



**INTELLECTUAL**  
PROPERTY OFFICE

# **Private Copying and Fair Compensation:**

## **An empirical study of copyright levies in Europe**

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**This is an independent report commissioned by the Intellectual Property Office (IPO).  
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(grant RES-173-27-0220).**

**Professor Martin Kretschmer  
2011**

Intellectual Property Office is an operating name of the Patent Office

Martin Kretschmer is Professor of Information Jurisprudence and Director of the Centre for Intellectual Property Policy & Management ([www.cippm.org.uk](http://www.cippm.org.uk)), Bournemouth University. Many thanks to Dr Sukhpreet Singh for research assistance. Author may be reached at: Bournemouth University, Executive Business Centre, 89 Holdenhurst Road, Bournemouth, BH8 8EB, +44 (0)1202 968749, [mkretsch@bournemouth.ac.uk](mailto:mkretsch@bournemouth.ac.uk).

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Private Copying and fair Compensation

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The Intellectual Property Office  
Concept House  
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NP10 8QQ

Tel: 0300 300 2000  
Minicom: 0300 0200 015  
Fax: 01633 817 777

e-mail: [information@ipo.gov.uk](mailto:information@ipo.gov.uk)

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# Abstract

Following the Information Society Directive of 2001 (introducing the concept of “fair compensation” for private copying into EU Law), total collection from levies on copying media and equipment in the EU tripled, from about €170m to more than €500m per annum. Levy schemes exist now in 22 out of 27 Member States (with only the UK, Ireland, Malta, Cyprus and Luxembourg remaining outside). Despite their wide adoption, levy systems are little understood, both in respect of their rationale and their economic consequences. Tariffs are increasingly contested in court, leading to a large gap between claimed and collected revenues. The European Commission has announced “comprehensive legislative action” for 2012.

This report offers the first independent empirical assessment of the European levy system as a whole. The research consolidates the evidence on levy setting, collection and distribution; reviews the scope of consumer permissions associated with levy payments; and reports the results of three product level studies (printer/scanners, portable music/video/game devices, and tablet computers), analysing the relationship between VAT, levy tariffs and retail prices in 20 levy and non-levy countries.

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## Key findings

- There are dramatic differences between countries in the methodology used for identifying leviable devices, setting tariffs, and allocating beneficiaries of the levy. There are levies on blank media in 22 EU countries, on MP3 players in 18 countries, on printers in 12 countries, on personal computers in 4 countries. Revenues collected per capita vary between €0.02 (Romania) and €2.6 (France). The distribution of levy revenues to recording artists is less than €0.01 per album.
  - These variations cannot be explained by an underlying concept of economic harm to rightholders from private copying.
  - The scope of consumer permissions under the statutory exceptions for private copying within the EU vary, and generally do not match with what consumers ordinarily understand as private activities.
  - In levy countries, the costs of levies as an indirect tax are not always passed on to the consumer. In competitive markets, such as those for printers, manufacturers of levied goods appear to absorb the levy. There appears to be a pan-European retail price range for many consumer devices regardless of levy schemes (with the exception of Scandinavia).
  - In non-levy countries, such as the UK, a certain amount of private copying is already priced into retail purchases. For example, right holders have either explicitly permitted acts of format shifting, or decided not to enforce their exclusive rights. Commercial practice will not change as a result of introducing a narrowly conceived private copying exception.
  - A more widely conceived exception that would cover private activities that take place in digital networks (such as downloading for personal use, or non-commercial adaptation and distribution within networks of friends) may be best understood not as an exception but as a statutory licence. Such a licence could include state regulated payments with levy characteristics as part of a wider overhaul of the copyright system, facilitating the growth of new digital services.
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# Summary report

*This short report explains key findings of the research in policy relevant language. Three underlying studies were performed: Study I entitled “**Legal and policy context**” reviews the implementation of levy systems in the EU; Study II entitled “**Empirical effects of copyright levy schemes**” reports data on the relationship between VAT, levy tariffs and retail prices for three products in 20 levy and non-levy countries; Study III entitled “**Economic rationales**” offers a framework for analysing state regulated levy systems.*

## 1. Legal basis

In EU copyright law, private copying has been given a specific meaning relating only to the reproduction right (i.e. not: communication to the public, distribution to the public, public performance or adaptation). Private copying is included among the closed list of exceptions permitted under Article 5 of the 2001 Information Society Directive. Article 5(2)(b) reads: [Member States may provide for exceptions or limitations to the reproduction right] “in respect of reproductions on any medium made by a natural person for private use and for ends that are neither directly or indirectly commercial, on condition that the rightholders receive fair compensation which takes account of the application or non-application of technological measures [referred to in Article 6].”<sup>1</sup>

## 2. Blurring between private copying and communication to the public

The narrow focus of the reproduction right does not map well onto typical copying behaviour in digital networks. Users may consider activities under the following headings to be private:

