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IFN Working Paper No. 1103, 2016

## **Two Sides to the Evasion: The Pirate Bay and the Interdependencies of Evasive Entrepreneurship**

Niklas Elert, Magnus Henrekson and Joakim Lundblad

# Two Sides to the Evasion: The Pirate Bay and the Interdependencies of Evasive Entrepreneurship

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*Abstract:* Evasive entrepreneurs innovate by circumventing or disrupting existing formal institutional frameworks by evading them. Since such evasions rarely go unnoticed, they usually lead to responses from lawmakers and regulators. We introduce a conceptual model to illustrate and map the interdependence between evasive entrepreneurship and the regulatory response it provokes. We apply this framework to the case of the file sharing platform The Pirate Bay, a venture with a number of clearly innovative and evasive features. The platform was a radical, widely applied innovation that transformed the Internet landscape, yet its founders became convicted criminals because of it. Applying the evasive entrepreneurship framework to this case improves our understanding of the relationship between policymaking and entrepreneurship in the digital age, and is a first step towards exploring best responses for regulators facing evasive entrepreneurship.

*JEL Codes:* L5; M13; O31; P14.

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## 1 Introduction

William Baumol's 1990 paper "Entrepreneurship: Productive, Unproductive, and Destructive" did for entrepreneurship economics what Douglass North (e.g., 1990) did for mainstream research on economic growth – it put the spotlight on institutions. Baumol (1990) relied on basic microeconomic assumptions to hypothesize that core entrepreneurial talents are used to maximize individual utility, not social welfare. Thus, entrepreneurship is not welfare enhancing by default. Rather, the way that institutions are rigged (the social structure of payoffs) influences the nature of the entrepreneurial activity. In this paper, we add to this analysis by studying the interdependency between formal institutions shaped by policymaking and entrepreneurial activities aimed at evading them.

Better knowledge of such interdependencies is important in a time when globalization, urbanization and digitization are fundamentally transforming societies and economies. New firms leverage digital technologies to access a global market instantly. For instance, digital service providers like Uber and Airbnb tap into urban markets across the globe to provide the matching of temporary housing and transport services. Other firms, like 23andme, provide personal genetic profiling to customers all over the world. And just as digital content separated songs from the cd, 3D-printing is on the verge of (temporarily) separating products from their physical form. All of these highly innovative examples have one thing in common: They challenge the existing institutional framework intended to regulate their business or markets one way or another. We argue that they can be described as examples of evasive entrepreneurship.

Evasive entrepreneurship is aimed at circumventing formal institutions in order to gain an advantage, facilitate change or exploit an arbitrage opportunity.<sup>1</sup> For instance, in order to avoid transportation market regulations, Uber consistently (and sometimes successfully) argues that it is not a transportation company but a technology company. Similarly, since Airbnb rentals often occur between individuals, the users typically do not comply with all the regulations that firms in the hotel industry face, even though

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<sup>1</sup> In North's (1990, p. 3) view, institutions are "the humanly devised constraints that shape human interaction". In this paper, our main focus lies on evasive behavior with respect to formal institutions, but we still acknowledge that laws and regulations can sometimes stand in conflict with the norms, values and beliefs of large social groups (Dowling and Pfeffer 1975; Safran 2003), as well as the fact that evasive entrepreneurs, while defying formal institutions, still operate within informal institutional boundaries, in the sense that their means and ends are legitimate to at least subgroups of society (Webb et al. 2009).

they compete with these firms. Evasive entrepreneurship always borders on the unlawful, but it is also an underestimated and poorly understood source of innovation in the modern economy.

The pace and character of technological development and entrepreneurship are changing, while regulations, regulatory processes and institutions adapt only slowly, if at all, to these changing circumstances. However, the *de facto* functions of existing regulatory frameworks are still affected by changes in their surroundings and need to adapt to remain efficient. For instance, Jenkins (2008) introduced the concept of “convergence culture” to illustrate how different media platforms are becoming increasingly entangled through digitization. Regulatory frameworks set up to regulate the different platforms will also converge and their applications overlap. Consequently, the level of regulatory complexity will grow, as will the risk for institutional contradictions and uncertainties.

We argue that evasive entrepreneurship can be seen as a vehicle of regulatory change; in and of itself, it is a means to test and provoke, as well as to indirectly bring about adaptations in the existing institutional framework. The occurrence of evasive entrepreneurs is a signal that there is a gap or an inconsistency in the regulatory structure being evaded. Regulators can respond by trying to adapt the institution either to accommodate or to remove the evasion. However, the market and institutional outcome of an evasion is a highly interdependent affair that neither entrepreneur nor regulator can fully control on their own. The evasion may end up as a celebrated innovation, or as a criminal offense.

To address these issues, we formulate a conceptual model aimed at illustrating and mapping the interdependencies surrounding evasive entrepreneurship and institutional change. We use this framework to study a recent and well-known case of evasion: That of the file sharing platform The Pirate Bay (TPB). It is arguably one of the most influential and well-known digital Swedish innovations in recent times, and for a while a considerable part of all Internet traffic went through the site’s tracker. Yet the venture always bordered on the unlawful, and regulators eventually decided that it was criminal. Its founders were convicted to jail and received million-dollar fines. A better understanding of this case may be central to interpret how today’s evasive entrepreneurs can challenge and affect regulatory frameworks, and to highlight how (and how not) regulators should respond to such challenges.

The rest of the paper is organized as follows. In section 2, we present a formal definition of evasive entrepreneurship and introduce our conceptual model to illustrate the interdependencies of evasion. In section 3, we present the TPB case, analyzing both the evasive entrepreneurship and the institutional response. The final section begins with a comparison between TPB and other cases of evasive entrepreneurship in order to give the themes discussed in the paper a broader context. We then go on to discuss our results and their implications for policymakers and regulators grappling with the thorny issue of how to deal with evasive entrepreneurs in ways that enhance social welfare.

## **2 Conceptual Framework**

Institutions in high-income countries are relatively good at directing entrepreneurship towards inherently productive purposes, but still bring about many instances of unproductive or destructive entrepreneurship (Baumol 1990). However, what appears to be an unproductive activity may be a second-best substitute for inefficient institutions (Douhan and Henrekson 2010). Institutions become targets for entrepreneurial innovativeness because changing their workings can be a means of earning entrepreneurial profit (Henrekson and Sanandaji 2011).

Inherently profit-driven entrepreneurship can alter the institutional setup (*de jure* and/or *de facto*) and thereby change the social reward structure which, according to Baumol, allocates entrepreneurial talent. Entrepreneurs can do this through two channels: (i) through political entrepreneurship (lobbying etc.) that is directly aimed at altering institutions, and (ii) through the evasion of institutions. In this paper we discuss the second channel, as such evasive entrepreneurship can change the workings of existing institutions, or trigger a response from regulators who alter institutions.

