command system.

Followers of Smith and Locke continue to insist that the level of government intervention tolerated by the mixed economy does more harm than good. Their

opponents continue to counter that, in our mixed economy, government still favors business interests and that allowing businesses to operate without regulatory oversight worsens our economic problems. On balance, however, it may be that the mixed economy comes closest to combining the utilitarian benefits of free markets with the respect for human rights, justice, and caring that are the characteristic strengths of government regulation.

Web Resources

Readers interested in researching the topic of globalization can find on the web both introductory discussions of globalization (<http://www.globalization101.org>) and more in-depth discussions (<http://yaleglobal.yale.edu/globalization>); statistics and data on globalization are also available (<http://globalization.kof.ethz.ch>); the web also has materials on Locke (<http://www.libraries.psu.edu/tas/locke/>), Marx (<https://www.marxists.org>), Smith (<http://www.adamsmith.org> and <http://oll.libertyfund.org/pages/smith>), and Ricardo (<http://oll.libertyfund.org/pages/ricardo>)

SHARED WRITING

Contemporary Application

Consider this statement: "Locke's views on property, Smith's views on free markets, and Marx's views on capitalism obviously do not hold true when applied to contemporary corporations." Do you think this statement is completely true, partly true, or completely false? Why? In what ways, if any, do you think Locke, Smith, and Marx would want to change the way contemporary corporations operate?

A minimum number of characters is required to post and earn points. After posting, your response can be viewed by your class and instructor, and you can participate in the class discussion.

Submit

0 characters | 140 minimum

SHARED WRITING

Evaluate the U.S. Economic System

Consider this statement: "Equality, justice, and a respect for rights are characteristics of the U.S. economic system." Would you agree or disagree with this statement? Why?

A minimum number of characters is required to post and earn points. After posting, your response can be viewed by your class and instructor, and you can participate in the class discussion.

Submit

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Case Study 3.1: The GM Bailout

By mid-December 2008, GM, the world's second largest auto manufacturer, was losing \$2 billion a month. Rick Wagoner, CEO since 2000, knew that GM did not have enough money to survive much longer. The year 2008, GM's 100th anniversary, was turning out to be its worst ever.¹ Wagoner already knew GM would end the year with losses of about \$31 billion. But that was an improvement from 2007 when the company lost \$38.7 billion, the fourth-biggest corporate loss in history. Those losses, and losses of \$1 billion in 2006 and \$10 billion in 2005, meant that the company Wagoner led lost an astonishing \$80 billion in four years.

Wagoner was a dedicated, affable, and likable man. In high school, he had excelled in all sports but, at 6'4", his height made him a star in basketball. Upon graduation, he was secretly hoping to become a professional basketball player. As a freshman basketball player at Duke University, it became clear to Wagoner

that he did not have the talent and drive to be a professional athlete. Instead, he majored in economics and also began dating Kathleen Kaylor, whom he eventually married. After graduating from Duke and getting an MBA from Harvard University, Wagoner went to work for GM. He rapidly worked his way up through the company's ranks. In 2000, Wagoner was named CEO, the youngest person to ever hold that position in the company's history.

The Company's Crisis

CEO Wagoner blamed GM's misfortune on a number of factors. One of the most significant factors, he felt, was the "Great Recession" of 2008 that had hurt the sales of all the auto companies, particularly when the troubled banks stopped lending money, so customers could no longer get car loans. Unfortunately, GM did not anticipate the credit crunch, and by 2006, it had sold off a controlling interest in GMAC, the previously wholly owned finance company that had provided cheap loans to its car buyers. After GM sold 51 percent of GMAC to Cerberus for

\$7.4 billion, Cerberus refused to let GMAC continue providing the same easy credit to GM's customers, which turned out to be a significant blow to GM's sales.