- (i) Making back-up copies / archiving / time shifting / format shifting
- (ii) Passing copies to family / friends
- (iii) Downloading for personal use
- (iv) Uploading to digital storage facilities
- (v) File sharing in digital networks
- (vi) Online publication, performance and distribution within networks of friends
- (vii) User generated content / mixing / mash-up (private activities made public)

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<sup>1</sup> Directive 2001/29/EC of the European Parliament and of the Council of 22 May 2001 on the harmonisation of certain aspects of copyright and related rights in the information society. See Study I: Legal and Policy Context

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In the analogue world, the private copying exception was aimed at discrete copies for non-commercial use in categories (i) and (ii). In digital networks, the distinction between private and public spheres has become blurred. Regularly, new services are invented that challenge earlier divisions (P2P, social networks, cloud servers).

### 3. Implementation of the private use exception in EU countries

Under the Information Society Directive, only activities (i), (ii), (iii) and (iv) can possibly fall only under the reproduction right (and therefore be eligible for a compensatable exception as private copying). Even within these groups of activities, the scope and legal construction of private copying differs considerably between countries. In some countries, sources need to be lawful, in others not; in some countries, there are a set number of permitted copies specified, in others there are definitions of private circles; in some countries, the levy is constructed as a statutory licence, in others as a debt; in some countries compensation is only due for private copying of music, in others for printed matter (reprographics) and audio-visual works.

As a mechanism for “fair compensation”, 22 out of 27 European Union members have chosen to meet the requirement through a levy system. The exceptions are the UK and Ireland (only time-shifting of broadcasts is permitted), Malta, Cyprus and Luxembourg (private copying treated as *de minimis*). Within the 22 countries that provide for a compensated private copying exception, levy schemes vary widely in the following respects:

- levies apply to different media or equipment that can be used to make copies (e.g. recordable carriers, hard disks, MP3 players, printers, PCs);
- levies differ in tariffs for the same media or equipment, and apply different methods of calculation (e.g. memory capacity, percentage of price);
- levies differ in whether they are imposed on the manufacturers, importers or distributors of media or equipment, or consumers;
- levies differ in beneficiaries (music, audio-visual, reprographic rightholders; wider cultural or social purposes);<sup>2</sup>
- regulatory structures differ (processes for setting tariffs and distribution, contestability of tariffs, governance and supervision of agencies).

The system as a whole is deeply irrational, with levies for the same devices sold in different EU countries varying arbitrarily. The following three figures illustrate the variable scope and density of levy schemes, and track the evolution of total revenues raised from copyright levies in the

EU. The underlying data can be found in Study I.

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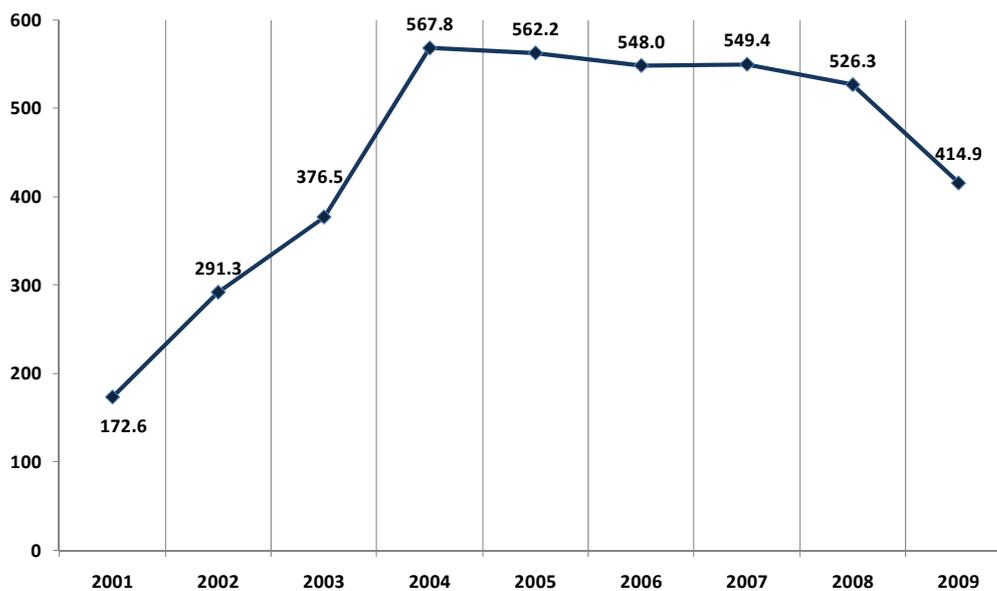
<sup>2</sup> For example, the distribution of levy revenues to recording artists is less than €0.01 per album; use of levy income for socio-cultural purposes differs between 0% and 33% of collected revenues. Variations have been catalogued in Study I.

