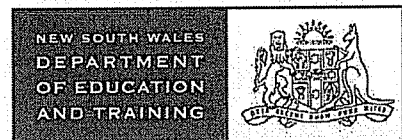


COPYRIGHT ADVISORY GROUP
SCHOOLS RESOURCING TASKFORCE

MINISTERIAL COUNCIL ON EMPLOYMENT, EDUCATION,
TRAINING AND YOUTH AFFAIRS



Early Childhood and Primary Education
Secondary Education
Technical and Further Education
Vocational Education and Training
Higher Education
Adult and Community Education

31 January 2007

Mr John Laughlin
Acting Director
Transport & Prices Oversight Branch
Australian Competition and Consumer Commission
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Melbourne VIC 3001

By email: john.laughlin@accc.gov.au

Dear Mr Laughlin

**Copyright Licensing and Collecting Societies: A Guide for Copyright Licensees
Draft for Comment, November 2006**

Please find attached our submission to the Australian Competition & Consumer Commission in response to the Copyright Licensing and Collecting Societies: A Guide for Copyright Licensees: Draft for Comment, November 2006.

This submission is made on behalf of the Copyright Advisory Group to the Schools Resourcing Taskforce (SRT) of the Ministerial Council on Education, Employment, Training and Youth Affairs (MCEETYA).

If you have any questions, please contact me on (02) 9561 8876 or by email: delia.browne@det.nsw.edu.au

Yours sincerely

A handwritten signature in black ink, appearing to read "Delia Browne". The signature is fluid and cursive, with a long horizontal stroke extending to the right.

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**THE COPYRIGHT ADVISORY GROUP TO THE SCHOOLS
RESOURCING TASKFORCE**

OF THE

**MINISTERIAL COUNCIL ON EDUCATION EMPLOYMENT TRAINING
AND YOUTH AFFAIRS**

**Submission to the Australian Competition
and Consumer Commission**

***"Copyright licensing and collecting societies:
a guide for copyright licensees"***

January 2007

An introduction to the Copyright Advisory Group

This submission is made on behalf of the Copyright Advisory Group to the Schools Resourcing Taskforce of the Ministerial Council on Education, Employment, Training and Youth Affairs (CAG). CAG is responsible for copyright policy and administration for the Australian school and TAFE sector (including the management of obligations under educational statutory licences), and represents almost all primary and secondary school educational authorities in Australia. CAG members include State and Territory Departments of Education, all Catholic Education Offices, the Independent Schools Council of Australia, and the great majority of TAFE colleges.

CAG and its members have a significant interest in copyright law and policy. In 2006 Australian schools (government and non-government) and TAFEs (excluding Victorian TAFEs) paid \$75.6 million in licensing fees to copyright collecting societies for statutory and voluntary copyright licences for the use of copyright materials in schools and TAFEs. This figure does not include any amount that individual schools or TAFEs may have spent in obtaining direct licences for copyright materials.

CAG members place a great deal of importance on the appropriate administration of copyright in Australian schools, and ensuring system and school-level compliance with educational exceptions and statutory licences. CAG works with administrators and teachers to ensure that the rights of copyright creators are respected, and that teachers and support staff have practical guidelines to facilitate the greatest possible compliance with the copyright licences granted to schools.

CAG recognises the importance of providing sufficient incentives to copyright owners, and the importance of the exclusive rights granted to copyright owners. However, CAG also supports the need for an appropriate balance in copyright law, and recognises the strong public benefits in public access to information, particularly for educational and cultural purposes.

The Copyright Amendment Act 2006

CAG supports the amendments to the *Copyright Act 1968* introduced by the *Copyright Amendment Act 2006*, including the ability of the Copyright Tribunal (Tribunal) to have regard to Australian Competition and Consumer Commission (ACCC) guidelines and the potential involvement of the ACCC in Tribunal proceedings.

Copyright licensing and collecting societies: a guide for copyright licensees

CAG was pleased with the prompt release by the ACCC of the *Copyright licensing and collecting societies: a guide for copyright licensees* (the Guidelines). The Guidelines have the potential to be an important tool for owners and users of copyright material (and their representatives).