Yet another problem was GM's labor costs. In 2008, GM was paying an average of about \$70 per hour for labor. That \$70 included \$30 that the worker actually received in wages, and \$40 that went to fund other labor costs including the worker's benefits and pension, plus the cost of providing health care and pensions to about 432,000 GM retirees. Because GM had been operating for 100 years, the number of its retirees was much larger than those of new car companies. Toyota, for example, was paying about \$53 per hour for labor in its U.S. manufacturing plants, of which \$30 went to the worker as wages, and \$23 went to pay for the worker's benefits and pension, but very little for retirees since the number was relatively low. In some of its plants, a Toyota spokesman said, it was paying as little as \$48 per hour for labor.

But perhaps the major cause of GM's difficulties was its self-inflicted dependence on large SUVs (sport utility vehicles). Japanese automakers could make small and mid-sized cars for less than it cost GM to make comparable cars. To compete, GM had to lower its prices until the profit margins on its small and mid-sized cars were vanishingly thin. But during the 1980s, when gas was cheap, GM discovered that large SUVs were big hits with male customers and with couples with growing families. Moreover, unlike its smaller car models, profit margins on its large SUVs were hefty, as much as \$10,000 to \$15,000 per vehicle. As its SUV sales boomed during the 1990s, GM expanded its line and eagerly converted many of its plants over to the production of the lucrative big vehicles. By 2003, the bulk of its profits were coming from SUV sales. But when the price of gasoline gradually crept upward, the costs of owning an SUV also increased, causing the SUV market to slow and then to decline. In 2004, unsold SUVs started piling up at car dealerships. When Hurricane Katrina made gasoline prices soar in 2005, sales of SUVs eventually collapsed. Thus, GM ended 2005 with a loss of \$10.4 billion. Things improved somewhat in 2006, but then losses climbed to record levels: \$38.7 billion in 2007 and \$30.9 billion in 2008. Unfortunately, by now GM's plants, strategic plans, research and development programs, and its mindset were all locked into the production of SUVs, and it would take years to change them.

Because of its reliance on SUVs, GM had put off investing in the small fuel-efficient cars a gas-conscious public had turned to in 2005. In the 1990s, GM had developed the technology for an all-electric car, the EV1. The EV1 was, in fact, the first mass-produced modern electric car made by a major car company. By 1999, GM had spent \$500 million producing the EV1 and \$400 million marketing it, yet had leased only 800 vehicles. Convinced that the car would never match the profitability of its SUVs, the company stopped making the cars, and in 2002, it repossessed all the EV1s it had leased and phased out the project. At the same time, both Toyota and Honda were introducing their small hybrid electric-gas engine cars into the United States. The hybrids turned out to be a commercial success and, more important, production of the cars allowed both Toyota and Honda to gain almost a decade of experience in hybrid technology, while GM continued focusing on its gas-guzzling SUVs. In a June 2006 interview published in *Motor Trend*, Rick Wagoner confessed that his worst decision during his

tenure at GM was "axing the EV1 electric-car program and not putting the right resources into hybrids."²

All of these problems had culminated in the \$80 billion loss that placed GM in the difficult situation Wagoner knew he had to deal with in the closing weeks of 2008. With many analysts predicting that GM would go bankrupt, banks—which themselves were barely surviving the worse financial crisis in decades—refused to loan the company more money. At the rate it was running through its cash reserves, Wagoner knew the risk of bankruptcy was growing daily. Given the company's dire straits, he decided that only a government bailout could save it.

The National Crisis

Government bailouts were not popular. In September 2008, the George W. Bush administration asked the U.S. Congress to pass legislation creating a \$700 billion fund called the Troubled Asset Relief Program (TARP). A reluctant U.S. Congress approved the TARP bill, which authorized the U.S. Treasury Department to use the funds "to purchase . . . troubled assets from any financial institution." The troubled assets were millions of mortgage loans that banks had extended to home buyers who were now unable to make their monthly mortgage payments, and whose homes were worth less than their mortgages because home prices had collapsed in early 2007. Since the homes were worth less than their mortgage loans, the mortgages could not be repaid in full when delinquent homeowners sold their homes or when banks confiscated them. Suffering huge losses, many U.S. banks were on the verge of failing as were European banks that earlier had taken over thousands of the U.S. mortgages that were now in default. Many economists predicted that these widespread bank failures would turn the deepening recession into a global depression worse than the worldwide Great Depression of the 1930s.