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## 4. Aggregate revenues, levy scope and levy density

The 2001 Information Society Directive introduced the requirement of “fair compensation” for statutory “private copying” exceptions into EU copyright law. This initiated a rapid rise in collection under levy systems from €172 million in 2001 to €567 million in 2004. Collection plateaued around the €500 million mark between 2004 and 2008, and is now beginning to fall as blank tapes, CDs and DVDs are disappearing from the market, and levies on new products are increasingly contested.

**Figure 1 - Aggregate levy revenues in EU (2002-2009)**



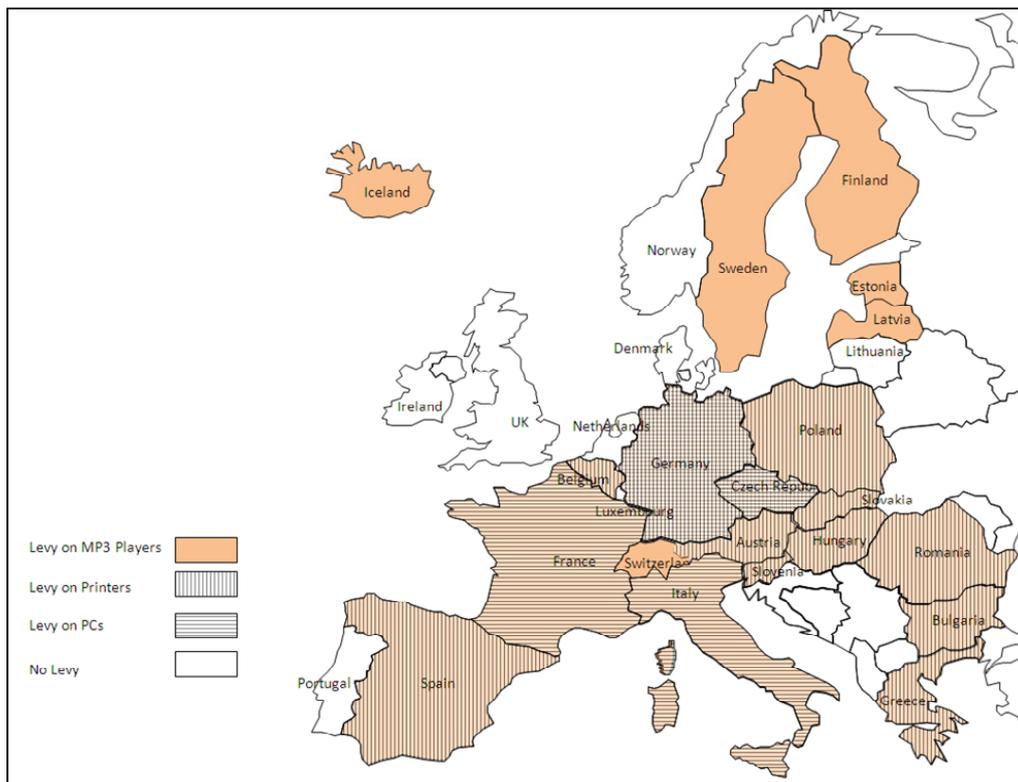
Source: European Commission; de Thuiskopie; Business Software Alliance

Collected fees need to be understood in a volatile context of claimed (but unpaid) and paid (but contested) tariffs. Recent examples of changes in tariffs and scope include:

- 1 January 2008: Amendment to German copyright law (UrhG 2. Korb): Tariffs in law replaced by negotiated tariffs between manufacturers and collecting agency ZPÜ; about €20m of claimed fees contested, and withheld by manufacturers.
  - 24 February 2009: Decision by highest Austrian court (OGH, 4 Ob 225/08d); levy on personal computers cancelled; compensation can only be due on equipment that is designed for copying.
  - 21 October 2010: *Padawan SL v Sociedad General de Autores y Editores de España (SGAE)*, Case C-467/08, European Court of Justice (ECJ): Business media and equipment not leviable; Spanish collecting societies may have to return certain fees collected under Art. 25 of the *Ley de Propiedad Intelectual*.
  - 11 April 2011: Dutch State Secretary for Public Safety and Justice Fred Teeven announces phasing out of levies (levies on recordable CDs will not be replaced by schemes on new media or equipment).
-

Across Europe, there are great variations in the products subject to copyright levies. There are levies on blank media in 22 EU countries, on MP3 players in 18 countries, on printers in 12 countries, on personal computers in 4 countries. In addition, there are currently nine countries where levies for mobile phones are claimed but contested, amounting to about €192 million in 2010 which may or may not become payable. The following map illustrates these differences for MP3 players, printers and personal computers (“no levy” here means “no levy on these three devices”).