CAG notes that the Guidelines are directed towards voluntary licences. However CAG believes that the Guidelines could affect decisions in relation to statutory licences as the approach taken with voluntary licences will have a strong influence on the approach taken with statutory licences. Therefore, CAG would like to take this opportunity to inform the ACCC of its experiences in administering the education statutory licences.

It is generally acknowledged that collecting societies occupy a monopoly position and that this is potentially a basis for concern. For example, in the ACCC's recent determination in respect of Australasian Performing Right Association Limited's (APRA) application for authorisation,¹ the ACCC stated:

'APRA has a virtual monopoly in respect of performance rights licences in Australia. Its input and overseas arrangements significantly limit any realistic prospect of music composers and users dealing directly in respect of performing rights in most instances. ... This concentration of members' rights exclusively with APRA means that APRA would be able to set prices for access to its repertoire without consideration as to what the economically efficient price of those rights would be. Indeed, unconstrained, music users would be forced to deal with APRA on whatever terms it saw fit, including in respect of licence fees and types of licences offered.'

The potential abuse of the monopoly power held by collecting societies is a cause for concern by CAG.

In CAG's experience, some collecting societies are more inclined than others to engage in meaningful discussions to achieve a negotiated outcome. Where discussions are not able to resolve a dispute, the only practical remedy available to (potential) licensees is to approach the Tribunal. Proceedings in the Tribunal are very time-consuming and expensive. While Education Departments and the Catholic and Independent schools have significant resources, those resources are limited and have many demands placed upon them. As a result, schools are very reluctant to divert resources to engage in unnecessary litigation. For many licensees, finding the resources for Tribunal proceedings is not viable at all.

This gives the collecting societies an advantage in negotiations – the collecting societies know that they can require licensees either to agree, or go to the Tribunal, the latter being undesirable and often not possible from a time and cost perspective. There is no third option for licensees, who are required to deal with the collecting societies to gain access to the vast majority of copyright materials.

This fact is recognised by the ACCC in the Guidelines²:

'...as collecting societies bring together the rights of parties who would normally compete with each other in the supply of copyright material, their operation creates scope for collecting societies to exercise market power in the setting of licence fees and conditions. In many instances, parties wishing to use copyright material have limited, if any, alternatives to dealing with the relevant collecting society.'

It is CAG's observation that the Guidelines proceed on the basis that existing constraints on collecting societies are sufficient to overcome these issues. CAG identifies the existing 'constraints' as the Code of Conduct for Collecting Societies (the Code), the collecting societies' dispute resolution procedures and the ability to take disputes to the Tribunal.

These constraints may be sufficient in some cases, however often the current framework does not achieve the intended outcome - not all (potential) licensees have a fair opportunity to reach a

¹ Determination of the Australian Competition and Consumer Commission in relation to Applications for Revocation and Substitution and Applications for Authorisation lodged by Australasian Performing Right Association Limited in respect of the standard arrangements for the acquisition and licensing of the performing rights in its music repertoire, 8 March 2006 at piii

² at p10 of the Guidelines

satisfactory negotiated outcome. Collecting societies still have an advantage in negotiations, they can require licensees to either agree or find the resources to go to the Tribunal.

As mentioned above, Tribunal proceedings require significant resources and for the reasons explained below, the Code and collecting societies' dispute resolution procedures are not satisfactory constraints.

CAG submits that the ACCC guidelines should provide another layer of constraint on collecting societies.

CAG's dealings with collecting societies

To provide some background to CAG's views, below is a summary of aspects of CAG's dealings with collecting societies that have been particularly difficult because of the position of 'virtual monopoly' collecting societies occupy.

As noted above, CAG's copyright expenses are very large. CAG is seeking to contain those expenses. One way it is endeavouring to do this is to ensure that all uses of copyright material occurring in schools and TAFEs are necessary. At the same time, it is vital not to inhibit use where that use is constructive.

