2011

Digital Distribution: Is it Really Finally Here

Robert Brown
Shawn Freeman
Michael Klotz
Steve Nix
Tom Paquin

Follow this and additional works at: https://scholar.smu.edu/scitech

Recommended Citation
https://scholar.smu.edu/scitech/vol14/iss3/15

This Article is brought to you for free and open access by the Law Journals at SMU Scholar. It has been accepted for inclusion in Science and Technology Law Review by an authorized administrator of SMU Scholar. For more information, please visit http://digitalrepository.smu.edu.
Digital Distribution: Is It Really Finally Here?

Moderator:
Ron Jenkins, Deputy Director, Development & External Affairs, The Guildhall at SMU

Panelists:
Robert Brown, COO & General Counsel, mygameIQ.com
Shawn Freeman, SVP Digital Commerce, GameStop Corporation
Michael Klotz, Director of Digital Games, The NPD Group, Inc.
Steve Nix, Director of Digital Platforms, id Software
Tom Paquin, EVP & CTO, OnLive

Introduction By Ron Jenkins, Development & External Affairs, The Guildhall At SMU

MR. JENKINS: We really appreciate everybody being here today. I am deputy director of the Guildhall at SMU, and I am excited about the panel we have today; it is a very interesting panel. We are going to do things a little bit differently. We are going to go through each speaker, and I want each speaker to spend a little bit of time speaking about what their organization does and how it fits into digital distribution. We have heard it forever, and the purpose of this panel is to answer some questions: Where are we really? Is it here? Is it not here? When is it going to work? Are we past the last mile? What is happening? Am I going to be able to go into my TV and say: “TV—World of Warcraft,” and there it is on my TV? I do not know.

I want to start first with Michael Klotz with NPD Group. Michael is the Director of Digital Games for the NPD Group. NPD group is a leading global provider of critical marketing and sales information that offers industry expertise across more industries than any other market-research company. Michael joined NPD in 1999, where he has since managed key account services and sales across the consumer electronics, information technology, and video games industries. His current focus is building NPD’s digital game offerings. As a spokesperson for NPD, Michael has spoken about emerging trends in the game industry at numerous industry events, including the Game Developers Conference, Gamefest, and New York Games Conference. Married and the proud father of two children, Michael holds a Bachelor’s degree in Business Management from the College at Old Westbury.

Michael, give us your state of the digital game business. How big is it? I am fascinated by your releases I get all the time, because people always call the university and ask: “How big is the game industry?” I say: “Well, what number do you want?” It is all over the board. Talk about what you do at NPD, and talk about the state of the digital game business and where you see it going in the next couple of years.

MR. KLOTZ: Thanks a lot, Ron. Just to address the question about digital games, it’s actually an interesting way that the question was phrased, because when you talk about digital games to various people, it means different things. Are we talking strictly about digital downloads? Are we talking about Facebook games? Are we talking about additional add-on content that
you can download off Xbox LIVE Arcade? There are a lot of different areas that “digital games” encompass.

One of the challenges for NPD—and why I am focused on this area right now—is that NPD has really tracked the retail space since the early '90s on video games and worked with retailers such as GameStop, Best Buy, and Target. NPD takes their retail information and packages it into databases to get the size of the market, to get the best known games out to the publishers, and to find the people that are interested in that space. On the digital side, it is a lot more challenging to get to that information. We use our consumer panel—as well as some partners in the digital space—to make sure that we are addressing that information through the best channels that we have available. We recently put out a press release about gaming content.1 Gaming content does not include hardware, accessories, or anything like that. It is just software, new and physical video games, used games, game rentals, subscriptions, digital full-game downloads, social-network games, DLC, and mobile game apps. We estimated the all-encompassing number for 2010 was about $15.5 billion in the United States. Just as a point of reference, physical sales were about $10.1 billion. So you are looking at about a third of consumer spending being spent outside the traditional retail channel. What is really interesting is the question of whether digital games are here yet. If you look at the physical market, it was down about 5% versus last year, but the digital pieces really made up for that decline, and the industry kind of came in flat when you compare 2010 versus 2009. This is a relatively new report from NPD. We are going to be digging deeper into it over the next few months and plan to release a lot more details towards the end of March.