### **2.1 Evasive Entrepreneurship**

The concept of evasive entrepreneurship was introduced in the early 00s by Coyne and Leeson (2004), who describe evasive activities as using resources and efforts to evade the legal system or avoid other agents' unproductive activities. Elert and Henrekson (2015) argue that evasive entrepreneurship constitutes a unique and underestimated form of innovation that – unlike many other forms of entrepreneurship – interacts directly and antagonistically with rules and regulations. They define the concept as a

*“profit-driven business activity in the market aimed at circumventing the existing institutional framework by using innovations to exploit contradictions in that framework”.*

The evasive entrepreneur is thus a combination of a Schumpeterian rule-breaker (Schumpeter 1934; Zhang and Arvey 2009) and a Kirznerian arbitrageur (Kirzner 1973), that is, an agent who breaks rules to gain an advantage relative to other actors and the existing market. Accordingly, if it is successful, evasive entrepreneurship is disruptive to both markets and institutions.

The evasive entrepreneur thrives when institutions are rife with contradictions. Institutional contradictions are best understood as inconsistencies, gaps or loopholes in institutional frameworks. Such contradictions may arise and increase for a number of reasons. For the purpose of this paper, one of the most interesting sources of contradictions is technological development and the way that it alters the conditions that the institutional framework relies on to function properly. Seo and Creed (2002, p. 225–226) describe institutional contradictions as a “complex array of interrelated but often mutually incompatible institutional arrangements” that “provide a continuous source of tensions and conflicts within and across institutions”. Elert and Henrekson (2015) describe three categories of institutional contradictions: (i) inconsistencies in regulation, (ii) lack of regulation, and (iii) complications in enforcement. The direct effect of evasive entrepreneurship is to change the *de facto* effect or function of institutions by exploiting their contradictions.

The innovations of evasive entrepreneurs, like those of any entrepreneur, can be incremental or radical, and some may be sufficiently revolutionary to create a pervasive effect throughout the economy (Freeman and Perez 1988). Since evasive entrepreneurship targets regulations and institutional frameworks directly, it also plays an important role in institutional change. It affects institutional structures not just by evading them (changing the *de facto* effect of extant legislation), but also indirectly by the feedback it generates to policymakers and other market actors. Widespread evasive activities and the existence of large rents earned by evasive entrepreneurs may be interpreted as a signal that some type of institutional reform is needed, either to stifle the entrepreneurial activity or to facilitate its expansion. Governments and regulators seeking to foster entrepreneurial compliance and innovation would do well to have a strategy for how to respond to such signals.

There are several ways in which this feedback can be transmitted to policymakers and ignite institutional change. For instance, a proactive politician may side with the evasive entrepreneur to advocate change,<sup>2</sup> or affected incumbents in the market may seek to rally political or legal support to stop the evasion and thereby initiate an institutional change process. Shifts in public opinion can also serve as a feedback from evasive entrepreneurship. What the public perceives to be fair, legal or moral can have a significant influence on the enforceability of laws and their institutional frameworks, for instance if an evasive entrepreneur offers a service that becomes widely popular or unpopular.<sup>3</sup> How the evasive entrepreneur engages policymakers also constitutes an important source of feedback (more on this in section 2.2).

The characteristics of the evasive activity exert an important influence on the institutional response. According to the Kaldor-Hicks criterion an institutional reform is efficient if the gain from it – at least theoretically – could fully compensate losers (Scitovsky 1941). If evasive entrepreneurial activities are welfare enhancing, they create additional resources *prior* to any reform. These resources may, at least in theory, be used to compensate the losers from the institutional reform, which would facilitate implementation. If, however, an evasive activity reduces social welfare, it is more likely to meet opposition, ultimately resulting in institutional change banning the activity.

The institutional response to the evasion can be divided into three categorical strategies, as lawmakers and regulators can choose to (i) adapt institutions to accommodate the evasive activity and thereby promote competition and market expansion, (ii) remain inactive, i.e., neither enforce nor change the affected legislation

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<sup>2</sup> As an example of such an alliance, consider the spark that ignited the transformation of China's agriculture. It emanated from the actions of a number of farmers in a poverty-stricken village in the Anhui province. In a secret agreement, the farmers decided to divide up the land and allow each household to work on its own. This organizational innovation amounted to a *de facto* privatization, and provided a second-best substitute for the inefficient institutions governing agriculture, amending the perverse incentives created by forced collectivization. While the farmers in theory ran the risk of jail sentences, they had the implicit support of local reform-minded officials, who chose not to enforce the rules of the collective farming system. The subsequent year's grain production in the village equaled the total production in the previous five years. The success of the innovation was propagated through lobbying by local officials and eventually resulted in institutional change that allowed contracts allocating land to households on a long-term basis and gave farmers the right to retain profits (Li et al. 2006).

<sup>3</sup> The importance of such institutional incongruence for affecting institutional change has been discussed by e.g., Helmke and Levitsky (2003).



or regulation, or (iii) enforce current laws and regulations more harshly or even pass new legislation that explicitly outlaws the evasive activity. Often, regulators will mix these strategies over time as part of the interaction with the evader.

Institutional reform may or may not be on the entrepreneur's agenda. On the one hand, agents introducing an evasive activity usually enjoy at least some temporary monopoly power vis-à-vis their competitors as long as regulators remain inactive. On the other hand, institutional change aimed at accommodating innovation and entrepreneurship in the area of evasion, meaning that it is no longer evasive, also removes uncertainties and may improve long-term potential for business growth. While actions aimed at changing the institutional setup are usually thought of as occurring within the political system, the notion of evasive entrepreneurship shifts the focus to institutional disruptions emanating from the market level. From a policy perspective, evasive entrepreneurship may therefore be understood as an alternative to lobbying or activism.

It may in fact be hard to distinguish between motives of profit and motives of institutional change, and for the purpose of our analysis they can be considered to co-exist. That is, evasive entrepreneurs can be driven by both economic and social motives. In the case of the founders of TPB, as we shall see, it does not make sense to study them exclusively as either profit-driven or change-driven.

## **2.2 The Interdependence of Evasion**

The impact of technological development is a complex process involving market actors as well as courts, governmental agencies and legislatures. The idea of a coevolution between law, technology and industry structure is not new (Hughes 1983). Many sociologists who study industry evolution stress that the industry itself strongly molds its own selection environment (Nelson 1995), as a new techno-economic paradigm usually requires a different set of institutions compared to earlier paradigms (Freeman and Perez 1988). Legal structures therefore often need to be modified to accommodate new industries. This was the case for intellectual property rights with respect to biotechnology, and likewise, a number of regulatory matters had to be settled before the enormous potential of electrification could be reaped (Nelson 1995; Hughes 1983). However, the unsustainability of the current system is often not apparent until it is aptly demonstrated by market actors. Etzioni (1987) argues that the social function of entrepreneurship is to provide adaptive reality testing, that is, to alter

societal patterns that have grown obsolete, making them more attuned to the new environment.

Evasive entrepreneurship affects institutions by destabilizing the current *status quo* – the relationship between the institutional structure and the entrepreneurial activity – thereby triggering an institutional response to the evasion. Neither the evasive activity nor the institutional response can by itself determine the outcome of this interaction, since the structure of resulting institutions is too complex to anticipate (Simon 1947; Hayek 1988). Accordingly, it is also difficult to separate deliberate design processes from unintentional, spontaneous institutional evolutionary processes (Hayek 1973; Kingston and Caballero 2009).