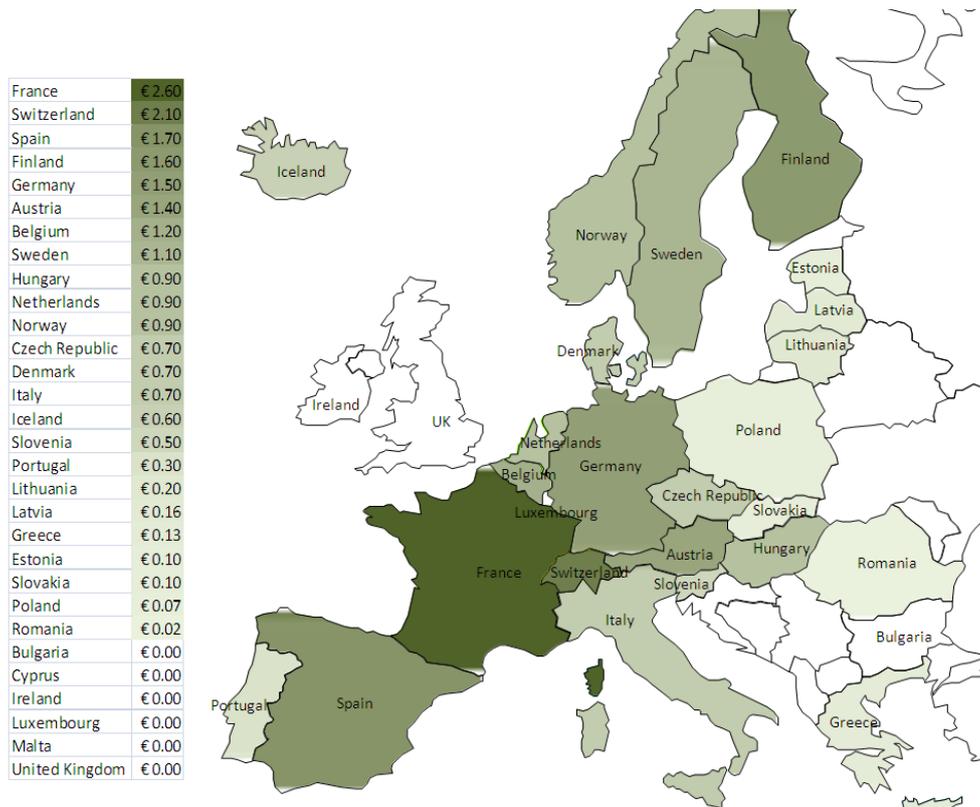
**Figure 2 - Levies applicable to MP3 Players, Printers and PCs (2009)**



Source: Annual reports of collecting agencies; de Thuiskopie, *International Survey on Private Copying Law & Practice* (21st revision 2010). Iceland, Norway and Switzerland are not members of the EU. They are added for illustrative purposes because their copyright legislation is EU compliant.

For the purposes of the next map, levy density is measured by revenues raised per capita of the population, ranging from €2.6 in France to €0 in non-levy countries, such as the UK and Ireland. Bulgaria has a levy scheme by statute but no reported collection.

**Figure 3 - Levy revenues per capita in Europe (2009)**



Source: Annual reports of collecting agencies; de Thuiskopie, *International Survey on Private Copying Law & Practice (21st revision 2010)*. Iceland, Norway and Switzerland are not members of the EU. They are added for illustrative purposes because their copyright legislation is EU compliant.

## 5. Empirical effects of levies on retail prices

Are levied products more expensive in levy countries than in countries that do not apply a copyright levy? In Study II, the following products were investigated for an analysis of the relationship between copyright levies and retail prices:

- (1) printer/scanners: levies are applied in 14 out of 27 Member States ranging between €0.72 and €56 per unit for an HP 4500 Officejet printer;
- (2) portable music/video/game devices: levies surveyed in 9 Member States ranged between €1.42 and €19.40 for Apple's iPod Touch 64GB;
- (3) tablet computers: may be classified as a personal computer in 4 Member States (carrying a possible levy per unit of €12.15 in Germany, €8.00 in France and €1.90 in Italy).

The empirical analysis, plotting retail prices in 20 countries against levy and VAT rates, indicates that markets for printer/scanners are highly competitive. Manufacturers find it difficult to pass on higher indirect taxes to the consumer. In some high levy countries (such as Germany), the HP Officejet 4500 printer is retailing at a similar price as in non-levy countries (such as the UK), and there appears to be no systematic link between wholesale and retail pricing. For producers of premium products, such as the iPod Touch, there is a statistically significant correlation between total indirect taxation and the retail price, suggesting that manufacturers are able to pass on higher costs to the consumer.

Generally, there appears to be a pan-European retail price point for consumer devices, regardless of divergent levy schemes, with only Scandinavian consumers willing to pay more. Product launch decisions for innovative products (such as tablet computers) seem unaffected by the level of indirect taxation. Further details on launch dates for three tablet computers (iPad1, iPad2 and Samsung Galaxy) are given in Study II.