MR. JENKINS: What can NPD do to improve the validity of the figures? The reason I ask is—again from an academic perspective—people call and ask us how big the video game industry is. I can look at Price-waterhouseCoopers’s stuff, and look at your stuff, and look at different things. There are a lot of things put out that claim the video game industry is twice as big as the movie industry. There does not seem to be a good repository of information regarding what the digital game industry includes. It just seems to be all over the market. How can we improve? What do you guys at NPD need to have better data?

MR. KLOTZ: We need the people in the digital space to work closer with us. That is really my focus right now—trying to figure out a way to work with Xbox LIVE, PlayStation, Valve, Big Fish Games, Facebook, all of the biggest players in the different areas that I mentioned. We are currently figuring out how we can work with them, and how we can provide information to them in exchange for the data they have. That way this data that we are putting out becomes more accurate, and we can dig down deeper into it with more granularity.

MR. JENKINS: Why will they not work with you on that data? It would seem that with public companies, you could get that data fairly easily because they have to report sales. What is keeping them from reporting those sales and why are they so guarded with it?

MR. KLOTZ: Without getting into too much detail on any individuals, there are a wide range of reasons. A lot of these companies hold that information tightly because it is a competitive advantage to not let others know how big they are, or conversely how small they are. They really want to make sure that they are digging through data that nobody else has access to, and making better decisions based on that data before anybody else gets a chance. So it is really just a matter of them just wanting to make better decisions, without their competitors finding out what those decisions are based on.

The reason why the digital space is so different from the traditional retail space is that if you go into a Best Buy, or a GameStop, or a Target, and buy a video game, it is the same video game at every location. There are collector’s editions that are exclusive, but essentially we can mask what retailer a video game came from. So you cannot look at our numbers and figure out how big GameStop is, or how big Best Buy is. All the numbers are totaled up to just find out what the top titles are.

Within a digital space, there is so much exclusive content that if Xbox LIVE Arcade decides to share all their information, it would be pretty easy to figure out how big Microsoft’s Xbox LIVE business is. This is because a vast majority of their games are exclusive to Xbox LIVE Arcade. That is one of the biggest reasons why it is more difficult on the digital side. The approach that we have taken is that we are reporting numbers like $15.5 billion, like I mentioned earlier. We are taking the total numbers and digging down into that without providing too much information behind the scenes. That we are still protecting those companies and their privacy, while still trying to provide the information that our clients are seeking from us.

MR. JENKINS: Have you done any studies, or have you looked at any trends that say where we are going to be five years down the road?

MR. KLOTZ: We do not do too much forward looking. We have looked at getting into that area, but one of the reasons why I do not think we have is because there are a lot of companies out there that do forecasting already. Unless we can do it significantly better than anyone else, we are not going to play in that area. We are going to focus on where our expertise lies and stick with that.

MR. JENKINS: Next, Shawn Freeman, who is with GameStop. Shawn is currently the Senior VP and General Manager of Digital Business for GameStop, the world’s largest specialty video game and entertainment-software retailer. In his role, he is responsible for leading the development and management of the digital aggregation and the retail strategy, employing a multi-channel approach that embraces GameStop’s more than 6,200 stores across the globe as well as the company’s website, GameStop.com. Shawn has twenty years of senior management experience. He was with the Chi-
cago-based TicketsNow.com and Senior Vice President for Ticketmaster in North America. He has worked as CTO for Handango, a leading smartphone retailer, and CIO for Hotels.com, one of the world’s leading online travel sites. So Shawn, what is GameStop up to? We want to know.