Institutional change may create substantial friction. Many actors (such as inventors, firm owners, managers, civil servants and politicians) have a vested interest in the continuation of the existing system (Law 1991) and the regulatory policy of a government often reflects powerful economic interests rather than public needs (Stigler 1971; Peltzman 1976; Buchanan et al. 1980). Furthermore, an important feature of political and economic institutions is their relative inertia (Glaeser et al. 2004; Scott 2008), and empirical research suggests that changes to a more efficient economic policy are usually “delayed”; reforms are not implemented when rational and informed observers would expect them to be welfare enhancing, but substantially later (Fernandez and Rodrick 1991; Drazen 1996). Taken together, these factors may entail both judicial and political friction, contestation and negotiation in what can be described as an “institutional war” (White 1992; Hoffman, 1999; Seo and Creed 2002). The resources and power available to actors are critical to their ability to influence the outcome (McAdam et al. 1988).

As a consequence, an evasive entrepreneur can make the first move towards institutional change, but cannot control the final results. When they are adapted to the evasion, institutions can prompt additional firms to enter into the new market and thereby increase competition. This kind of development may be detrimental to the original evader and even put him out of business. Conversely, simply cracking down on evasive activities may end up hampering overall entrepreneurship, innovation and the ability to leverage new technologies to promote growth.

A hallmark characteristic of an interdependent decision-making process commonly studied in game theory is that the outcome depends not only on one's own choices but also on the choices of the other player(s). With this in mind, we construct a simple model of the evasive interaction. This model should not be considered a static picture, but rather a game board that makes it possible to distinguish the positioning of the entrepreneur in relation to the regulator over time. The interaction between the two players can be likened to a dialogue, where each move is affected by previous moves and by the surrounding context.

		<i>Regulator's decision</i>		
		(Adapt to) Enforce current laws	Remain inactive	Adapt to accommodate
<i>Entrepreneur's decision</i>	Abide by			
	Alter			
	Evade			

When deciding how to act, the entrepreneur's options are listed in the three rows: a) to act as most market actors do and abide by current regulations, b) to act as an institution-altering entrepreneur and try to adapt regulations, or c) to act as an evasive entrepreneur and evade regulations. Upon observing an entrepreneurial act, the regulator has the options listed in the three columns: d) to enforce current regulations (or strengthen them in order to uphold the current state of regulation), e) to remain inactive and let the evasive entrepreneurial activity continue, or f) to adapt regulations to accommodate the activity when it is evasive, that is, legalizing it. Although admittedly crude, this model allows for a better overview of the interdependence of evasion.

For instance, an entrepreneur would probably be happy to evade regulation if she

knows that the regulator will remain inactive (middle bottom box: evade/remain inactive) or will adapt to accommodate the evasion (bottom right box: evade/accommodate).<sup>4</sup> However, if the regulator attempts to enforce current laws, the entrepreneur may have to try either to alter regulation (middle left box: alter regulation/enforce current laws) or to abide by the current state of regulation (top left box: abide by /enforce current laws).

With respect to evasive entrepreneurs, the bottom right box (evade/adapt to accommodate) could be considered an equilibrium that promotes change, since neither the entrepreneur nor the regulator would have wished to change their strategy had they known what the other player would do. The bottom middle box (evade/remain inactive) is a possible equilibrium for the entrepreneur, who essentially has monopoly in his market, but not so for the regulator who will most likely be pressured to take action by incumbent firms or potential competitors if the evasive activity is successful. The top left box (abide/enforce current laws) is an equilibrium that inhibits change.

In game theory, individual payoffs are assigned to each potential outcome, and strategies are analyzed and evaluated based on how well they manage to maximize those payoffs. In this model, assigning specific payoffs while also maintaining the model's general applicability to different cases of evasion would be impossible, not least because of the complexity involved in institutional change. However, it could be argued that the joint payoff of cooperation (abide by/enforce or evade/adapt to accommodate) are higher than the other payoffs simply because they do not require a conflict which would be costly in terms of time and money for both parties. The payoffs are also related to the time-span each player acts on. An entrepreneur may engage in evasive activities to reap quick rewards and then move on, or may do it as part of a long-term strategy to grow and expand his business. An individual policymaker may be solely interested in being re-elected, whereas a government has a long-term interest in upholding and adapting its institutional and regulatory framework to remain globally competitive.

We should also stress that being evasive is not necessarily a constant state over time.

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<sup>4</sup> Oftentimes, having their evasive activities accommodated by regulation is in the interest of entrepreneurs. Sometimes it is not, however, as suggested by Yandle's (1983) notion of "bootleggers and Baptists". Regulations are sometimes supported by groups that want the ostensible purpose of the regulation (Baptists who want to ban liquor sales) and by groups that profit from undermining that purpose (bootleggers who want to eliminate competition).

Rather, an entrepreneur may start out by attempting to alter an institutional structure, but when the regulator remains inactive or resists by enforcing current regulations the entrepreneur may choose to become evasive. Conversely, an entrepreneur may start out as evasive, but switch to an altering strategy if the regulator enforces current regulations in a way that makes it impossible to continue the evasion. Regulators could also proactively reform either to enforce current regulation or to accommodate new types of market solutions, thereby encouraging entrepreneurs to explore the new opportunities or to adapt to a stricter regulation.

Understanding evasive entrepreneurship as part of an ongoing, or iterative, game also opens up for a more general interpretation of how regulators respond to evasion, and perhaps also how they could become better at it. Given that evasive entrepreneurship is unlikely to disappear as long as globalization, urbanization and digitization continue to transform societies and economies, policymakers will need to build consistent long-term strategies to cope with it.

In short, this model provides a basic tool to map cases and to look for best responses to evasive entrepreneurship. Its main purpose is to illustrate and emphasize the interdependent and interactive nature of evasive entrepreneurship and thereby lay down a foundation for further analysis. In the next section we will attempt to apply it to the case of The Pirate Bay.

### **3 The Pirate Bay Case**

#### **3.1 Copyright, Making Copies and Sharing Files**

A copyright is a “property right in an original work of authorship ... fixed in any tangible medium of expression, giving the holder exclusive rights to reproduce, adapt, distribute, perform or display the work” (*Black’s Law Dictionary* 1999, p. 337). Economically, copyrights and other immaterial property rights can be rationalized as means to promote creation and investment, since they enable control of the reproduction and distribution of creative works (Tratos 2007).

Since the ratification of the Berne Convention of 1886 (Monlux 2009), a system of international intellectual property regulations has been established with the help of international agreements. The system has no courts of its own, but is instead based on collaboration between nation states and their legal structures. It is currently protected

by a series of international sentinel organizations, all of which are primarily under the direction of the World Intellectual Property Organization (WIPO), a specialized agency of the United Nations. WIPO currently has 184 member states (Dahlberg 2010, p. 155–156; Burke 2010, p. 70).

The Swedish Copyright Act from 1960 stipulates the absolute right of a copyright holder to control when, where and how a copy is made. Copyright infringement is the use of works protected by copyright law without permission, encroaching on certain exclusive rights granted to the copyright holder, such as the right to reproduce, distribute, display or perform the protected work, or to make derivative works.<sup>5</sup> However, the act mentions a number of so-called *fair use* exceptions.