To assist CAG in doing this, it commissioned a study of the issues arising from copying in schools. The study resulted in a report (the Smart Copying Report) that included a number of recommendations. One of those recommendations was to implement multi-jurisdictional cross-licensing arrangements between the various Australian education jurisdictions. Another was to further research the copying practices of schools, one of the purposes being to identify publications that CAG should seek to directly license.

CAG is in the process of implementing the Smart Copying Report recommendations. It has executed cross-jurisdictional licenses and is seeking to obtain further data on the copying practices of schools with a view to directly licensing certain publications. The key way of obtaining the required information is to review the data collected during the sampling survey conducted in conjunction with Copyright Agency Limited (CAL) for the purposes of the education statutory licence. Numerous requests have been made to CAL to gain access to that information, which have been rejected. CAG believes that one reason for this rejection is to stop CAG obtaining information that would assist it in negotiating direct licences. This issue is presently before the Copyright Tribunal and is the subject of a stated case to the Federal Court.

The reason for explaining this background is to demonstrate that direct licensing has proved very difficult. CAL does not directly and actively block CAG's attempts to directly licence, however there are a range of circumstances that impede CAG's progress. These circumstances include gaining access to relevant data and being able to meaningfully work with CAL to achieve an outcome. It has been CAG's experience that recourse to the Tribunal has been necessary, as CAL has not been open to adopting mediation.

A further difficulty experienced by CAG is that, as a general rule, much of the information needed to determine appropriate licence fees is peculiarly within the possession of collecting societies. Presently, that information can only be obtained during the discovery stage of Tribunal proceedings. It would greatly assist negotiations if the Guidelines required collecting societies to provide information relevant to the rates that might be charged. For example, details

of the types of illustrations copied by schools, for which a rate must be determined. The absence of such information makes it very difficult to reach an outcome.

The Code of Conduct for Collecting Societies

In CAG's experience, the Code and Code Review Process do not adequately address the problems faced by licensees when dealing with the collecting societies. There are numerous difficulties with the Code that result in it not being a satisfactory constraint on collecting societies.

The Code Review Process

During the 2005 review process, CAG raised some significant concerns with its dealings with certain collecting societies. These concerns included substantial delay, inflexible and unfair conduct and the adversarial approach taken. CAG was disappointed with the way these concerns were (not) dealt with during the Code Review Process. Consequently, CAG raised these issues with the Attorney-General's Department. The Department is in the process of addressing CAG's concerns with the Code Review Process.

This experience has resulted in CAG being very apprehensive about the process, including its procedural fairness. CAG will not engage in the Code Review Process in the future.

Shortcomings of the Code

The Code itself suffers from significant shortcomings that inhibit its ability to act as a satisfactory constraint on collecting societies.

These shortcomings include the fact that:

- the Code is voluntary;
- no minimum standards of conduct are prescribed and the guidance that is included is broadly drafted without sufficient detail of what is appropriate;
- the Code Reviewer is appointed by collecting societies; and
- the licensees making comment in the Review Process are usually in ongoing relationships with the collecting societies, meaning they will generally be reticent to voice their concerns.

As mentioned above, CAG has raised these issues with the Attorney-General's Department. It raises them here to demonstrate that the existing 'constraints' on collecting societies are not satisfactory. Some further curb on the conduct of collecting societies is required.

The collecting societies' dispute resolution procedures

As previously mentioned, in CAG's experience, the dispute resolution procedures provided by the collecting societies are not adequate to provide copyright licensees with a third option, ie an option other than agreeing with the collecting society or going to the Tribunal.

CAG has found some collecting societies unwilling to engage in mediation. Whilst alternative dispute resolution is provided for in the Code, it has been CAG's experience that collecting societies are reluctant to take part when dealing with a group of licensees. The collecting societies adopt the view that the alternative dispute resolution procedures are for disputes with individuals. CAG submits that the Guidelines should call for collecting societies to engage in alternative dispute resolution, regardless of who the (potential) licensees are.