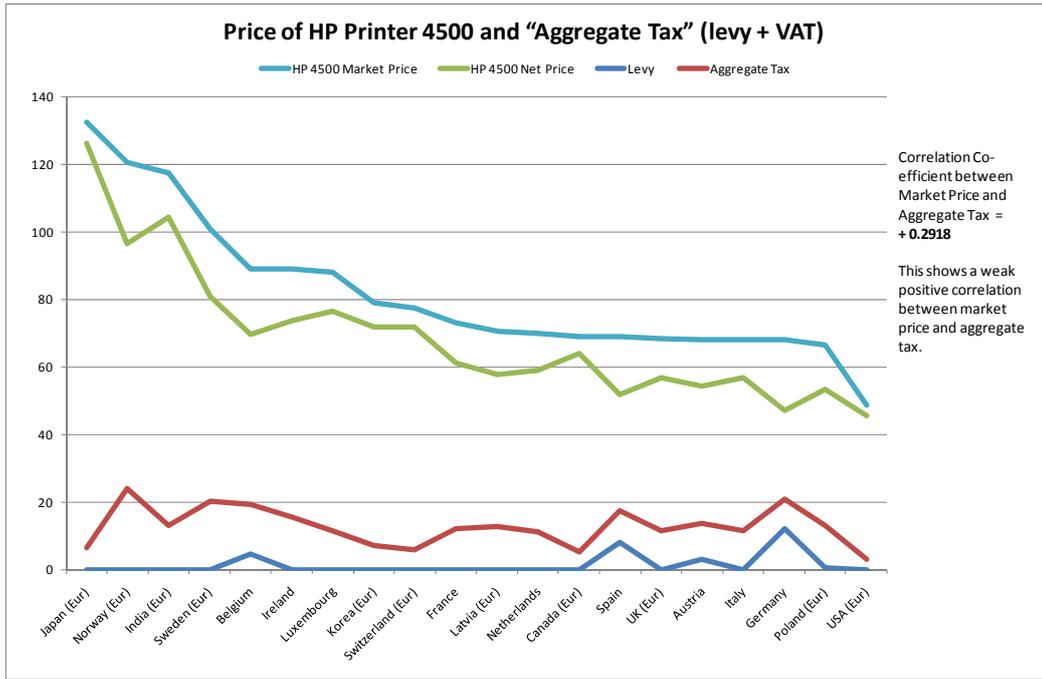
The following two figures illustrate the relationship between the total level of indirect charges (copyright levy plus VAT) and retail prices for the Apple iPod Touch (64GB) and the Hewlett Packard Office Jet 4500 in a variety of countries, including the four countries that account for 75% of levy revenues in the EU: France, Germany, Spain and Italy; and countries neighbouring these large levy markets where cross border effects should be most prominent. In addition, non-levy countries, and the home markets of the products investigated were added. The countries are ordered from left to right by descending online retail price (April 2011, lowest price available, at Euro exchange rates of 15 April 2011).<sup>3</sup>

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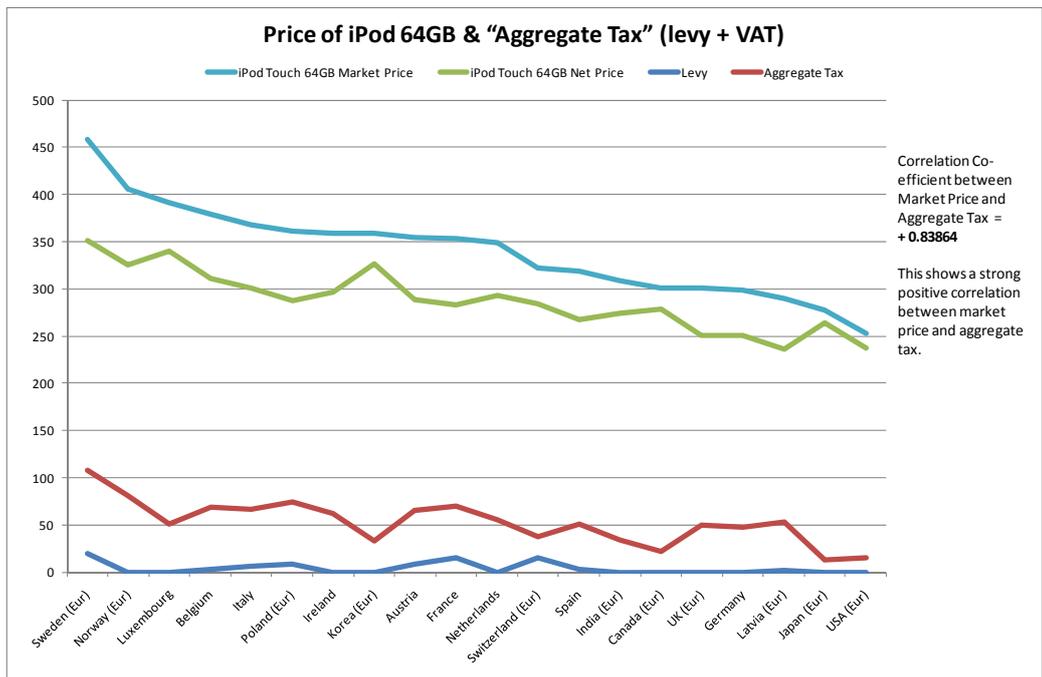
3 The methodology for product and country selection, as well as the process of data collection is explained in detail in Study II.