Notably, temporary copies and private copies can under certain circumstances be made without permission from copyright holders (11§–12§) (Johansson 2010, p. 108; Li 2009, p. 291–292). These exceptions were put in place to acknowledge the implausibility of enforcing a complete ban on “home copying” between friends, and were combined with the so-called cassette tape retribution system, which meant that a levy was paid by manufacturers or importers of storage media to the rights holders’ organization Copyswede. The system worked fairly well for cassette and video tapes since geographical dissemination was limited, making copies was tedious and time-consuming, and the quality declined significantly for every copy of a copy that was made.

The regulatory framework thus worked because it relied on weaknesses or imperfections in the technological infrastructure, rather than the desired behavior of the individuals making copies. However, regulations that rely on technological limitations are not robust to innovation. With the advent of digital content, the Internet and BitTorrent trackers, the setting for home copying suddenly became global while copies no longer deteriorated in quality. Yet the exceptions to the Swedish copyright legislation persisted, and would prove crucial to the story of TPB.

### **3.2 The Pirate Bay as Evasive Entrepreneurship**

TPB is a file sharing website based on BitTorrent technology. It was started in 2003 by Fredrik Neij and Gottfried Svartholm, who were later joined by Peter Sunde and Carl

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<sup>5</sup> The act was amended in July 2005 (through the government bill *Upphovsrätten i informationssamhället*) following the EU decision in 2001 to ban downloading of copyrighted material without permission.

Lundström. TPB has its origins in Piratbyrå (The Pirate Bureau), an organization describing itself as a think tank devoted to a free copy culture. The Pirate Bay founders first established a Swedish BitTorrent tracker, providing a platform for sharing content locally. However, they also realized that because of its unique features, BitTorrent technology would most likely put copyright regulation into a quandary.

Instead of simply copying a file from one hard drive to another, BitTorrent technology allows for a large number of users who all have the same file to aggregate into a swarm, from which an additional user can obtain the file by copying small pieces of it from a large number of users. This is enabled by a tracker that coordinates the different copies of a file (making sure that they are all instances of the same file) distributed in the network of users. The technology provides decentralization, redundancy and robustness to the communication network, since no user is required to rely exclusively on one specific user to complete a file transfer.

From a copyright perspective, the introduction of BitTorrent technology was disruptive, in Sweden and elsewhere. While it was illegal for an individual to freely distribute copies without the consent of the rights holder, it was not evident whether or not it would be illegal to let people copy a small piece of that content from a large number of different sources and assemble them into a complete copy (Rydell and Sundberg 2009, p. 103). More legal ambiguity was created by the fact that the central server need not ever have access to the original file being uploaded by the user, just the tracker pointing to the location of the file (Li 2009, p. 287).

It was Gottfrid Svartholm, then working in Mexico, who set up a BitTorrent tracker for the Pirate Bureau's members (Li 2009, p. 287–288). TPB was hence engaging in evasive entrepreneurship from the beginning: They exploited geographical inconsistencies in copyright legislation and enforcement between Mexico and Sweden by hosting a Swedish file sharing service in Mexico.

The tracker quickly became popular, and in November 2003 it was made public under the name The Pirate Bay. Demand soared quickly, and the tracker was moved to Sweden in early 2004 (Rydell and Sundberg 2009, p. 104). In the winter of 2004, the then-largest BitTorrent site Supernova was dismantled after legal pressure from rights holders. However, demand did not wane. Instead, it relocated to TPB, which quickly became the world's largest tracker.

The actual copying and file sharing was done by the users and their client software, completely independent from TPB, although the tracker made everything significantly more efficient and easier. At one point as much as 70 percent of the world's torrents, i.e., the meta data files that coordinate all instances of a specific version of a file, were estimated to be trafficked through TPB's tracker – a considerable part of the world's internet traffic. Even though copyright infringement on a large scale was taking place, TPB's moral and legal responsibilities were not entirely clear (Snickars 2010, p. 342). This can be explained by a number of institutional contradictions that TPB successfully exploited.

First, TPB benefited from institutional inconsistencies, both in terms of geography and of implementation of regulation. If different nations or states have different rules, an entrepreneur can benefit from institutional arbitrage by locating where rules are less binding or less enforced, provided that there is free movement. In Tratos' (2007, p. 217) words, "because the Internet knows no state or country boundaries, the laws of states and countries other than the physical location of the Internet publisher or broadcaster may apply, particularly where the audience or market exists in a locale other than the location where the materials are being placed onto the Internet." The first TPB tracker was hosted in Mexico to avoid legal scrutiny, and TPB's servers would subsequently also be relocated as an additional evasive measure (Rydell and Sundberg 2009, p. 104).

As a file sharing platform, TPB also benefited from the aforementioned grey area in previous copyright regulation that allowed for "home copying" between friends (which can in turn be interpreted as a regulatory accommodation to an inconsistency based on the implausibility of enforcing a complete ban on making copies and giving them to friends). This exception was of little consequence for cassette and video tapes since making copies was costly, occurred locally and led to a reduction in quality. With digital content, the Internet and BitTorrent trackers, the setting for home copying suddenly became global and copies did not deteriorate in quality.

Second, TPB benefited from institutional contradictions due to a lack of regulation. As mentioned previously, the legal implications of copying a file by downloading a series of small pieces from a large number of different users and putting them together were not clear (Rydell and Sundberg 2009, p. 103) simply because this had previously not been a viable option for making copies. New technology had enabled a new practice



for which there was no regulation, and legislation was lagging behind. For a long time, Sweden had comparatively lenient laws concerning piracy (Wikström 2009, p. 9), and the country increasingly gained notoriety as “a piracy safe haven”, and a reputation as a rouge nation with respect to illegal file sharing (Brooks 2006). Burke (2010) argues that by the time any legal actions were taken against file sharing the practice had already become deeply entrenched in Sweden’s technological culture (cf. Norton 2006b).

Evasive entrepreneurs can consciously shape their innovations so as to slide through these cracks in the legal system. Prosecutor Håkan Roswall observed in an internal memorandum in 2005 that the TPB founders had obviously studied Swedish copyright legislation in order to exploit its potential flaws and thereby “obstruct prosecution”. The TPB founders counted on not being convicted for copyright infringement due to the fact that they did not actually store any copyrighted material on their servers, or actively disseminated such material. They also felt protected from suspicion of accessory to copyright infringement due to the BitTorrent technology; since each person in the data swarm shared only fragments of copyrighted material that were useless on their own, it seemed doubtful that anyone could be convicted for breaking the copyright act. The prosecutor made the same observation (Rydell and Sundberg 2009, p. 129).