In spite of the looming financial crisis, many had opposed the plan to bail out the banks. A hundred leading economists signed a letter to the U.S. Congress that said lack of "fairness" was a "fatal pitfall" of the plan because it was "a subsidy to investors at taxpayers' expense. Investors who took risks to earn profits must also bear the losses."³ Calling the bank bailouts "socialism for the rich," the Nobel prize-winning economist Joseph Stiglitz wrote, "this new form of ersatz capitalism, in which losses are socialized and profits privatized, is doomed to failure. Incentives are distorted [and] there is no market discipline."⁴

The Request

Nevertheless, if U.S. banks were able to get bailout money from Washington, perhaps GM could do the same. So Rick Wagoner and two GM board members flew to Washington on October 13, 2008, to meet with officials of President George W. Bush's administration. During the meeting, Wagoner summarized the precarious position of the company and asked for a loan from the TARP fund. Bush's people balked at the request, saying the legislation explicitly said TARP funds were for financial institutions, so they could not be used to provide loans to car manufacturers. Turned down by the administration, a desperate

Wagoner turned to the U.S. Congress. On November 18 and 19, he and the CEOs of Chrysler and Ford—the two other U.S. auto companies were also going through difficult times—came before Congressional committees and asked for legislation authorizing government funds to aid the auto industry. Committee members, however, became angry, particularly when the auto executives admitted they had not prepared plans detailing how they would use the funds nor what changes they intended to make to ensure that they could return to profitability. In the end, the three CEOs were told to come back in December with detailed financial plans for their companies. In early December, the CEOs dutifully returned to the U.S. Congress with plans in hand and repeated their requests for financial assistance. A few days later, both the U.S. House and the Senate proposed legislation to aid the auto companies. Unfortunately, while the House approved the auto aid bill on December 10, the Senate voted it down. Without the support of both the House and the Senate, the proposed legislation was dead.

Wagoner was stunned and despaired for the future of the company he had served for over 30 years. But his despair turned to elation when he got a telephone call from the Bush administration. The administration had decided the U.S. Treasury could, after all, use the TARP funds to provide loans to GM as well as to Chrysler. (Ford had decided it could survive without government money.) On December 19, 2008, President Bush announced that the U.S. Treasury would provide GM with a \$13.4 billion loan from the TARP fund, while Chrysler would get a \$4 billion loan. In announcing the assistance to the auto companies, the Bush administration declared, “the direct costs of American automakers failing and laying off their workers . . . would result in a more than one percent reduction in real GDP growth and about 1.1 million workers losing their jobs.”⁵ To get the money, Wagoner had to agree that by February 17, 2009, GM would hand over a detailed plan specifying how it would achieve “financial viability” and the plan had to be acceptable to U.S. Treasury officials. With his back to the wall, Wagoner agreed to the terms and on December 31, 2008, GM got a first installment of \$4 billion from its allotted loan amount; it received another \$5.4 billion on January 16, 2009, and a final installment of \$4 billion on February 17, 2009.

Many objected that bailouts violated the free market philosophy embraced by many Americans and replaced it with a kind of socialism. Republican Senator Bob Corker said the GM bailout “should send a chill through all Americans who believe in free enterprise.”⁶ Several Republican members of Congress submitted a resolution on the bailouts that said they were “moving our free-market based economy another dangerous step closer toward socialism.”⁷

A New Administration

By February 17, 2009, newly elected President Barack Obama had taken office, and his administration would end up finishing the auto bailout that the previous administration had set in motion. As part of the “viability plan” that he had agreed to submit by February 17, Wagoner was to renegotiate GM’s union contracts to make its labor costs competitive with foreign car makers in the United States, reduce the number and models of cars it made, shrink its unsecured debt of \$27.5 billion down to