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**Figure 4 - Relationship between price, levy and VAT (HP printer)**



**Figure 5 - Relationship between price, levy and VAT (iPod Touch)**



The two figures demonstrate that the price at which a product retails is dependent, not necessarily on the level of indirect taxation in a country but on market conditions and consumers' willingness to pay. The United States generally has the lowest prices; Germany's consumers seem to be getting a good deal despite quite high indirect charges; Scandinavians appear to be willing to pay a premium.

The extent to which it is profit maximising for firms to pass on copyright levies to consumers (rather than absorb the costs) depends on a number of factors. These may vary across different markets. Relevant factors include the degree of competition, elasticity of demand, and if levies are applied uniformly to all manufacturers (firm-specific or industry-wide costs). It also matters that levies, as indirect charges, are not fixed costs but depend on sales. Unless added explicitly on the retail price (as prescribed only in Belgium), the extent of pass-on is difficult to establish.

Making the levy explicit on consumer retail advertising and receipts may be explored as a policy solution, together with explicit consumer permissions "bought" with the levy.

## 6. The concept of harm

In the 2010 *Padawan* decision, the European Court of Justice held that the concept of "fair compensation" "must be regarded as an autonomous concept of European Union law to be interpreted uniformly throughout the European Union".<sup>4</sup> With reference to Recitals 35 and 38 of the Information Society Directive, the Court found (at 42) that "fair compensation must necessarily be calculated on the basis of the criterion of the harm caused to authors of protected works by the introduction of the private copying exception".

The concept of harm is problematic, and has failed to acquire a coherent meaning. From the jurisprudence on awarding damages, harm in law is likely to be interpreted as a lost licensing opportunity, i.e. a fee that could have been charged.<sup>5</sup> However, there is a circularity here: if there is a copyright exception, there is no infringement, and no licence could have been issued. Thus by definition there is no harm in law from a permitted activity.

In economics, harm is a lost sale, i.e. if copying replaces a purchase that otherwise would have been made. Evidence on the extent of private copying presented to the Copyright Board in Canada shows that in 2006-2007, portable music players (such as iPods) contained on average 497 tracks of music, of which 96% were copied.<sup>6</sup> In total, 1.63 billion copies of tracks were

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4 *Padawan SL v Sociedad General de Autores y Editores de España (SGAE)*, Case C-467/08, 21 October 2010. The intellectual origins of the concept of "fair compensation" can be traced to a decision of the German federal court in 1964 (BGH, NJW 1964, 2157; GRUR 1965, 104 - *Personalausweise*), and the copyright law of 1965 (UrhG). See Supporting Study I.

5 Under the common law concept, damages shall put the claimant in as good a position as if no wrong had occurred: *Robinson v Harman* (1848); *Livingstone v Rawyards Coal Co* (1880).

6 8 Exhibit CPCC-3: *Étude de marché sur la copie privée d'enregistrements musicaux au Canada 2006-2007* (11 January 2008); 695pp report prepared by Circum for Société canadienne de perception de la copie privée (CPCC). The methodology is based on monthly telephone surveys of about 1,000 Canadians (above the age of 12), a sample representative of all Canadians. The data in the report are based on 12,011 "entrevues" between July 2006 and June 2007.

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being made in Canada from July 2006 to June 2007. Of these, about half (808 million) were copied on digital recorders; of these 808 million, about 345 million (42%) came from the Internet. Only 20% of these tracks were authorised downloads (e.g. from iTunes). Thus, from July 2006 to June 2007, there were 646 million copies being made from unauthorised Internet sources that found their way on the typical portable music player.

How many of these downloads have been listened to, rather than stored? How many have replaced purchases? How many have led to purchases? These questions (illustrated here by reliable Canadian data) are hotly contested in the academic literature, and empirical studies have come to opposite conclusions.