MR. FREEMAN: How about I share what I am up to? I was brought in about fourteen months ago. A few years ago, the company commissioned some primary research to take a look at digital distribution—the evolution of games to either digital games or digital distribution. I think one can say digital games are sort of a superset of digital distribution. Obviously, there are some games you can play within the browser that you do not actually have “delivered” to you. We took a look at that a few years ago and realized that digital distribution ultimately was inevitable. So one question of this panel is: “Do we think it is coming?” I think the answer is sort of a resounding “Yes.” We believe in it, and probably most people believe in it. So we began to take a look at what we wanted to do with our business to prepare for that. I was one of the folks brought in as part of that strategy.

Over the last fourteen months, I have been working on a couple of things. One, we have a significant online business today, and that business is growing. That business is still centered largely on the physical distribution of games. While we have a relationship with the consumer—electronically or digitally—ultimately the games, for the most part, are still fulfilled physically. We ship games to the consumer rather than having them pick games up in the store. You can also buy from us online and pick up at our store now. We have a tremendous community of gamers within our company. Globally, we have 40,000 gamers across 6,500 stores that are just about as passionate about games as digital customers are. Then, we have 500 million people walk in our stores every year to discover games, and then ultimately purchase a game. We are trying to take that experience and move that experience online.

Ultimately, in my view, digital distribution is just another way of handing the game to the consumer. The discovery experience is really important. How does a consumer find the right game for them? What GameStop has done better than any other retailer is create the best discovery experience, and that is evident when you walk into one of our stores. As a parent, I meet parents all the time who share stories about their experiences in GameStop stores: being able to walk into a GameStop store, talk to a very knowledgeable and understanding salesperson, and ultimately get great advice on what game to buy. We want to take that experience online. We have started that experience with our e-commerce site. But now we are starting to either acquire or build other capabilities that will ultimately allow us to deliver games electronically or digitally rather than physically through the mail.

MR. JENKINS: So what does that do with your relationship with your current business model with publishers? I think everybody is on the outside looking in wondering “Where is GameStop going to be five years down the road?” How are you dealing with that in your company? As companies get bigger, one side of the company sometimes competes with the other side of
the company. So how are you managing that, and how are you managing relationships with developers and publishers?

MR. FREEMAN: It is a good question. I look at it a couple of ways. I think for the most part, what we are doing today is hoping to deliver digital versions of the games we sell on disk. That means that we are ultimately talking to the same customers, the same developers, and publishers. I do not think the nature of the conversations is any different than when we were conversing about a disk in a box. I think that will continue to hold true until some sort of other method of delivering content is part of what we are doing. We are beginning to look at other games that are outside of what we would consider our core business. A good example is our acquisition last year of a company called Kongregate, which is one of the leading providers of casual browser-based games, or Flash games. That was very different from our core business and opened us up to conversations with developers and publishers that we were not working with before. The economics of that business are different. The business models of that are different and are continuing to evolve. That is leading us into conversations that are different than conversations we have had in the past. All I can say is that the conversations are evolving. I think anyone that is in that business would say that the business models are continuing to evolve. How you monetize consumers in that world is continuing to evolve, so the basic economic relationships will also continue to evolve.

MR. JENKINS: I think, from what I read, the big advantage is the price point. Instead of putting it in a box, if I am able to download it, the price should be lower. It would expand sales and more people could get to it. How do you see that? Have you guys talked about that? What does that mean to your business model?

MR. FREEMAN: Again, I cannot get into the specifics on the conversations we are having with our partners. We pay very close attention to the economics of the digital distribution of the same games that we do a very good job of selling physically today, as well as other types of games. I think it is still something that has to be defined a bit for us. You would suggest that—and I think this is sort of true when you look at other types of media—there is a consumer perspective that digital distribution should be less expensive to distribute, and therefore less expensive to purchase digitally.

MR. JENKINS: I did not say that. I said it was reported, but I am glad you are getting to that point.