\$9.2 billion by getting creditors to cancel part of their debt in exchange for GM stock, and invest in fuel-efficient hybrid and electric vehicles.⁸

Wagoner had quickly entered negotiations with the United Auto Workers (UAW), GM’s major union, and with creditors. But GM’s creditors stubbornly refused to reduce their debt by the amount the government wanted. In the end, GM did not reach the debt reduction targets the U.S. Treasury wanted it to reach by February 17. Nevertheless, in the final “plan for viability” it submitted to the U.S. Treasury on February 17, GM said it would cut 37,000 blue-collar jobs and 10,000 white-collar jobs, close 14 plants over 3 years, eliminate 4 of its 8 car brands, cut manager salaries by 10 percent and all other salaries by 3 to 7 percent, and shift the costs of retiree health insurance to an independent trust funded in part with GM stock and in part with debt. However, as the plan indicated, GM would need an additional \$22.5 billion from the government to continue operating to 2011.⁹

The Auto Task Force Obama had put together to review GM’s proposed plan was not happy with the plan. Steven Ratner, who headed up the task force said:

It was clear to us from the “viability plans” that the companies had submitted on Feb. 17 that GM and Chrysler were in a state of denial. Both companies needed gigantic reductions in their costs and liabilities. They had way too many plants and workers for expected car volumes. And their labor costs were out of line with those of their most direct competitors . . . I was shocked by the stunningly poor management that we found, particularly at GM, where we encountered, among other things, perhaps the weakest finance operation any of us had ever seen in a major company.¹⁰

“Team Auto,” as the Obama task force called itself, spent over a month studying the plan and concluded that GM’s optimistic assumptions that its market share would grow in the future, its costs would decline, and in a few years it would have positive cash flows were out of touch with reality. On March 30, 2009, the Obama administration told the company that its plan was not acceptable and did “not warrant the substantial additional investments . . . requested.” Nevertheless, GM was given 60 days, until June 1, to try to extract deeper concessions from its creditors and was also given another loan of \$6.36 billion to carry it through the next two months. Although GM continued trying to work with its creditors, the Obama task force soon realized that the only way GM would force its creditors to forgive GM’s debt was by filing for bankruptcy.¹¹ This would give a federal judge the authority to cancel as much debt as was needed for the company to become a viable business again. On March 31, the U.S. Treasury informed the company’s board of directors that if it filed for bankruptcy, the government would provide the funding it would need to emerge as a viable company.

By this time, Rick Wagoner’s fate had been sealed. In mid-March, Steven Ratner asked Wagoner about his plans and he replied, “I’m not planning to stay until I’m 65 but I think I’ve got at least a few years left in me . . . , but I told the [Bush] administration that if my leaving would be helpful to saving General Motors, I’m prepared to do it.”¹² On Friday, March 27, Wagoner attended a meeting with the Auto Task Force to discuss GM’s

restructuring plans. Before the meeting Steven Ratner pulled him aside and said, "In our last meeting you very graciously offered to step aside if it would be helpful. Unfortunately our conclusion is that it would be best if you did that." Wagoner agreed to step down, and on March 30 he submitted his resignation from GM.

Bankruptcy and Restructuring

On June 1, 2009, GM entered bankruptcy. The U.S. Treasury created a new company named General Motors Company, and the now bankrupt "Old GM" sold its most profitable brands and most efficient manufacturing facilities to the new General Motors Company that used \$30 billion of the government's money to buy them. The creditors of Old GM received a 10 percent share of the new company plus proceeds from the sale of the assets of the old company. A 17 percent share of the new General Motors Company was put into a trust to pay for union retiree health care benefits; the union trust also received a \$2.5 billion note from the new company and \$6.5 billion of its preferred stock. The government of Canada, which had contributed \$10 billion to bail out several GM plants in Ottawa and Ontario, got 12 percent of the new company. The remaining 61 percent share of the company became the property of the U.S. government in return for a total of \$50 billion it pumped into the enterprise. The U.S. government also retained the right to elect 10 of the 12 members of the board of directors of the New GM. The government was now the major owner of a car company.¹³