Third, TPB had the advantage of an institutional contradiction based on enforceability. If file sharing were to be considered a crime, it was not TPB but all of its users that committed that crime. Accordingly, in order to enforce the regulation, authorities and rights holders would have to engage in legal processes against each individual, or as it was repeatedly framed in the public debate, the government would have to label an entire generation of young people criminals.<sup>6</sup> Furthermore, as Hinduja (2012, p. 242) observes, the fact that laws are in place that outline the illegality of copyright infringement and prescribe punitive sanctions for their transgression is largely meaningless unless interpreted in light of the effect these laws have on the people for whom they are intended to apply, that is, what legitimacy these laws enjoy. A great many people engaged in file sharing at the time, and they did not consider copyright infringement morally wrong (Larsson 2010, p. 190). Notably, few Swedes saw (or see)

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<sup>6</sup> “Our view is that copyright legislation should be protected, but we do not want to criminalize an entire youth generation,” Swedish Prime Minister Fredrik Reinfeldt stated in a debate (SVT 2008).

file sharing as a serious crime, or even as a crime at all. Andersson and Snickars (2010, p. 36) argue that this was an important factor for TPB's success. In addition, the media attention that TPB received both prior to and during the trial against its founders possibly promoted their causes of shaping public opinion and of profiling themselves as (benevolent) evaders or rebels.

Fleischer (2010) describes TPB as an assemblage of "hardware, software and humans". The technology mainly consisted of the servers, a search engine, a torrent file archive, a tracker, a popular site, a blog and a web shop. In essence, it only enabled transactions of digital content by connecting and coordinating a distributed network of users – in short, by matching supply and demand. Together with the network of users, the BitTorrent technology blurred the borders between up- and downloading (Fleischer 2010, p. 263) and consequently challenged the institutions around copying and copyright infringement. Schollin (2010, p. 224) accordingly argues that the openness and scope of TPB was its strength, while the users were its value. This brings us to the importance of how the TPB founders handled their end of the evasion.

It would later be a central part of the legal case built against TPB to argue that it was profit-driven, notably by advertising revenue from the website.<sup>7</sup> However, the founders were clearly driven by more than profits and for the analysis at hand the non-profit motives behind TPB are equally important, if not more so. The TPB founders can be aptly described as a type of entrepreneurial activists, driven by a desire for social change as part of the anti-copyright movement. The name of the site not only underscores its ideological agenda, but also makes the evasiveness of TPB quite apparent, as the practice of labeling those who infringe on copyright legislation as pirates dates back to at least the early 1600s (Dekker 2000). Although TPB clearly had a political agenda, they avoided traditional ideological and partisan associations (Andersson and Snickars 2010, p. 33–34).

The TPB founders did not primarily lobby policymakers directly to induce them to accept or adapt to the new technology. Instead, they engaged in lobbying the public

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<sup>7</sup> The founders claimed that they had only earned small amounts, but were unwilling to disclose anything about the site's profitability. In the subsequent trial, the prosecutor concluded that the site through the years had generated SEK 1.2 million in advertisement revenues (Rydell and Sundberg 2009, p. 136–137). Given the widespread use of their innovations, this appears very modest. Then again, it has been observed that innovators are only able to capture a few percent of the total surplus from their innovations (Nordhaus 2004; Baumol 2010, p. 51).

directly and in building an activist movement around TPB. It is important to remember that while TPB was not the first popular BitTorrent site it was unprecedented among them as a standard bearer for a cause – a quite aggressive line of copyright reform or even copyright abolition. Hence, while legal pressure from the copyright industry had induced previous sites like Supernova to close down, the TPB founders instead took an offensive stance (Rydell and Sundberg 2009, p. 107–109). TPB became notorious for openly embracing piracy and for ridiculing threats of legal actions from copyright organizations and media companies by posting their complaints and cease-and-desist letters on its website (Lewen 2008). During the trial against them, the TPB founders maintained their aggressive strategy and together with the think tank Piratbyrån rallied followers in an online event named “spectrial” to protest the trial, calling it a political spectacle (Hässler 2009).

TPB sold merchandise and received donations from its users. It seems that this voluntary financing rested on a foundation of trust tied to TPB’s symbolic value, which in turn depended on how the site and its founders were perceived (Fleischer 2010, p. 264). For instance, the rebel image of TPB was tarnished when it was confirmed in 2007 that the site had received financial support from Carl Lundström, who was also known for financing far-right political movements in Sweden (Jibbenga 2007; Rydell and Sundberg 2009, p. 107). Furthermore, the importance of the perception of TPB as motivated by non-pecuniary goals was clearly demonstrated in 2009, as news broke out that the founders were trying to sell the domain name. Although the deal was ultimately called off, it damaged the symbolic value of TPB as a non-commercial net community, and substantially undermined the site’s popular support (Fleischer 2010, p. 264–265).

### **3.3 The Institutional Response to TPB**

The evasion enabled by the BitTorrent technology disrupted the content distribution industry and TPB became the global figurehead of this evasion. The actual effects of file sharing on record and movie sales were (and remain) unclear, however. On the one hand, it was argued that downloaded copies displaced physical record and film sales. On the other hand, file sharing made it easier for consumers to discover new content and increased the exposure of small and independent artists in a manner similar to that provided by services like YouTube today. Andersson and Snickars (2010, p. 29–31)

and Söderberg (2010) argue that unregulated file sharing should not be considered to be in opposition to the market ecosystem, but a complement to it.<sup>8</sup>

Nevertheless, global incumbents in the copyright industry took action against TPB. Industry actors condemned digital music piracy, sued software services and individual file sharers while also lobbying for stricter laws and harsher penalties (Dean 2003a; Hinduja 2012, p. 243; Burke 2010, p. 69–70; Brown 2008). Sweden was no exception. Prominent anti-piracy organizations active in Sweden were (and are) Antipiratbyrån, Business Software Alliance, the International Federation of the Phonographic Industry (IFPI) and the Motion Picture Association (MPA), which is the international branch of the MPAA.

The impetus for institutional response in Sweden did not only come from Swedish actors. According to district prosecutor Håkan Roswall, the U.S. government threatened to apply sanctions against Sweden within the WTO framework (Rydell and Sundberg 2010, p. 130–131), but this claim was later denied by the Swedish government. Meanwhile, the MPA's executive president John G. Malcolm wrote a letter to Swedish state secretary Dan Eliasson in March 2006, stating:

As I am sure you are aware, the American Embassy has sent entreaties to the Swedish government urging it to take action against The Pirate Bay and other organizations operating within Sweden that facilitate copyright theft. As we discussed during our meeting, it is certainly not in Sweden's best interests to earn a reputation among other nations and trading partners as a place where utter lawlessness with respect to intellectual property rights is tolerated. I would urge you once again to exercise your influence to urge law enforcement authorities in Sweden to take much-needed action against The Pirate Bay. (Mennecke 2006)

The same month, the Swedish Justice Department drafted a directive, signed by Minister for Justice Thomas Bodström, encouraging the National Police Board and the

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<sup>8</sup> It is unclear to what extent the decline in record sales in Sweden and other countries (IFPI 2012) can be attributed to file sharing. Swedish record sales did not fall at all during the preceding Napster era, and the Swedish industry's aggregate revenue remained roughly unchanged despite the advent of TPB, with live sales going up (Schollin 2010, p. 214). Claims about revenue losses due to piracy are often based on the assumption that most unauthorized copies would be replaced by the sale of a legitimate product if it were not for file sharing (Cammaerts and Meng 2011). For example, in the 2009 trial, when record and movie companies demonstrated how much they "should" have been paid for each download of their protected works, they used a calculation method which if applied consistently would mean that the value of the files shared through TPB would amount to hundreds of billions of SEK (Larsson 2010, p. 189; USD 1  $\approx$  SEK 7 in 2006–2007). Evidently, this is widely off the mark, since it is based on the implicit assumption that the price elasticity is zero (Oberholzer-Gee and Strumpf 2007, p. 4).