MR. FREEMAN: Yes, we are certainly aware of that. I do not know if that is necessarily going to be the case as more of the business begins to shift to digital distribution. I think that is something that has yet to be proved. Right now, our core business is still physical games that are played on consoles. Greater than 95% of that business is still physical retail. It is hard to say today whether the economics of that business model will change dramatically once the percentage of games that are delivered digitally is more substantial.
MR. JENKINS: Thank you. For the last three years, GameStop has been at this conference. They have been willing to talk about used games, and anything else you want. Thank you for coming.

Tom, you guys are kind of the new guys on the block a little bit. We are very fascinated by your product offering. I hope when you talk, you tell us more about your company: where your vision is, where you think you are going, and how that fits into the game space. Tom Paquin provides vision, expertise, and leadership to the technical research development of OnLive as Executive Vice President and Chief Technology Officer for OnLive. With more than twenty years of management experience in leading technology companies, Tom has a track record of turning new ideas into technology products that become household names. Most notably, Tom helped found a little company called Netscape. Tom led the engineering of browsers and servers for Netscape 1 and 2 and spearheaded many innovative initiatives such as the development of SSL and web cookies. He later founded Mozilla, the not-for-profit company responsible for FireFox web browser and the Thunderbird email application. So Tom, what is this thing called OnLive?

MR. PAQUIN: OnLive is an idea born of the concept of being able to do high-quality, low-latency video encoding (low latency being a millisecond or less). The idea is to take a computer—which is a pain to administer and carry around and power and find a place for—and get rid of it. Extend your monitor cable, keyboard cable, and mouse cable way out to wherever the computer happens to be located. If you can virtualize all your software cloud-like, then we would not have to worry about computers anymore. If you extend keyboards to include game controllers, guitars, guns, and joysticks, then suddenly games are very available. About a year and a half ago, when we announced this, the world was jumping up and down saying:

“Yes, all very interesting, but if I press my button here, and it goes out over the Internet, and then some computer or some Xbox sees the press, and then the game figures out he is shooting, I must draw red on screen. Then the graphics card has to deal with that, and then we have to compress it. Then we have to send it back over the internet. Then you have to receive it, decompress it, and then display it. You are going to be dead six weeks before you even realized the bullet was fired.”

That is what we started with, the fact that we could get the video compressed very quickly. Chapter two—which has required more actual work—has been able to make this all work on, shall we say, imperfect residential networks. The backbone of the Internet is fungible and pretty usable in North America, and very usable in other parts of the world. It is the last hundred feet, as opposed to the last mile, that is the trick. So, technologically, my company has done several things. We have figured out the latency video encoding. We have done a tremendous amount of work on dealing with erratic, sporadic, changing, dynamic, network environments. And we offer game service. So we have a bunch of servers—three parts of the United States—running AAA games. They are running high-end games on very high-end machines with fancy graphics cards. This is not about Flash
Digital Distribution: Is It Really Finally Here?

The idea is you go buy a game, or demo a game, or rent a game, and anywhere you go, all you need is a screen and input device and you can play that game. We offer this service on PCs and Macs. There is a download—you install it and run it. We also have a little doohickey that you hook up to your TV, so all you need is your input device and your TV. We are starting to migrate into the TV. So basically, a chip set that is capable of drawing video can run our service. At the consumer end, it is just: “Oh, here is a USB event—send it up. Here is a bunch of video coming down from the sky—draw it.” And we try to make this happen quickly. That is the nature of the beast. Notably, there is no actual distribution in there. The games stay in the cloud, they run in the cloud—on computers in the cloud—and there are no bits to copy. There are no second sales. You buy the rights to the service, and you get the right to play this game in perpetuity.

There was an interesting question from the previous session about some rights. We have a feature called “brag clips.” For example, you are shooting the monster on level nineteen and you finally kill it or do something else cool. We TIVO everything all the time, and we save the last ten seconds of whatever you were doing as a brag clip. Later you can label it, sort it, rate it, and publish it. All your pals can see your brag clips. Brag clips are very popular. I have to go back and read our agreements. I do not know who owns the rights to the performance in the brag clip. It is an interesting little question. But definitely in the pursuit of our business, we have discovered that—when you do something new—you annoy a lot of lawyers. There is a list of things that are difficult when you do something today that just yesterday was perceived to be out of the realm of possibility—whether you have a large installment base or small installment base, or whether you are making money or not making money. My lawyers spend an enormous amount of time redlining things and not enough time saying: “What are we going to do about it?”