Hal Varian shows (developing Liebowitz' concept of "indirect appropriability")<sup>7</sup> that we need to distinguish the number of works produced and the number of works consumed. If sharing is permitted, or takes place, the producer is likely to sell fewer units of the work, but since the consumer derives greater value from each unit, the producer's profit may even increase (if pricing is right). However, if the availability of free copies pushes the retail price to marginal cost, the original seller will find it hard to raise the price to a level where he can recover the cost of production. The basic idea remains the same: "if the willingness-to-pay for the right to copy exceeds the reduction in sales, the seller will increase profit by allowing that right."<sup>8</sup>

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7 Hal A. Varian (2005), "Copying and Copyright", *Journal of Economic Perspectives* 19(2): 121-138; Stan Liebowitz (1985), Copying and Indirect Appropriability: Photocopying of Journals", *Journal of Political Economy* 93(5): 945-57.

8 Varian, *ibid.* p. 130

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## 7. Distinction between “priced into purchase” and “statutory licence”

Reconsider the consumer activities listed in section two above. For (i) [Making back-up copies / archiving / time shifting / format shifting]; and (ii) [Passing copies to family / friends], a certain amount of copying appears to be already priced into the purchase (Varian’s argument). For example, right holders have either explicitly permitted format shifting, or decided not to enforce their exclusive rights. There is no lost sale, and the European criterion of harm may be treated *de minimis*, i.e. no compensation is due. Commercial practice will not change as a result of introducing such a narrowly conceived private copying exception.

A more widely conceived exception that would cover private activities that take place in digital networks [activities (iii) to (vii)] might be better understood as a statutory licence. Possible rationales for issuing such a licence include: making the copyright system more permissive for consumer led innovation, as well as non-economic arguments (such as influencing the bargaining position of creators versus producers, or preserving fundamental rights of privacy). The EU concept of “compensatable harm” contributes little towards assessing an appropriate scope and tariff for such a licence. There is no case for copyright levies unless the payment of levies is linked to clear consumer permissions, and an argument is made why scope and tariff of these permissions cannot be left to the market.<sup>9</sup>

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9 See Supporting Study III.

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## Postscript

In May 2011, the European Commission announced “comprehensive legislative action” regarding private copying levies for 2012: A Single Market for Intellectual Property Rights: Boosting creativity and innovation to provide economic growth, high quality jobs and first class products and services in Europe, Communication from the European Commission (COM(2011) 287 final). Section 3.3.4. reads: “The proper functioning of the internal market also requires conciliation of private copying levies with the free movements of goods to enable the smooth cross-border trade in goods that are subject to private copying levies. Efforts will be redoubled to kick-start a stakeholder agreement built on the achievements of a draft Memorandum of Understanding (MoU) brokered by the Commission in 2009. A high level independent mediator will be appointed in 2011 and tasked with exploring possible approaches with a view to harmonising the methodology used to impose levies, improve the administration of levies, specifically the type of equipment that is subject to levies, the setting of tariff rates, and the inter-operability of the various national systems in light of the cross-border effects that a disparate levy system has on the internal market. A concerted effort on all sides to resolve outstanding issues should lay the ground for comprehensive legislative action at EU level by 2012.”

How do state regulated licences with levy characteristics compare to privately negotiated levies? On 6 June 2011, Apple announced<sup>10</sup> that it will offer in the U.S. a service that scans computers for music files, and then give access to these on any device from Internet (cloud) servers for a fee of \$24.99 per annum. In effect, Apple’s iCloud attempts to legalise private collections of music files, regardless of origin. The terms of agreement between new digital services and right owners are not transparent. What is the share of royalties between publishers and labels; what is the split between major and independent labels; how much will be passed on to artists? These details matter greatly for an assessment of the intervention of intellectual property rights from a competition perspective, and the comparative merits of state regulated levies. This is in urgent need of further empirical research prior to legislative action on copyright levies.

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10 Announcement at Apple Worldwide Developers Conference (WWDC, 6 June 2011).

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# Study I: Legal and Policy Context

## The requirement of fair compensation

“Private copying” is a loose label for activities that most users of copyright materials believe should be beyond the control of right owners. It is important to note that the domain of the private is not co-extensive with the non-commercial. Some activities are pursued without monetary gain, yet addressed to a public audience. Some activities take place in the private sphere but may affect commercial exploitation.

In EU law, private copying has been given a specific meaning relating only to the reproduction right (i.e. not communication, performance or adaptation). Private copying is included among the exhaustive list of exceptions permitted under Article 5 of the 2001 Information Society Directive.<sup>1</sup> Article 5(2)(b) reads: [Member States may provide for exceptions or limitations to the reproduction right] “in respect of reproductions on any medium made by a natural person for private use and for ends that are neither directly or indirectly commercial, on condition that the rightholders receive fair compensation which takes account of the application or non-application of technological measures [referred to in Article 6]”<sup>2</sup>

In the 2010 *Padawan* decision, the European Court of Justice held that the concept of “fair compensation” “must be regarded as an autonomous concept of European Union law to be interpreted uniformly throughout the European Union”.<sup>3</sup> The intellectual origins of the concept of “fair compensation” can be traced to a German decision in 1964 in which the highest federal court (*Bundesgerichtshof*) held that a prohibition against private copying was not enforceable. The decision led to the introduction of the German levy system with the copyright law of 1965 (UrhG).<sup>4</sup>

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1 Directive 2001/29/EC of the European Parliament and of the Council of 22 May 2001 on the harmonisation of certain aspects of copyright and related rights in the information society.