GM was not the only firm that became a (partially) state-owned company during the financial crisis. On February 27, 2009, it was announced that in exchange for \$25 billion the U.S. Treasury was taking 36 percent ownership of Citigroup, Inc., a large banking company driven to the brink of failure by the financial crisis. On September 16, 2008, American International Group (AIG), an insurance company also brought to its knees by the financial crisis, announced that the government, through its Federal Reserve Bank, was taking ownership of 80 percent of the company in exchange for \$85 billion.

Super Socialism?

Many observers pointed out that the government's new ownership of companies is the kind of government ownership of the means of production that Marx and other socialists advocated. As Robert Higgs, editor of the *Independent Review*, wrote, "the government is resorting to outright socialism by taking ownership positions in rescued firms."¹⁴ The Mackinac Center, a conservative research institute that was focused on promoting "the free market," published an article by Michael Winther that stated:

There are only two economic systems in the world. . . . These two economic systems are generally described as "the free market" and "socialism." . . . Socialism is characterized and defined by either of two qualities: Government ownership or control of capital, or forced pooling and redistribution of wealth. . . . [T]he current bailout could be described as "super-socialism" because it involves every possible component of socialism:

the forced redistribution of wealth, increased government control of capital, and even the extreme of socialism, which is government ownership of capital. Our federal government is not content to just regulate the markets (capital), but is also taking the next step of purchasing ownership interest in previously private companies.¹⁵

WRITING PROMPT

Think Critically about the GM Bailout

1. In your view, should the GM bailout have been done? Explain why or why not using the ideas of the various thinkers discussed in this chapter. In your view, was the bailout ethical in terms of utilitarianism, justice, rights, and caring?
2. In your judgment, was it good or bad for the government to take ownership of 61 percent of GM? Explain why or why not in terms of the theories of Lock, Smith, and Marx.

The response entered here will appear in the performance dashboard and can be viewed by your instructor.

Submit

Case Notes

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Case Study 3.2: Accolade versus Sega¹⁵

Accolade, Inc. is a small software company located in San Jose, California, that had prospered by making and marketing games that could be played on Sega game consoles. Its most popular game so far was a game called "Ishido: The Way of Stones." Sega had not granted Accolade a license to make games for its consoles, and Sega derived no income from sales of Accolade's games.

In the early 1990s, Sega marketed a new game console called Genesis, and Accolade engineers discovered that their games would no longer work on the new console because Sega had inserted new secret codes and security devices into its Genesis consoles that prevented other game programs from working on the console except those made by Sega. To get around this problem, Accolade engineers set to work reverse engineering Sega's new console and several of its games.

Reverse Engineering

Reverse engineering is the process of analyzing a product to discover how it was made and how it works. First, Accolade took several Genesis consoles apart to learn how its security mechanisms worked. Then, Accolade decompiled several of Sega's game programs.

To understand what this involved, it is necessary to understand that the software that makes up a game is produced in a two-step process.

- Engineers write the program for the game using a software language that is easily understood by an engineer who knows the language and that consists of a series of comprehensible instructions such as "GOTO line 5." This version of the program is called the *source code*.
- Once they have finished writing the source code, the engineers enter the source code into a computer that compiles the code, essentially translating it into a machine language consisting of zeros and ones (such as 00011011001111001010). Although the new compiled code is virtually impossible for a human to understand, the series of zeros and ones that make up a compiled code can be read by the game console computer and provides the basic instructions that make the game operate.