MR. JENKINS: I think our last panel is going to help you with that because they are going to talk about partnerships with their attorneys. A question is: “Where are you in the marketplace?” How many OnLives are installed?

MR. PAQUIN: We are new. We are young. I do not think we are actually publishing our user numbers because of all the previously mentioned reasons. Our hockey stick has started. We launched it in June—six or seven months ago. We have crept along, but the numbers have gone up. We are still microscopic from a console point of view. I think Nintendo is making a couple million Wiis a month. That is not us. We would like to get there. Right now, we are two hundred people in Palo Alto. As a start up, we are insane because in order to do the things I just described, you have to invent around thirty things. Ideally, to do a startup properly, you want to invent just one thing. So in that way, we are entirely too big.

We need more games. I think we have about 30 games. When a brand new console comes out, or a new platform of any form comes out, there is an adoption curve. It takes time. We are six months into this new console. I
am happy with our user community and our user community is happy with us. You might have guessed from the way our service works that if you do not have a very good internet connection, you are not going to like our service very much. So there is a bit of self-selection going on. But if you have a half-decent internet connection, then you will tend to be satisfied with our service.

One of the interesting things that we have not completely figured out what to do with is the feature in our system where we “videoize” everything. This allows all the players to watch each other play. There are privacy settings, but I can watch my friend descend into level 15 and blast the red dragon. We have kibitzers (watchers) now that go into the arena full of people playing Shoot ‘em Up Five and watch the guys that are really good. They know the guys that are really good, and they go in and just watch them play. It is astonishing how much time people spend watching other people play the game.

MR. JENKINS: What are you doing with all that data?

MR. PAQUIN: That is the thing. We haven’t really figured out what to do with it. We have ridiculous amounts of information on what people are doing, where they are doing it, and how they are doing it. But we are not clear about what we are going to do with the data yet.

MR. JENKINS: Now we switch to another side of the fence to my friend Robert Brown. Robert is the only attorney on the panel. He is general counsel at Pragmatic Solutions, the parent company of mygameIQ. He has over 20 years of business-development and revenue-generating experience with an emphasis on Internet, technology, and entertainment gaming industries. Robert’s expertise is in business development and intellectual-property law, with an emphasis on privacy law. Robert led the American Federation of Television and Radio Artists (AFTRA) Interactive Media Agreement, as well as handled the modernization of their information-technology agreements. He served as Vice President of Operations and general counsel for an internet-marketing-consulting company specializing in data collection. Robert is a graduate of Arizona State University and Whittier Law School. He is a member of the Pennsylvania Bar, and lives in California. With mygameIQ, you have a bit of a different business model. You work both on the entertainment side and the educational side of video games. Tell us a little bit about your company, what you hope to do, and what mygameIQ does.

MR. BROWN: We got started about six or seven years ago with the U.S. Army, which is our biggest customer. We are the only external development team that works with the U.S. Army. We do all their middleware, their back-end, and so forth. The U.S. Army came to us about two years ago and said that they wanted to move from fixed media to doing nothing but digital distribution. We were in the fortunate position that they were capable of making a quick decision and sticking with the decision. So we developed technology that basically allowed them to convert over to digital distribution. Everything with the Army is about saving money. So they wanted to stop pressing disks and having warehouses of disks. They wanted to do every-
thing digitally, update the process, and be able to handle everything from a marketing standpoint.