Swedish Prosecution Authority to take joint action to combat intellectual property crimes more efficiently (Rydell and Sundberg 2010, p. 130–131). TPB was not mentioned explicitly by name, as that would have amounted to ministerial rule in a specific case, which would have been a violation of the Swedish constitution.

A raid against TPB took place on May 31, 2006. Swedish police seized TPB's servers and arrested two of its founders (Rydell and Sundberg 2010, p. 127–131). It has been suggested that the raid was at least partly undertaken due to pressures from the U.S. government and from the MPAA (Norton 2006b). MPAA was triumphant in a press release, where they said that: "Intellectual property theft is a problem for film industries all over the world and we are glad that the local government in Sweden has helped stop The Pirate Bay from continuing to enable rampant copyright theft on the Internet" (MPAA 2006).

Prior to the raid, Peter Sunde and Fredrik Neij had managed to make almost complete backups of the TPB site before it went offline (Norton 2006b; Rydell and Sundberg 2010, p. 135). Consequently, TPB reappeared only three days later, openly mocking the police for its inability to keep the site closed.

The raid also had far-reaching unintended consequences. First, the increased attention doubled the number of TPB users (Norton 2006a). Second, TPB changed its structure following the raid, becoming more decentralized and evasive. The founders first relocated their servers to Russia and the Netherlands and later spread them across the world, making sure that not even the people in the inner circle knew where the machines were located. Third, the raid propelled the newly founded Pirate Party to media prominence (Rydell and Sundberg 2009, p. 136), giving it a kind of publicity that money could not buy: Its website became one of the most visited in the world during the first week of June 2006, and membership increased from 2 200 to 6 600 people.

Unrelated to, but fueled by TPB, the Swedish Pirate Party was founded in 2006. After the raid it was followed by parties in other countries, notably in Austria and the United States, and by 2009 there were Pirate Parties in 20 nations around the world (Li 2009, p. 289). The site [pirate-party.us](http://pirate-party.us) had 100 000 visitors in its first week. Founder David Segal said in an interview (Milchman 2006): "I think the raid is what brought this whole thing to my attention, and to the attention of people around the world. The raid

in Sweden could turn out to be the best thing that happened to the internet community.”

The Swedish Pirate Party initially demanded a complete abolition of copyright, but soon became more pragmatic.<sup>9</sup> Copyright legislation was to be reformed and limited to five years, and to not cover non-commercial uses (Rydell and Sundberg 2010, p. 119, 143). The evidence strongly suggests that the Pirate Party’s success in the June 2009 election to the European Parliament – where they got 7.1 percent of the votes and one seat – was intimately tied to what happened to TPB.

The attention given to copyright issues also rubbed off on the policies of other Swedish parties. Even established center-right parties (like *Folkpartiet* and *Moderaterna*) began to question traditional copyright protection and its legal framework (Andersson and Snickars 2010, p. 12). Other parties in Sweden have adopted many of the issues and views advocated by the Pirate Party (Li 2009, p. 289–290), albeit with different emphases on individual freedom and integrity, a modified copyright protection, and net neutrality. The debate on file sharing and the media exposure that the Pirate Bay was enjoying nationally and internationally hence appears to have had considerable effect on policymakers. The TPB case arguably pushed most parties into endorsing the view that copyright law is in need of some form of “modernization” (Andersson and Snickars 2010, p. 18–23).

In parallel with the growing partisan interest in copyright issues, TPB went to court. In January 2008, at a time when TPB was one of the world’s 100 most visited websites, the prosecutor decided to charge its frontmen Peter Sunde, Fredrik Neij, Gottfrid Svartholm and Carl Lundström with complicity in and preparation to crimes against the copyright act (Rydell and Sundberg 2009, p. 137). One of the main issues for the prosecution was the technology. Convicting any of the accused as an accessory of a copyright crime required that the crime had in fact been committed. With the BitTorrent technology this was still far from evident, a fact that lies at the very heart of the evasive entrepreneurship behind TPB. It could be argued that the prosecutor “hedged” his bet by including the label preparation to crime against the copyright act

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<sup>9</sup> Li (2009, 289-290) defines the core issues of the Pirate Party as follows: First, a fundamental reform of the copyrights system; second, an abolition of the patent system; and last, increased respect for personal privacy.

(Rydell and Sundberg 2009, p. 216–217). In this respect, the legal action represents an institutional response towards strengthening and enforcing current regulations.

The joint criminal and civil prosecution that was labeled “the copyright dispute of the decade” started on February 16, 2009 in Stockholm’s district court. The verdict was reached on April 17, sentencing all four defendants to one year in prison and a total of SEK 30 million in fines and damages. The appeal trial in 2010 shortened the sentences of the three defendants who appeared in court that day. (Svartholm did not appear, citing health reasons. He would later flee the country.) However, the fines were raised to SEK 46 million. In 2012, the Supreme Court of Sweden refused to hear an appeal in the case.

Returning to the game board presented in section 2, the interaction between TPB and the government follows a straight path to conflict in the bottom left corner (Evade/Enforce). TPB adopted an evading strategy, and they also signaled that they have no interest in moving to an altering strategy. For instance, they publicly discredited and ridiculed warnings and seize-and-desist orders they received, thereby effectively burning their bridges to alternative strategies. This may have contributed to building their political movement among the general population. However, it also tied them to the mast with their evading strategy and made them an antagonist, among legislators and policymakers in the institutional framework. Regulators were initially passive (Evade/Remain inactive), but soon moved towards an enforcing strategy (Evade/Enforce). At least partially, they were pushed to make this move by incumbents and by other governments lobbying for it. Consequently, the game was reduced to a zero-sum game and a purely antagonistic conflict where a positive payoff for one player corresponds to a negative payoff for the other player. Assuming that both parties, knowing each other’s choice of strategy, would have preferred or at least been ambivalent about another outcome, it could be argued that this state of affairs is not an equilibrium outcome.