Further, although the recent changes to the *Copyright Act 1968* mean that the Tribunal can require mediation, this is only applicable once proceedings have been commenced. There is not sufficient incentive for collecting societies to meaningfully engage in alternative dispute resolution *before* proceedings are commenced.

Tribunal proceedings are expensive and divert resources from the primary role to which those resources should be applied, for CAG, that is advancing education. Diverting resources in this way produces inefficiencies that are contrary to the public interest.

In CAG's view, the Guidelines should place more emphasis on the need to settle any dispute first by bona fide negotiations and, if that fails, alternative dispute resolution processes, without the necessity to go to the Tribunal.

Guidelines for collecting societies

CAG submits that the Guidelines should provide a layer of constraint that is additional to the Code, existing collecting society dispute resolution procedures and recourse to the Tribunal.

The objective, in CAG's view, should be to provide impetus for the collecting societies to engage in meaningful discussions to achieve a negotiated or alternative dispute resolution outcome. The Guidelines should incorporate guidance for the collecting societies, including behaviour of which the societies should be particularly aware and that may be regarded as unsatisfactory.

CAG notes that the Guidelines identify aspects of arrangements that are desirable,³ however in CAG's view this does not go far enough. For example, below is a relevant extract of the Guidelines, with comments marked.

'The ACCC considers that collecting societies should make input and output arrangements that minimise the anti-competitive effect of their operation.

In particular, arrangements will be less anti-competitive if they:

- *do not prevent or inhibit direct negotiation between copyright owners and users. Collecting societies, if requested to, where possible should facilitate (potential) licensees' efforts to directly licence copyright material.*
- *are as unrestrictive as possible, striking an appropriate balance between flexibility in licensing and standard application forms*
- *allow adjustments to blanket licences in appropriate circumstances, including an appropriate adjustment to the fee*
- *are clear and readily available to users of copyright*
- *allow for alternative dispute resolution processes where appropriate. Mediation should be attempted before resort is made to Tribunal proceedings.*
- *ensure that collecting societies, if requested to, where possible provide to (potential) licensees information relevant to the determination of licence fees.*

³ at p33

*Allowing direct negotiation between copyright owners and users of the copyright material is important because it potentially affects the prices of licences to use copyright material. Where licensees have the option of negotiating a license directly with the owners of copyright, this is likely to place a competitive constraint on collecting societies in setting licence terms and conditions, driving them toward efficient outcomes. Such provisions should **in practice** not deter direct dealings between copyright owners and users of the copyright material.*

Flexibility in licensing and allowing users to acquire licences with adjustments to the normal rate charged is only appropriate when the additional costs associated with administration, enforcement and calculation of charges do not outweigh the benefit.'

By including more detail of the kinds of behaviour that are and are not appropriate, the Guidelines will provide a much needed, further constraint on collecting societies.

Pricing of copyright material

CAG submits that the pricing principles included in the Guidelines (at pp34-37) should be reconsidered. CAG has consulted with economic expert, Greg Houston of NERA Economic Consulting. Attached is a paper outlining Mr Houston's criticisms of the relevant section, which CAG asks the ACCC to consider.

In summary, the authors of the paper consider that:

'In developing these guidelines the ACCC has omitted to address a number of issues that are relevant to the pricing of copyright material namely:

- *the role of alternative revenues sources that are available to the creators of original works;*
- *the availability of substitutes to copyright material and the constraint that these substitutes place on the pricing of copyright material;*
- *consideration of the ability and willingness of consumers to pay for the copyright material;*
- *the role of comparable market transactions in assisting to determine the appropriate licence fees to charge; and*
- *the potential to transfer monopoly power from the collecting societies to the users of copyright material if due consideration of the above matters is not taken into account.'*

Conclusion

CAG thanks the ACCC for the opportunity to make this submission and would be pleased to meet with the ACCC to discuss these issues further, or to provide any further information that would assist with the inquiry.

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31 January 2007

Remuneration for the use of copyright material - comment on the ACCC draft guidelines

NERA

Economic Consulting

Project Team

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1. Executive Summary

This report comments on the draft guidelines prepared by the Australian Competition and Consumer Commission ('the ACCC') on the pricing of voluntary copyright licences and licence schemes.