Software game programs (and, in fact, all software programs) that are sold in retail stores consist of such compiled code. Decompiling is an attempt to reverse the two-step process through which the program was originally produced. Basically, the compiled or machine code that makes up the software program is fed into a computer that attempts to translate the machine language (i.e., the series of zeros and ones) back into the original source code language (i.e., instructions such as "GOTO line 5") that can be understood by the engineer. The engineer can then examine the new source code and discover exactly how the program works and how it was put together. The process of decompiling is not always completely accurate, and sometimes engineers

have to work hard to figure out exactly what the original source code was. Many engineers believe that reverse engineering, particularly decompiling, is inherently unethical.

Legal Viewpoints

Unethical or not, Accolade engineers succeeded in getting the information they wanted, and with this knowledge they were soon able to write games that would work on Sega's new Genesis consoles. Sega, however, immediately sued Accolade, claiming that the company had infringed on its copyright. Initially, the U.S. District Court in San Francisco agreed with Sega and issued an injunction forcing Accolade to withdraw its Sega-compatible games from the market.

Sega lawyers argued that when Accolade reverse engineered its software programs, Accolade had illegally made copies of Sega's source code. Because this source code was owned by Sega, Accolade had no right to copy or reverse engineer it, and Accolade in effect had stolen Sega's property by doing so. In addition, the new games that Accolade wrote had to include secret codes that were required to allow the software to work on the Genesis console. These secret codes, Sega claimed, were also owned and copyrighted by Sega and so could not be copied by Accolade and inserted into its game programs.

Accolade appealed the decision of the U.S. District Court to a higher court, the Ninth Circuit Court of Appeals. Accolade claimed that the secret codes and security devices that Sega had used and that had to be known to allow games to play on the Genesis console were in effect a public interface standard. An *interface standard* is a standardized mechanism that one kind of product must use if it is to be able to work on another product. (The standard prongs that an electric cord must have if it is to fit into a standard outlet are an example of a simple interface standard.) Such interface standards cannot be privately owned by anyone, but are public property that can be used and duplicated by everyone. It was permissible, Accolade lawyers argued, to duplicate the source code because this was merely a way of getting access to the interface standard on the Genesis consoles. It was permissible for Accolade to include copies of these secret codes in its games because they were public property. Accolade's arguments eventually won out when it appealed the decision of the U.S. District Court in the Ninth Circuit Court of Appeals. The Ninth Circuit Court of Appeals overturned the earlier decision and essentially agreed with Accolade.

However, many legal experts disagreed with the Ninth Circuit Court of Appeals. They felt that Accolade's arguments were wrong and that the company had really stolen Sega's property. The security devices and secret codes that Sega had developed were not like the interface standards that different companies must agree on when working on products that must be compatible with each other. It is true that when companies are working on products that must be compatible with each other—tires that must fit on cars, or electric plugs that must fit into electric sockets—they need to agree on a public standard interface that no one will own, but that everyone will be able to freely use. However, some legal experts have argued, Sega's Genesis console was a product that belonged to Sega alone and for which Sega

wanted to be the sole provider of games. Thus, this was not a case of different companies having to reach an agreement over a public standard; it was a case of a single company making use of its own private technology to make its own games. So, critics of the court's decision concluded, there was no public interface standard involved in the Accolade–Sega case.

WRITING PROMPT

Think Critically about Accolade versus Sega

1. Analyze this case from the perspective of each of the theories of private property described in this chapter (i.e., from the perspective of Locke's theory of private property, the utilitarian theory of private property, and the Marxist theory of private property). Which of these views do you most agree with and which do you think is most appropriate for this case?

2. In your judgment, did Accolade go too far in trying to discover the underlying source code of Sega's programs? Does a company have a right to reverse engineer any product it wants?

The response entered here will appear in the performance dashboard and can be viewed by your instructor.

Submit

Case Notes

16. This case is based on Richard A. Spinello, "Software Compatibility and Reverse Engineering," *Case Studies in Information and Computer Ethics* (Upper Saddle River, NJ: Prentice Hall, 1997), pp. 142–45.