Pragmatic is basically a data company. We specialize in collecting information, assessing and analyzing the data, and trying to figure out what makes people tick. We work with institutions, people, and different industries. We saw the gaming industry was ripe because it gave a metaphor for people to understand why people do things. As people try to learn, we felt that gaming was more identifiable, and that is why we targeted education and serious games. We targeted games with a purpose and games that are interesting. We thought it was an underserved niche. Especially in the digital-distribution market where the larger distributors—like Valve and Steam—are not really interested in games that are not going to be AAA titles, games that do not have massive audiences, or games which are not going to do big numbers for them in the first 30 days. We saw an opportunity to target those users and bring games that were not as well known, or not as popular, to a much larger audience. So we tried to have some AAA titles and bring people to those. Then we tried to take the AAA audience and expose them to games that they had not seen before. We work with Federation of American Scientists, with HopeLab, and other similar companies that have pretty remarkable games that people do not normally get the opportunity to see. So we try to bring those games to a larger audience, and try to establish a market that people have not really seen before.

MR. JENKINS: What are you guys doing with all your data? What are you doing to safeguard your data? What kind of legal issues do you have since you do both entertainment and educational games? What things are you worried about?

MR. BROWN: From a development standpoint, we try to work with developers and make the data useful to them. The reason we actually targeted the serious educational and independent game industry is because those are the people that really seem to be interested in data. A lot of the larger companies are interested in data, but they do not really know what to do with it, and they just want to collect it or use it for sales data. We wanted to be able to use the data and actually target it, have it go back into the game, and have it affect gameplay. That was the initial concept. Could developers actually take the experience, take the data that they get from what people are doing, and improve or impact what is happening in the game? That is the first level.

The second level is to then figure out if there is some type of marketing or strategic advantage to be gained from the data. We want to go slow with that because we do not want to be out front where a lot of companies have not necessarily figured out what to do with the data. We do not want to be bleeding edge—where we are doing things that people find objectionable—or just blatantly market to people. We want to try to enhance the user experience. We initially developed technology where we could do in-game advertising but decided the industry was not ready for that and was not accepting of the in-game advertisements. We decided that there were better ways to do
it. We have done more things around the game. We are using the data to understand what the user experiences, to be able to market to them, and to be able to show them interstitial ads—which are shown as they go from game to game. Our system is set up in a channel metaphor. We actually have sponsors for the overall channels. And we work with large companies like Big Download, Newton, and Women in Games, and basically have channels that are dedicated to that particular content. We try to market that information based on the data that we collect.

MR. JENKINS: Last but not least is our friend Steve Nix. Steve is Director of Digital Platforms at Id Software. At Id Software, Steve focuses on digital distribution of Id’s legendary gaming brands, including Doom and Quake, and RAGE. Previously Steve managed external relationships for Id’s business development. Steve’s background in the game industry includes being the CEO of Ritual Entertainment, where he built the company to a multi-team and multi-platform studio that sold multimillion-dollar units during his six years there. Steve graduated from Texas Tech and from SMU’s MBA program. Steve, tell me what you are doing at Id as their Digital Platform Director.

MR. NIX: At Id we pioneered the shareware model, but for most of the company’s existence we have depended on traditional retail distribution of our products. When I was Director of Business Development, I started determining and working on our digital initiatives. Over time, I became interested in what we were doing digitally on things such as mobile phones. We have a web game called Quake Live for mobile phones where you can actually play a full 3-D shooter in a web browser anywhere in the world. Finally, I decided to focus completely on digital initiatives, so the company changed my title to Director of Digital Platforms. I do everything from managing our digital backlog across the various digital distribution channels, to managing what we are doing on XBLA with our games like Doom, Doom Two, and recently with Quake Arena Arcade and the release of Wolfenstein 3-D for PSN. I have launched five titles on the iPhone with Id’s various brands, which have been very successful for us. We have had some of the top-selling applications on the iPhone including the release of RAGE last fall. We are owned by a company called Zinemax Media and downloadable content (DLC) is a big part of our corporate strategy as well. We have done well with the DLC units, and they are growing increasingly important to us.

MR. JENKINS: You have been with Id practically forever. How much of your company is focused on this area, and where do you see it going in the future?