In developing these guidelines the ACCC has omitted to address a number of issues that are relevant to the pricing of copyright material namely:

- the role of alternative revenues sources that are available to the creators of original works;
- the availability of substitutes to copyright material and the constraint that these substitutes place on the pricing of copyright material;
- consideration of the ability and willingness of consumers to pay for the copyright material;
- the role of comparable market transactions in assisting to determine the appropriate licence fees to charge; and
- the potential to transfer monopoly power from the collecting societies to the users of copyright material if due consideration of the above matters is not taken into account.

The basis for these conclusions is addressed in detail in the remainder of this report.

2. Introduction

This report has been prepared by NERA Economic Consulting ('NERA') following a request by Minter Ellison to provide comments on draft guidelines prepared by the ACCC on copyright licensing. The ACCC's draft guidelines, entitled "Copyright licensing and collecting societies: a guide for copyright licensees" ('the draft guidelines') were released for public consultation in November 2006.

Specifically, NERA has been asked to comment from an economic perspective on section 8.3 of the draft guidelines entitled "Pricing of copyright material", which appears at pages 35-37. The stated purpose of this section of the draft guidelines is to articulate:

.....some broad principles it [the ACCC] considers relevant to the pricing of copyright material¹

The development of these principles is particularly important since under the recently amended terms of the *Copyright Act 1968* ('the Act'):

- in applying the provisions of the Act as they relate to the pricing of voluntary copyright licences and licence schemes, the Copyright Tribunal ('the Tribunal') may have regard to guidelines made by the ACCC;² and
- the Tribunal may make the ACCC a party to a proceeding before it, if the ACCC applies and the Tribunal considers it appropriate.

The remainder of this paper is structured so as to address each of the main comments that we have on the draft guidelines.

¹ Australian Competition and Consumer Commission, Copyright licensing and collecting societies: a guide for copyright licensees, Draft for comment, November 2006, page 35

² This applies to voluntary licences and licence schemes only. When considering statutory licences, other factors may be relevant.

3. Context for pricing of copyright material

The ACCC provides a helpful discussion of the context for the pricing of copyright material at the commencement of section 8 of the draft guidelines. It reminds the reader³ that collecting societies bring together parties that would normally compete with each other and that this gives rise to a degree of market or monopoly power in setting the licence fees and conditions for the use of copyright material over which a collecting society has control.

The draft guidelines note that the Tribunal originated from concern at the monopoly power of collecting societies. In counterbalancing that monopoly position, the determination by the Tribunal of reasonable charges and conditions for the use of copyright material has regard to the wider public interest, where this is taken to include the effects of competition in markets.

The wider public interest is served in two main ways by these collecting societies:

- it gives rise to an improvement in efficiency through a reduction in transaction costs; and
- it prevents the transfer of monopoly power from one market to another.

A reduction in transaction costs arises because people wanting to make use of copyright material do not individually have to seek out and negotiate with each owner of the relevant copyright. Rather, each user simply needs to approach the relevant collecting society to obtain access to a range of copyright material. The alternative, involving negotiations with each owner of copyright would often be an onerous task since there are a range of works with a range of owners and often the copyright rights in a work will be held by a number of different individuals or organisations. For example, a piece of music is not only subject to the copyright held by the composer and songwriter, but also the copyright in relation to the musical recording and the printed sheet music. The creation of collecting societies eliminates the need for users to contact each different owner of the relevant copyright, and the need for each copyright owner to negotiate with a vast number of potential users.

The formation of collecting societies also helps to prevent the leveraging of monopoly power created in one market into another. As recognised by the draft guidelines, the collecting societies possess a degree of market power. The requirement that all members of the same class of consumers be provided access to the material at the same price stops the collecting societies from using their monopoly power effectively to determine who will have access to the copyright material. Without this requirement, copyright owners (by charging monopoly prices and/or refusing to supply certain potential customers) could effectively lock out potential users of copyright from gaining access to the material. This could conceivably allow copyright owners to limit the number of users of copyright material, thereby giving rise to the potential to distort related markets that use copyright material as an input for their products. Such limitations on access to copyright material can lead to a reduction in competition or, in some situations, a substandard product.