Summary

1. The effects of globalization have led many people to question the ethics of free trade and free markets, especially in light of the impact that global free trade has had on workers and poor nations. A key issue is the proper roles of command systems and markets. In the United States, three thinkers historically have been responsible for the prevailing ideologies regarding the relationship between markets and government commands: John Locke, Adam Smith, and David Ricardo. A fourth thinker, Karl Marx, was a critic of capitalist free markets.
2. While John Locke did not directly discuss markets, he did argue that if there were no governments, people would be in a state of nature, in which they would have a natural right to life, liberty, and property. People form governments to protect these natural rights. Governments, therefore, should not take away people's liberty or property, except when necessary to protect others from harm to their lives, liberty, or property. Many thinkers have used Locke's views to argue that government should not interfere with the freedom of people to exchange their property in markets. Critics of Locke have countered that Locke did not show that people have these natural rights and that, even if such rights existed, they would not override all other rights. Critics also argued that free markets create inequalities and that Locke's assumption of people as atomistic individuals was incorrect.
3. Adam Smith used a utilitarian argument to support his view that government should not intervene in the free market. He argued that the invisible hand of market competition would lead market sellers to provide what consumers need at the lowest "natural price." Moreover, a system of competitive free markets would lead producers to use their resources as efficiently as possible. If government interferes with these free market forces, he argued, it would only reduce the efficiency of markets, leaving everyone worse off. Smith assumed that the kind of society he was discussing had a private property system, a type of system that earlier thinkers such as Thomas Aquinas had favored. Later economists such as Ludwig von Mises and Friedrich A. Hayek supported Smith by arguing that governments cannot allocate resources as efficiently as the free market does. Critics of Smith have argued that Smith did not consider the power of large companies or the monopolies created by patents, that he ignored external costs, and that he wrongly assumed that all humans are fundamentally self-interested. Economist John Maynard Keynes criticized Smith's claim that government intervention always makes things worse. Keynes argued that during economic depressions, aggregate demand is not sufficient to absorb an economy's aggregate supply of goods, and government spending must then make up for the deficit in order to lead the way out of the depression.
4. David Ricardo focused on free trade between nations and, like Smith, used a utilitarian argument in his defense of free trade. In what has been called the single most important argument in the history of economics, Ricardo introduced the concept of comparative advantage. He argued that if each country specializes in producing what it can make more efficiently than other countries and traded for what other countries made more efficiently, then all countries would be better off. Today Ricardo's argument remains the key rationale supporting globalization and free trade between nations. Many people have pointed out,

however, that Ricardo makes several assumptions that no longer hold, and, moreover, that he did not foresee that international rule setters might be influenced by the more powerful nations who might use those rule setters to exploit weaker nations.

5. Karl Marx was a harsh critic of the injustices of free market societies. He argued that in a capitalist free market society, workers were exploited because they do not receive the full value of what they produce with their labor. The owner unjustly takes their value as profit. Marx also made a number of other arguments. For example, the way each society organizes itself to produce the goods it needs determines its social classes. Most societies have organized their production by having a working class, which provides the labor, and a ruling class, which controls and directs that labor. Each society's government, laws, social beliefs, and social institutions are designed to protect the position of its ruling class. Capitalist societies are divided into two classes: a class of workers who must sell their labor to the capitalist owner in order to survive and a class of capitalist owners who

unjustly exploit them. In capitalist societies, workers suffer immiseration: as wealth gets concentrated in ever fewer hands, economies fall into periodic depressions, unemployment rises, and wages decline. Critics say that Marx assumed that a just society must have no inequalities, but the productivity that free markets make possible may be more important than any inequalities they may produce. Critics also argue that free markets protect other forms of freedom and that Marx's predictions have not turned out to be correct.

6. Most societies today are based neither on free markets nor on government commands alone. Instead, most use mixed economies that retain a market and private property system and rely on government to remedy the inequalities and problems that free markets may create. Societies today also struggle with the question of what kind of property rights, if any, should protect intellectual property. Some have argued that Locke's notions of private property should be applied to intellectual property, while others claim a more Marxian view, that intellectual property should have a collective or common ownership and serve the good of all.