MR. NIX: The digital team and the groups I manage are a small portion of the development team. We have multiple titles in production. These modern AAA games take a lot of people to complete. Thus, we are a small component of the overall studio, and an even smaller component of the overall company. But we all see digital growth as important to the overall growth of the company. Id Software and Bethesda Publishing, Id’s publishing arm, are about creating great content first and foremost. Ultimately the distribu-
tion system does not really matter to us. We are concentrating on how to have the best content available. What do consumers want, how do they want it, and when do they want it? For a company like Id, it's about making great titles. We always focus on quality and games that really resonate with the consumers. Id needs to be flexible with our distribution methods. Obviously, we are predominantly retail now, but we will take advantage of new models as they come to market—such as PC digital distribution and the iPhone.

MR. JENKINS: As a developer, what type of technical issues do you have to deal with from these different distribution methods? Do you have to change the games? Yesterday our friend Rich told us that there were no "shooter games" on phones, and you have shown me six you have that are "shooter games" that appear to be pretty good. So from a technical standpoint, what kind of issues do you encounter? Are there legal issues such as who owns the game or how should the game go? Do you have to do different deals with every distribution partner?

MR. NIX: That is the way it is looking right now. We will literally have to do different deals with each upcoming digital distribution partner, including Steam, which has the largest market share. We go out and individually make deals with each distribution partner. We gauge their competence when we meet with them, and then decide who we are going to use for publishing. Some groups are great. Id gives them the games unprotected, with no digital-rights management on them, and they wrap them, put the website together, and do all the groundwork. When they send it back for approval, Id can tell them if the games and website run correctly and if everything is ready. There are other teams, such as newer start-ups, who are not as skilled in those areas. It takes a lot more hand holding when working with the newer teams, and there is the risk they could mess up.

Most companies are limited by their business development, quality assurance, and legal bandwidth. There are probably a hundred digital PC distribution companies out there. Some are established, and some are just getting going. Companies like Id have to rank these distribution companies and decide the order in which to work with them. We go through all this trouble to publish our games with these companies, and spend all the money to get the games done, so we have to make sure it will be worth our while. If they only sell five copies, we have wasted our time and theirs.

MR. JENKINS: Shawn to that point, how are you dealing with some of the legal and technical issues of digital distribution as you move forward?

MR. FREEMAN: My area of expertise is not the legal side. But on the technical side, I think our ambition is to be able to deliver games to our customers anywhere, and on any device. That is going to require us to build a lot of technology. We are in the process of building the necessary technology now. One of the exciting things about the business is all the different devices and ways for consumers to play games today. There are connected TVs, BluRay players, mobile devices, tablets, and other things that are playing games with impressive quality. There are a lot of different ways consum-
ers want to play games, so we are in the process of developing technology to
deliver games on multiple devices, which is not a trivial exercise.

MR. JENKINS: Steve, you talked a little bit about Valve, and Michael,
if you can speak to this: what kind of impact does Valve have on the market?
And do you believe their business model will continue to grow or change?
What do you think they are up to?

MR. NIX: Clearly Valve is the leader of the market. What they have
really done—after PC games were in decline for several years—is show that
there is an avid base of PC gamers out there, and most people believe their
sales are increasing, not decreasing. I think Valve proved the PC digital-
distribution model, and a lot of people have moved into this market because
of Valve. I think the PC digital-distribution space will continue to do well
and will continue to grow. As far as exactly where it is going to go, if any-
one claims to know that, they are probably going to be wrong. But the basic
business will continue to grow.

MR. KLOTZ: Based on some of the reports we did last year, if you look
at the front-line AAA titles that are available for download on the PC, I
believe Valve owns nearly 80% of the revenue that is earned in that channel,
thus they take a majority of the sales there. They also do amazing things in
fostering their community, so that people that are playing games on Valve
continue to engage in the community and find new content to download. The
percentage of people that are aware of Valve and that purchase games is
much higher than any other website or any other digital distribution model.