³ *Ibid*, page 34

The draft guidelines proceed to discuss the pricing of copyright material principally by reference to the public interest, which the ACCC describes in economic terms as the “socially optimal level”⁴ of production of copyright works.

We very much agree that the socially optimal level of production is the correct reference point in economic terms from which to consider the pricing of copyright material. We also agree that the fact that the additional cost of producing an extra unit (‘the marginal cost’) of copyright material is often near zero lies at the heart of the problem of determining prices for such material that will encourage the socially optimal level of production. The near zero price that a ‘text book’ economic analysis would normally call for is unlikely to deliver a socially optimal production of copyright works.

Notwithstanding the ACCC’s correct identification of the problem of pricing copyright material, in our opinion its discussion in the draft guidelines of the issues arising does not give sufficient recognition to two important aspects of the market for copyright material. These are that:

- first, the sources of revenue for the creation of original works are not limited to licence fees generated by means of the collecting societies – and so the incentives for the production of new copyright material do not depend on licence fee revenue alone; and
- second, in determining the socially optimal level of production, of no less importance than the costs of this production (and whether or not producers are able to recover that cost) is the demand side of the market – this amounts to addressing the question of whether or not users are willing and able to meet those costs, thereby ensuring that the creation of original works is not artificially curtailed by prices that are ‘too high’.

The omission of these two considerations in its assessment of the market for copyright material means that the draft guidelines do not give sufficient weight to matters that should cause the ACCC to qualify the principles or conclusions that it draws in discussing the pricing of copyright material.

⁴ *Ibid*, page 36

4. Role of alternative revenue sources

The draft guidelines correctly point out that, in markets that are characterised by effective competition, prices reflect the marginal cost of production and that this is generally sufficient to ensure that production will tend towards the socially optimal level, particularly over the long run. However, the marginal cost of producing another unit of copyright material (once the original work has already been developed) is often very low or close to zero.

It follows that a short run perspective on marginal cost is not a viable basis on which to set prices for copyright material, because of its implications for the creation of new material. Unless there is some form of incentive (means of payment) to create copyright material, this form of production will fall below the socially optimal level.

Whilst these sentiments are correct as a matter of principle, in our opinion the draft guidelines over-emphasise the importance of copyright licences administered by collecting societies (as opposed to licences granted by copyright owners individually) in determining the strength of this incentive to create new copyright material. The draft guidelines make the statement⁵ that:

Setting total remuneration [by means of collecting society administered copyright licence fees] equal to the short-run marginal cost would not provide an incentive for further creation of original works, and the production of such works would fall below the socially optimal level.

The draft guidelines further state⁶ that:

To provide incentive for investment in the production of new copyright material, the sum of remuneration paid [by means of collecting society administered copyright licence fees] by all users of the material should also cover the cost of creating new material.

It is important to recognise that these statements are correct only to the extent that income collected by means of the collecting societies is the *sole source of revenue* to the creators of original works.

In practice, the creators of original works are likely to have access to a number of different potential sources of income, in addition to the licensing of copyright in their works by collecting societies. Such alternative or additional sources of income may include, for example:

- in relation to musical works, revenues earned from the licensing of 'Grand Rights', the licensing of works for use in films and the publishing of print music;
- in relation to books, revenues arising from the sale of books in either electronic or print form; and

⁵ *Ibid*, page 36

⁶ *Ibid*, page 36

- in relation to sound recordings, revenues earned from the sale of CDs and music online.

Given that copyright licensing revenues administered by collecting societies are but one source of potential income to the creators of original works, it follows that even if licensing fees were set equal to their marginal cost, the incentive to create original works would not be eliminated, as the draft guidelines suggest. Rather, a more balanced assessment would recognise that the incentives for the creation of original works would risk falling below the socially optimal level where *income from all potential sources* was insufficient to cover the costs of production.

