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What's in it for me?

by: Larry Kubal, Labrador Ventures – January, 2007

As 'user generated content' evolves, newer startups offer incentives for shared content – will it work?

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Time Magazine finally got it right for the 2006 Person of the Year. This time it was neither Osama bin Laden nor George Bush. It was you. Me. All of us who create, share, and define online content and the power of the Web consumer experience.

It was an interesting selection, particularly driven by the massive growth of YouTube, the continued success of MySpace, and the widespread legitimization of blogs everywhere. If ever there was a year when the online user – or more specifically the user who generates his or her own online content – got to run the show, this was it. Examples abound: Wikipedia, the online encyclopedia that is written, re-written and edited by its own users and readers grew even more influential; Craigslist, nothing more than a collection of classified ads posted by Craigslist users (and in many ways policed by them as well) generated more traffic than ever before, and Web 2.0 companies such as Revver and Dapper – video sharing and content 'eBay' startups, respectively – were some of the hottest VC deals around.

Yet, suddenly content creation alone no longer seems to be a good enough model. The newest twist is revenue sharing with, and incentive programs for, a site's users and contributors in exchange for their user generated content. It's suddenly all the rage. MetaCafe, a YouTube-like video sharing startup, is now one of the Web's fastest growing video sites, attributing it success to what it calls its Producer Rewards program. This program pays $5 for every 1000 'views' if a video breaks 20,000 views, according to NewTeeVee.com, a blog for next-generation video-related technologies. And the company further states it is already generating between 1.2 - 1.5 million unique visitors a day. According to Arik Czerniak, MetaCafe's CEO, the Producer Rewards program already accounts for 8 percent of the site's total traffic, claiming that the top 200 videos on Metacafe had more views that the top 200 videos on YouTube.

Is this the latest evolution of the power and control that has shifted hands to the online consumer? Or is revenue sharing with a site's content creators just another creative gimmick by Web 2.0 startups looking to generate heaps of traffic in a hurry while gaining a leg up on the non-revenue sharing competition? Indeed, it could be a bit of both. Yet, before VCs jump even further onto the user generated content bandwagon in search of the latest and greatest revenue sharing business models, it would be well worth our time and money to understand both financially and behaviorally what is going on and see if they really make sense long term.

A lot of them *'there'*?

Essentially, it's a simple concept. Companies across the online content spectrum are now layering in revenue sharing models for, theoretically, the benefit of their users – particularly their 'power users' – in the hope of generating massive increases in web traffic and online page views. Yet, how much are these users really getting paid, and who is actually garnering the greatest benefit here? According to Om Malik, founder and editor of GigaOm.com, a well followed blog in the technology arena, this extra revenue share kicker is more about the company than about the user. "It's a cheap way to grow traffic right now but I'm not sure there's a lot of there there," says Malik.

On one hand, sites like The Daily Reel appear to be going out of their way to compensate their best content creators, announcing in December that it will begin paying contributors for original videos, which will appear exclusively on TheDailyReel.com for a limited time before being syndicated to other sites. How much contributors are paid varies depending on the scope of their deals and their notoriety in the online video world, yet in addition to any upfront payments, video makers will get a cut of any ad revenues from the syndication of clips. Other video-sharing sites such as Break.com also seem willing to pay up – in marginal terms – for videos deemed potentially viral. In November, Break.com increased the amount it pays for videos to $400 from $250. (For animated content, it will pay up to $2000.) And in October, even Google agreed to share ad revenue from the sequel to the popular "Diet Coke & Mentos Experiment" video with its content creators.

On the other hand, payments on many lesser sites might not ever add up to much more than a cold

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plate of Top Ramen, even as VCs of all stripes continue to throw money at such deals in large amounts. Recently, ExpoTV, a site focused on user-generated product demonstrations and reviews, announced a $6 million Series A round of funding led by Masthead Venture Partners and Prism VentureWorks. Described as a YouTube for product reviews, ExpoTV rewards its users for their content through a "Pay-per-Play" program where a user receives $0.01 each time any of a user's published Video Opinion reviews are played. (Payments are made once per month via PayPal.) Yet as Malik describes it, "under these types of models, you have to be very, very good at this to make a living … and we're not even talking a documentary filmmaker's living." The other issue is that not every video can be propogated against.