		<i>Regulator's decision</i>		
		(Adapt to) Enforce current laws	Remain inactive	Adapt to accommodate
<i>Entrepreneur's decision</i>	Abide by			
	Alter			
	Evade	② ←	①	

#### 4.4 Subsequent developments

Following the legal developments related to TPB and file sharing, many authors worry about tendencies towards a more institutionally sanctioned, regulated Internet, in conflict with other democratic principles (e.g., Andersson 2010, p. 69; Fleischer 2010, p. 276; Söderberg 2010, p. 252). Rydell and Sundberg (2009) point to the trend that the control apparatus has increasingly relocated outside of the democratic system, as copyright holders and their representatives increasingly participate in police work.<sup>10</sup>

In the 00s, the European Union also greatly strengthened its copyright legislation (Larsson 2011) and the EU directive Ipred prescribed a general increase in penalty levels. Ipred was passed by the Swedish parliament in 2009. This feature of the EU Copyright Directive is among the most contentious, and its implementation was met by considerable resistance in Sweden (Larsson and Larsson 2010). The introduction of the Ipred legislation in Sweden initially reduced the number of file sharers, but the decline turned out to be temporary. In fact, a poll in October 2009 showed that TPB rulings and the strengthened Ipred legislation did not affect Swedish attitudes to illegal

<sup>10</sup> Such was the case both at the TPB raid and in the so-called Linköping Case, when the Anti-Piracy Bureau searched a man's computer. The latter case also illustrates the tendency to harsher sanctions for copyright crimes, as the man received a conditional sentence and a substantial fine. The conditional sentence, in turn, made it possible to use harsher means against file sharers more generally, including police searches of their lodgings (Rydell and Sundberg 2010, p. 198–200).



downloading of movies. 75 percent of all young people engaged in file sharing in 2009 (Andersson and Snickars 2010, p. 10–12), and although the original TPB website is only occasionally active, a popular clone of the site still ranks as one of the most popular Torrent sites on the Internet (Torrentfreak 2015).

If anything, it would appear that the difference between formal legislation and informal norms among users increased with respect to file sharing in the years since TPB trial. Lundblad (2010, p. 132–133) argues that ineffective court rulings have unfortunate consequences: The law is ridiculed when TPB is declared illegal but nothing happens. Arguably, the likelihood that legislation will survive is low if a large proportion of all citizens decide to circumvent it (Ekström 2010, p. 82)..

An important question is then whether it is at all possible to regulate and enforce a more restrictive and more encompassing copyright protection (Larsson 2011 p. 190). It appears that the institutional contradictions that TPB relied on in its evasion are growing more apparent and troublesome to ignore or counteract. This ought to act as an important signal to regulators. The outcome of evasive entrepreneurship is indeed interdependent, and there is no guarantee that opting for stronger enforcement will have the intended effect. And if it doesn't, moving out of that position may prove to be difficult.<sup>11</sup>

## **4 Discussion**

Studying TPB as a case of evasive entrepreneurship proves to be fruitful not only to understand the case as such, but also to further explore the interdependencies of evading institutional structures. There are two sides to the evasion, and they depend heavily on each other.

The TPB founders chose an offensive evasion strategy aimed at ridiculing existing regulation and mustering public opinion for their cause. This made it harder for regulators to respond to their evasion without turning the interaction into an

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<sup>11</sup> Among suggested reforms of the copyright system in a liberalizing direction is the idea of freeing up creative works sooner by requiring that copyright holders pay a fee at frequent intervals to keep their rights (Lessig 2008). Another suggestion is to impose a levy or tax to compensate copyright holders for revenues lost due to media piracy (Ekman 2006). Such a levy could be collected in a manner similar to the television license fees in many EU countries. Suggestions have also been made to impose levies on broadband connections and/or taxes on ISPs, and then distribute the proceeds to rights holders (Burke 2010, p. 89). Yet another solution would be a private license for free distribution and downloading, a measure that would mean more money to copyright holders if it was combined with a quantity-based payment scheme (Johansson 2010, p. 115–117).

antagonistic conflict. It should also be noted that the Swedish government had to shape their strategy with respect to international copyright agreements, which further restricted their scope of action. In response, the Swedish government eventually chose to take the measures necessary to strengthen the current regulation and convict the people behind TPB in court, i.e., they adapted to enforce the existing regulation.

It may be tempting to draw the conclusion that the outcome was inevitable, but doing so would be to ignore that the international laws and regulations are also subject to change and evasion. Moreover, the outcome neither resulted in a complete eradication of the evasive activity nor in adamant law enforcement. TPB is still online and file sharing with BitTorrent technology continues. Thus, the issue is still far from settled. It could furthermore be argued that file sharing, and TPB in particular, sowed the first seeds for a market for digitized content. Actors like Netflix and Spotify later moved in to capitalize on this market and became attractive alternatives to file sharing by providing customers with streaming options, freemium business models and low prices.

In a sense, TPB is one of the most significant and successful Swedish innovations in the last 50 years. It is therefore remarkable that both regulators and entrepreneurs seem to have ended up with the short end of the stick. The entrepreneurs have been sentenced to jail and forced to pay large fines. Meanwhile, Swedish policymakers appear to be no closer to establishing an institutional framework that can gain the legitimacy of a new generation of file sharers and leverage the potential of the Swedish information economy to promote further innovation. This raises the question of how policymakers should respond to evasive entrepreneurship in order to promote its advantages while inhibiting its potentially negative consequences.

#### **4.1 Alternative Endings?**

The TPB case could have played out differently. To see this we make a comparison with other cases of evasive entrepreneurship. Specifically, we focus on how they differed in their approach and interdependencies.

First, consider the introduction of commercial television in the 1980s. At the time it was illegal to broadcast commercial TV to Swedish households. However, the entrepreneur Jan Stenbeck and his holding company Kinnevik were able to exploit several institutional contradictions to evade and challenge the regulatory framework in

order to introduce the channel TV3 (Ewertsson 2002). The president of Kinnevik made the following statement in the company's 1987 Annual Report 1987 (Ewertsson 2002, p. 5, authors' translation):

In our entrepreneurial efforts we look for business opportunities with high initial thresholds, high future growth preferably driven by new technology, and an oligopoly-oriented competition situation. These opportunities are often found close to the public monopolies, which is also the case for several of Kinnevik's new companies.

More specifically, the firm exploited the following two institutional contradictions. First, the regulation of TV and radio transmissions had yet to be adapted to the emerging satellite technology, which made it possible for TV3 to transmit TV-signals to Sweden from space out of a head office in London, where it had been located at least in part due to favorable legislation (Ewertsson 2002, p. 6–8). Second, Kinnevik exploited an exemption in the ban on commercial TV that allowed cable TV networks consisting of up to 101 subscribers. They did so by establishing Finvik AB, a company that supplied central cable receiver facilities that served no more than 100 households at a time (Ewertsson 2002, p. 9).

The strategy worked. The Swedish Cable Board ruled that TV3 had not broken the cable law and that it was allowed to continue its operations, with a member of the board observing that the channel's commercials could not be banned unless new legislation was enacted. A government commission was launched with the purpose of exploring options for the future of this field (Blomberg and Larsson 1990). The commission eventually concluded that it was no longer beneficial to ban commercials on Swedish television in view of the new technological landscape. The stringent measures required to achieve this goal would jeopardize other television-related political priorities (Jörnmark 2013, p. 120–125).

Unlike TPB, Kinnevik was a financially strong and well-established market actor, which could alternate between an evading and an altering approach. Ewertsson (2002, p. 2–3) argues that Stenbeck and Kinnevik needed to “link together several different components to a consistent and complete system: programs (content), individuals, and organizations were to be combined with relevant technological, economic, legal, social and political skills” and that “new large-scale socio-technological combinations like TV3 needs wide social and financial support as well as political legitimacy to survive.”