One consequence of this omission is that the discussion in the draft guidelines of the conceptual attractiveness of determining the remuneration of copyright owners by reference to the cost of creating the relevant material needs to be qualified. In our opinion the draft guidelines should acknowledge that, in determining the appropriate remuneration of copyright owners, income from all other sources would need to be netted off from any measure of total production cost before the amount to be recovered from licences administered by collecting societies could be determined.

The absence of any acknowledgement of the role of alternative or additional sources of revenue for the creators of original works means that the draft guidelines tend to overstate the incentive problems arising from setting remuneration by means of copyright licensing fees at marginal cost. Given the existence of other sources of revenue and so alternative forms of incentive for the creators of original works, it is too strong to say that marginal cost pricing of collecting society administered copyright licence fees would result in production *well* below the socially optimal level - unless one had some indication of the percentage of revenue from collecting society sources as opposed to other sources.

The above observation does not detract from the important role of collecting societies in ensuring the sustainable creation of original works. Our point is simply that the ACCC has overstated the role of copyright licences and the positive incentives they give rise to by suggesting that the full cost of production should be recouped from such licensing fees. Application of such a principle is likely to over-compensate the creators of original works, and lead to a greater than socially optimal amount of production.

Given the difficulty in quantifying the costs and the amount earned from other sources of revenue, the use of comparable market transactions should be considered to help determine the appropriate price. This is discussed in greater detail in section 6.

5. Role of potential substitutes and the consumer

5.1. Potential substitutes

In determining the appropriate level of remuneration for copyright material, it is also important to take account of the nature and extent of available substitutes. As indicated above, the creators of original works are likely to be in a position to earn revenue from sources other than copyright licences administered by collecting societies. Such forms of revenue represent potential substitutes from the perspective of the creator of original works.

Importantly, substitutes for the use of copyright works also arise from the perspective of the consumer. For example, a nightclub would be subject to copyright licensing fees for the playing of recorded music. However, one alternative open to that nightclub would be to hire a live band to perform. Likewise, a pharmaceutical company could obtain a licence directly from the publisher of a scientific textbook, rather than paying licensing fees to the relevant collecting society for the photocopying of material from the book.

The availability of such substitutes puts a constraint on what people are willing to pay for the use of copyright works and so puts a constraint on the amount that is able to be charged in the form of licensing fees. As the price of licences becomes greater, users are likely to seek alternative means of meeting their needs that involve either a more limited form of licence or none at all. Such responses by copyright users will cause less original works to be produced, thereby also giving rise to the risk of sub-optimal outcomes from a societal perspective.

5.2. Role of consumer demand

The consideration of available substitutes amounts to making an assessment of the demand side of the market for the use of copyright material. However, in its draft guidelines the ACCC focuses exclusively on the circumstances surrounding the supply of copyright works and the costs associated with this supply. The draft guidelines involve no discussion of the role of the demand side of the market, which is likely to place a constraint on how much is supplied and its cost.

In assessing the demand for the use of copyright material, the alternatives or substitutes available to consumers need to be taken into account. The existence of substitutes will place a constraint on the amount that can be charged. Whilst collecting societies have a virtual monopoly on the licensing of copyright in original works, some works may no longer be subject to copyright or may not be eligible for copyright originally. These works will provide a substitute or alternative to the copyrighted works.

By way of example, the performance of a Shakespearean play will no longer be subject to copyright protection whereas the performance of a play by David Williamson will be subject to copyright. Those works that are no longer subject to copyright represent an alternative to using copyright works and so act as a constraint on the amount that can be charged for the use of copyright works.

Of course, in some circumstances there may be no effective substitute available to the organisation wishing to use the copyright material. For example, a radio station seeking a blanket licence for its airing of popular music would not realistically be able to seek out

licences with each and every relevant copyright owner - its only real alternative would be to move to a 'talk format'. In this situation, substitutes may not place an effective constraint on the licence fees able to be charged by the collecting societies and due account needs to be taken of the users' willingness and ability to meet the cost of copyright licence fees.