MR. FREEMAN: I would say that a lesson that we have learned at
GameStop is that you cannot segment consumers by platform. Those gamers
are engaging in games on their PC, their consoles, their mobile devices, or in
other ways. This has brought us back to being interested in the PC space
after we had walked away from that space as a company. I think the other
interesting part of that space is that digital distribution has re-opened the
opportunity for back catalog. What GameStop has seen in that market is
tremendous sales of titles that you could not get shelf space for in retail
anymore. Developers and publishers find ways to monetize those titles
today.

MR. BROWN: Legally, all individual distribution sites are negotiating
individual deals with companies, and it is incredibly labor intensive. I am
constantly put in the pecking order of companies asking how big our market
share is and being told: “We will get to you when we do that.” Several
distribution sites have different business models. Ours is a more integrated
approach where you are a mygameIQ customer and log in with a mygameIQ
account, and then we pass you through. So there is some integration work.
There is not a lot of integration work, but it does require some time with the
developer—usually a half day. The legal issues with that involve sharing the
customer. The customer is a mygameIQ customer, but we pass the informa-
tion along so it is their customer as well. Not a lot of digital distribution sites
do that. Several just do links or wraparounds, so it becomes more problem-
atic as to who owns the customer.
MR. KLOTZ: We see the issues of “who owns the customer” and “who owns the sales information” all the time when we are looking to work with new digital partners. We have partners who wanted to work with us and could not because they do not own the sales information of particular titles. This becomes part of the issue of why it can be so difficult to work with some of these companies.

MR. JENKINS: Robert, is ownership determined when you make the agreement?

MR. BROWN: Yes. Surprisingly ownership does not come up as often as you think. It is either taken for granted, or it is a new territory and people are not as sophisticated about it. From a point of making deals, ownership has never been a bone of contention and we never debate the issue because people just take it for granted. But it will probably become a problem down the road as people try to do sales reporting, and then ultimately when data becomes a commodity. When we can make money off of it and sell it to people—or resell it—then you have to ask questions: Who receives that money? Do we keep it? Do we make a deal with it? Should it be more of a business issue? These are issues that have not been fully addressed in all the contracts. The contracts just state that we own it, and that is just the way it is. At some point it will become a bigger business issue.

MR. JENKINS: Let’s take some questions. Does anyone have any questions from the floor?

AUDIENCE QUESTION: This question is geared towards Tom, regarding OnLive. Do you see the advent of OnLive being a success and continuing to move forward with more advertising, with the advertising being a continuing source of revenue? For example, Hulu plays advertising before its programming and sometimes in between. Is that a possibility for digital online distribution? For example, before a game will play, advertising may run or perhaps advertising could run in between segments of a game.

MR. PAQUIN: Definitely. To get to a game in our service you go to a service portal, choose a game, buy a game, and then get into the game. It is an interactive experience and there are several opportunities to choose what you present as advertising, and how those presentations would be monetized. We have not done advertising yet, even though the opportunity sits dormant, waiting to be exploited. Right now we are just trying to get people interested in the games.

When you have a centralized game service, you can modify the games in real time, especially if the games themselves are authored to bring in data as they run. Though trickier, this can be done on a console as well. One could have in-service data advertisements as well as in-game advertisements, much like seeing a billboard change as you drive by. The opportunities are endless. It is just a matter of where companies will put their money and effort.

MR. NIX: Actually, we have a similar idea. With the Quake Live platform that we have at Id software, if one is a standard user and has not paid for a subscription, they will be served a video before the game starts. We
also have dynamic end-game advertisements. The problem I have found is that there is not a good video aggregation service out there that specializes in the video game space and does these types of pre-roll videos. Basically, even the largest U.S. companies who want to do something in Europe have to go there and sign a separate subsidiary contract. There is no global company that has millions of videos available that we can serve into a game on a pre-roll basis to monetize a user in that way. In the U.S. we probably only monetize 10% of the actual video use, and the rest of the users are playing videos that come from our parent company or the publishing arm of our parent company. So there is a good opportunity out there for someone to build a business just getting millions of videos ready for videogames that do want to monetize in this way.