If TPB had followed a track similar to that of TV3, it could arguably have ended up in a position closer to that of Spotify (a freemium music streaming service that negotiates with rights holders to provide their content in return for compensation based on listening frequencies, subscription fees and commercial revenues). Although the BitTorrent technology is highly decentralized, the platform, search engine, top lists and commercial banners could have been used to shape an extended business model. With such an approach, the regulatory response may also have looked very different. However, given the idealistic or ideological motivations behind TPB, it is doubtful that the founders even considered this. Where Kinnevik alternated between altering and evading, the founders and operators of TPB essentially adhered to an offensive evasive strategy until the end, perhaps hoping that it would indirectly lead to institutional change if they succeeded.

New business types are leveraging digital solutions to introduce new types of service-providing platforms. Uber for example, provides a matching of supply and demand of transport services in cities around the world. Each driver has her or his own business, while Uber vets the drivers, provides an app that connects them to riders, handles payments (and claims a fee) and allows both parts to rate each other transparently to promote good behavior. In a similar way, Airbnb provides a platform for leasing and renting temporary housing. Again, both residence owners and guests can rate each other and Airbnb handles the payment and claim their share. Uber is not a taxi company, but it competes with taxi companies. Airbnb is not a hotel, but it competes with hotels.

Both Uber and Airbnb are prominent examples of contemporary evasive entrepreneurship. Like TPB they are global in reach, but unlike TPB they are local in use. That is, they may encounter different regulatory responses in different cities and thereby get very different outcomes of their evasive activities. Both companies appear to have followed a strategy of maximizing the number of establishments, and users from all over the world have been able to use the services. In the wake of conflicts with incumbents and negative regulatory responses, both companies are now mixing their evasion with altering strategies and increased lobbying. For instance, Uber's low-cost service UberPop has been banned in France, Germany and Italy, while the company is involved in legislative conflicts in several other locations (Nguyen 2013). In 2015, the Swedish court Hyresnämnden ruled that housing associations have the

right to forbid its members to rent out their apartments via Airbnb (Goldberg 2015). The service also faces restrictions and regulatory responses aimed at enforcing current regulations in countries such as Spain and Germany (Hellekant 2015b). However, in other countries the regulatory responses have been more forthcoming, with laws being adapted to accommodate the service to different degrees (Coldwell 2014).

Because of their geographically localized submarkets, Uber and Airbnb can learn iteratively from the regulatory response in each country and city. To a lesser extent this was also the case for Kinnevik. Stenbeck's venture attempted to establish TV3 in several Scandinavian countries simultaneously and could also draw on experiences from a previous attempt in Luxembourg (Ewertsson 2002, p. 5, 8–9). This adds an important dimension to the evaders' strategy. Like a chess game, the outcome may not be known from the start, but there are a set of standard openings that each player can learn to relate to. Furthermore, these companies can leverage success from one place across the entire global market, giving them an extremely valuable source of data, business knowledge (largely tacit and therefore difficult to imitate), and arguments for their cause.

Uber and Airbnb initially engaged exclusively in evasive behavior, but as a reaction to unfavorable regulatory responses, they complemented the evasion with altering strategies, such as lobbying and efforts to win the public opinion. Airbnb has also espoused an abiding strategy by adapting their service to collect and forward local taxes, with Paris being a prime example (Hellekant 2015a).

All in all, it is evident that evasive entrepreneurship takes different forms depending on the context in which it occurs. In many cases entrepreneurs choose to mix evasion with altering or even abiding strategies. What makes TPB stand out is that it was based solely on an offensive, evasive strategy. In that respect, it resembles activism to a greater degree than the examples discussed in this section.

## **4.2 Concluding remarks**

Entrepreneurship is shaped by institutions, but also influences them. On the one hand, entrepreneurs choose how to employ their entrepreneurial talent depending on the incentive structure as determined by relevant rules and regulations. In this way, and as highlighted by Baumol in his classic 1990 paper, institutions fundamentally determine the distribution of this talent across productive, unproductive and destructive activities.

On the other hand, entrepreneurs respond actively to the environment they face, which tends to affect institutions. The TPB case forcefully illustrates the latter effect.

Legislation and policymaking processes have remained largely unchanged while digitization and technological development rapidly and profoundly have transformed the fundament of many markets and with that the preconditions for entrepreneurship. This increasing tendency of policymaking to lag behind technology-driven innovation and entrepreneurship is a serious problem for at least four reasons.

First, entrepreneurs and innovators may not be able to afford to wait for policymakers to adapt regulations and give the green light to new ventures, which implies that evasive entrepreneurship may become an increasingly necessary solution for entrepreneurs in order to test new ideas in highly dynamic markets. Indeed, in a conference on the sharing economy in 2013, Kevin Laws of the site AngelList (which unites startups and investors) said, “the approach almost all startups take is to see if they can be successful fast enough so they can have enough money to work with the regulators” (Santa Clara High Tech Law Journal 2013).

Second, if regulatory frameworks are updated too slowly, it may become increasingly complex to interpret whether a specific innovation or venture is legal, that is, determine what laws apply and how they should be interpreted. This holds especially true for digital, data-driven services that combine different data sources across sectors of the economy or across national borders since they may end up with regulatory inconsistencies or difficulties to comply with several different or fragmented sets of regulations. Such increased institutional uncertainty is likely to become an impediment to firms that cannot afford the legal process to find out whether their business model is legal.

Third, if the gap between regulation and technological development continues to grow so that old regulations need to be increasingly bent to apply to new technological innovations, there will be a rising level of noise in the interaction between regulators and entrepreneurs. Consequently, they will have a harder time communicating and finding common ground.

Lastly, the supply of entrepreneurship is arguably affected by the institutional response to entrepreneurship. If policymaking and legislation appears to inhibit entrepreneurship or make it an increasingly insecure activity, this will also influence

how potential entrepreneurs choose to channel their efforts. Thus, slow institutional adaptation may not only hold back or slow down technology-driven entrepreneurship; it can also reduce the number of entrepreneurs willing to put in the necessary effort to overcome these thresholds.

All in all, not only do we argue that evasive entrepreneurship is an underestimated and unique source of innovation and economic development. We also conclude that a crucial factor lies in finding appropriate response strategies for regulators and policymakers. If this fails, large parts of the potential benefits of evasive entrepreneurship are unlikely to be reaped. The Pirate Bay is a case in point: While it was ultimately determined to be unlawful, the venture nevertheless paved the way for a digital content market that has changed dramatically in the wake of file sharing.

Entrepreneurial activities cannot be classified as socially wasteful without a contextual understanding of the way they interact with the institutional setup. *Prima facie*, it seemed obvious that file sharing of music and films over the Internet should be banned in order to safeguard incentives in the entertainment industry. However, as we have seen the challenge from file sharing forced the industry to develop new business models for the distribution of music and film adjusted to the new technology. As a result, consumers can now benefit from highly valuable and flexible services at very low prices compared to before. Thus, evasive entrepreneurship can offset deficiencies in the existing institutional framework, trigger policymakers to adapt regulation, and force incumbents to adapt to a changing market.

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