Without consideration of these issues, collecting societies may effectively 'lock out' those users that are unable or unwilling to pay the higher licence fees. Excessive prices may provide the collecting societies with the potential to transfer their monopoly power to certain users of copyright material with the ability to pay these higher fees. Further, prices that are 'too high' from the consumers' perspective will lead to lesser production of original works, and so sub-optimal outcomes from a social welfare perspective.

The ACCC's draft guidelines make no reference either to the constraints that substitutes form on the price that can be charged for the use of copyright material, or to the role of consumer preferences more generally. For the creation of any copyright work to be socially optimal, it is a requirement that some consumers must be willing to pay to experience the benefits of that work.

In giving explicit consideration only to the supply side of the market for the creation of original works, the draft guidelines effectively assume that:

- there is a end-market for all relevant works that has a sufficient number of consumers willing and able to pay for the relevant material; and
- that there is an absence of substitutes for the relevant copyrighted works.

Both of these demand-side considerations will act to constrain the price charged for the use of copyright material and should be explicitly acknowledged in the draft guidelines. As a matter of principle, socially optimal production cannot be achieved through consideration only of the supply side of a market. What consumers want, the alternatives available to them, and how much they are willing to pay, form important constraints on any production-orientated assessment of the appropriate price in a market.

6. Role of market transactions

The draft guidelines give due recognition to the difficulties associated with measuring supply costs in the context of determining the equitable remuneration of copyright owners. However, they provide little in the way of practical assistance for overcoming this hurdle. In part, this would seem to be a consequence of the exclusive focus of the draft guidelines on the supply side of the market for the relevant copyright material.

In our opinion, it would be helpful if the draft guidelines were to give explicit recognition to the potential role of transactions that have already taken place for the use of the same or similar rights as those the subject of the copyright licence in question.

An important attribute of prior transactions for the same or similar rights is that they encapsulate information from both the supply and demand sides of the relevant market. If exchange has taken place, it can be assumed that both parties to such transactions were willing participants – since, if not, either the copyright owner would have refused to make the right available or the relevant consumer would have declined to make the purchase.

7. Price discrimination and licence fee structure

7.1. Price discrimination

In our opinion the underlying economic principles in the section of the draft guidelines entitled 'price discrimination and licence fee structure' are sound. In circumstances where the supplier of a good or service has market power, the ability to price discriminate will tend to improve efficiency and is more likely to deliver a socially optimal outcome.

However, there is some risk that the draft guidelines place too much emphasis on the ability and use of price discrimination. In order for price discrimination to improve social outcomes it is necessary to be able to identify those segments of the field of consumers that have differing levels of price elasticity and in some cases to quantify these values. This is an extremely difficult analysis to achieve in practice. If this distinction cannot be made then the efficiency enhancement potential for price discrimination is doubtful.

The ability to discriminate in terms of price also presupposes the absence or limitation of substitutes. If price discrimination leads to certain customer segments being charged too much, those consumers will switch to an alternative product or producer. Substitutes again impose a cap on the amount that can be charged to any consumer. Although price discrimination is an efficient way to price goods and services for which there are limited alternatives, we believe in principle, its likely role in the context of copyright licensing is given too much emphasis in the draft guidelines.

7.2. Licence fee structure

The draft guidelines are correct to state that collecting societies have to strike an appropriate balance between the advantages of charging different prices to different consumers whilst also providing for the ease of administration of their licensing function. The draft guidelines also provide examples of metrics that could be used as an approximation of the use of copyright material by different users, and illustrate relatively simple and more complex methodologies for calculating the fees depending on the circumstances in which the copyright material is to be used.

In our opinion, it is important to recognise that no one method can or should be endorsed for use in all circumstances. There may be a range of suitable charging metrics for each circumstance. Rather, the most important task is to ensure that the guidelines are flexible enough to allow different methods to be used in different circumstances, taking account of the principles that are well described in the final paragraph of the pricing section of the draft guidelines.

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