Thus, has anyone really asked the question whether American Express or BMW really want to place their ads against just any ordinary user generated video? Or, in reality, just how many user generated content sites can actually become self-sustaining from ad revenue. How far out on the long tail can you go and still be viable? Much the way reality TV reached overkill proportions, so too could these sites – and early stage VCs will have taken unnecessary risks in a potentially oversaturated space.

Everybody's doing it!

Still, there's nothing like good hype to keep things interesting. In fact, not only are new startups embracing the revenue sharing models, the space is so 'hot' that even established Web 2.0 standouts are jumping on the bandwagon.

Non-profit Wikipedia announced recently that its for-profit affiliate company, Wikia Inc., is ready to give away all the software, computing, storage and network access that Web site builders need to create community collaboration sites, for free! In fact, Wikia will provide customers – bloggers or other site developres who meet its criteria for popular Web sites – one hundred percent of all ad revenue from any sites they build. The only catch, in what the company jointly refers to as open source software, open content, and 'OpenServing', is that it requires that sites built with the company's resources link to Wikia.com, which itself makes money through advertising. (Apparently even Amazon.com was impressed enough with the new model to invest in the company, becoming Wikia's first corporate investor following a $4M funding in March from Bessemer Venture Partners and Omidyar Network.)

Yet, where the model works best is perhaps far away from the over-hyped video content sharing web sites currently all the rage. One company, Cambrian House, thinks it has the user generated content revenue sharing model to end all others. The company uses 'crowdsourcing' – what is known as the 'wisdom and participation of crowds' – to discover and commercialize software ideas, with contributors of such content ideas ultimately earning royalties from the successful launch and future revenue generation of their products.

The 'user generated content' process works something like this: First, an idea is submitted to Cambrian House by aspiring entrepreneurs who might not have the bandwidth or resources to fully develop their ideas into companies. Second, crowds test and vote on the ideas, putting top ideas through monthly 'IdeaWarz'. Concepts that win 'IdeaWarz' are opened up to the development community where contributors can select certain project tasks in exchange for 'royalty points'. (Each idea selected starts with approximately 1500 royalty points, with 75 going to the idea creator, roughly 750 being retained by Cambrian House, and the balance being divvied up by those actually doing the work in building the product.)

Once a product goes live on a web site built by Cambrian House, as long as the product sells, idea creators and contributors all share in the revenues generated to the extent they've earned their own royalty points. "This is a way of getting beyond the hype cycle, where new technology gets released at the peak of inflated expectations," says Cambrian House CEO Michael Sikorsky. "Here, there's a generic way to monetize collaboration." The success of this model appears to be taking off – with Sikorsky boasting that the company was producing revenue within just 12 days of its being in business; a statistic that should be far more near and dear to an early investor's heart than simply analyzing the latest web traffic patterns.

Does all of this activity mean that revenue sharing paradigms – regardless of the online content sector they address – will become the new de facto standard among Web 2.0 startups, and that VCs must now demand their Internet companies adopt such models or risk being run over by competitors? Not likely.

The model, if it works at all, could yield higher highs in web traffic but will likely only do so from user generated content that would have performed well regardless. As Malik says, "At the end of the day, traffic comes from just two things, either the quality of the content or, like MySpace, something just happens." And it's that latter 'something' that is just a very, very hard thing to replicate, regardless of how much revenue or how many incentives one might choose to share. The potential financial rewards for content creators are unlikely to be significant enough to make the difference competitively among sites. And the as yet unanswered question is: can the inclusiveness of revenue sharing models behaviorally change community dynamics such that "something just happens?"

While we all look for the next magical MySpace to add to our portfolios, we shouldn't mistake a revenue-share business model for that ineffable magic. Revenue sharing with users might become common, but its ability to provide competitive differentiation is probably a fleeting thing. Even though it's the flavor of the moment; the sparkle of this fad, too, will likely fade with time.

This is one in a series of monthly columns on seed and early stage investing that Labrador Ventures was selected to contribute to the *Venture Capital Journal.*

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