2 “Technological measures” is international treaty speak for copy protection, implemented by digital rights management systems. In December 1996, two “Internet” treaties were adopted under the auspices of the World Intellectual Property Organisation, the “WIPO Copyright Treaty” and the “WIPO Performances and Phonograms Treaty”. It was the objective of the Information Society Directive to transpose into EU law the main obligations under these Treaties.

3 *Padawan SL v Sociedad General de Autores y Editores de España (SGAE)*, Case C-467/08, 21 October 2010. In the Information Society Directive, a requirement of “fair compensation” is common to three possible exceptions and limitations: reprography (Art. 5(2)(a)), private use (Art. 5(2)(b)), and reproductions of broadcasts made by social institutions (Art. 5(2)(e)).

4 BGH, NJW 1964, 2157; GRUR 1965, 104 – *Personalausweise*; Fromm/Nordemann, *Urheberrecht: Kommentar zum Urheberrechtsgesetz, zum Verlagsgesetz und zum Urheberrechtswahrnehmungsgesetz* (10th edition, 2008). The author is grateful to Prof. Dr. Jürgen Becker [formerly CEO of GEMA and collecting agency ZPÜ] and Dr. Robert Staats [CEO, VG Wort] for discussions on the origins and legal context of the German levy system.

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While German copyright law construed the levy as a statutory licence necessitated by a constitutional norm (the inviolability of the private sphere), the new European concept of fair compensation relies on an evaluation of harm as a result of the unauthorised reproduction of protected works. With reference to Recitals 35 and 38 of the Information Society Directive, the ECJ found in *Padawan* (at 42) that “fair compensation must necessarily be calculated on the basis of the criterion of the harm caused to authors of protected works by the introduction of the private copying exception”.<sup>5</sup>

For ease of reference, Recitals 35 and 38 of the Information Society Directive (2001/29/EC) are given here in full:

(35) In certain cases of exceptions or limitations, rightholders should receive fair compensation to compensate them adequately for the use made of their protected works or other subject-matter. When determining the form, detailed arrangements and possible level of such fair compensation, account should be taken of the particular circumstances of each case. When evaluating these circumstances, a valuable criterion would be the possible harm to the rightholders resulting from the act in question. In cases where rightholders have already received payment in some other form, for instance as part of a licence fee, no specific or separate payment may be due. The level of fair compensation should take full account of the degree of use of technological protection measures referred to in this Directive. In certain situations where the prejudice to the rightholder would be minimal, no obligation for payment may arise.

(38) Member States should be allowed to provide for an exception or limitation to the reproduction right for certain types of reproduction of audio, visual and audio-visual material for private use, accompanied by fair compensation. This may include the introduction or continuation of remuneration schemes to compensate for the prejudice to rightholders. Although differences between those remuneration schemes affect the functioning of the internal market, those differences, with respect to analogue private reproduction, should not have a significant impact on the development of the information society. Digital private copying is likely to be more widespread and have a greater economic impact. Due account should therefore be taken on the differences between digital and analogue private copying and a distinction should be made in certain respects between them.

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5 “Fair compensation” must be distinguished from the concept of “equitable remuneration” (*angemessene Vergütung*), another autonomous EU construct with German origins. It appears in Article 8(2) of Council Directive 92/100/EEC of 19 November 1992 on rental right and lending right and on certain rights related to copyright in the field of intellectual property (OJ 1992 L 346, p. 61). It has been interpreted as a right to obtain money in place of a full exclusive right (Case C-245/00 *SENA* [2003] ECR I-1251, at 24). According to the European Commission, equitable remuneration requires a minimum standard of payment without evaluation of harm (2006 Impact Assessment, p. 16). Hugenholtz et al. argue (2003, p. 36) that “equitable remuneration”, as a notion based on fairness, may require higher levels of payment than payments based on harm (P.B. Hugenholtz, L. Guibault, S. van Geffen (2003), *The Future of Levies in a Digital Environment*, Amsterdam: Institute for Information Law (IViR)).

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In the preparatory work for a 2006 Recommendation (“Fair Compensation for Private Copying in a Converging Environment”; not adopted), the European Commission explained levies as “a form of indirect remuneration for right holders, based on the premise that some acts of private copying cannot be licensed for practical purposes by the relevant right holders”. If they could, there would be no need for a private copying exception, nor for levies.<sup>6</sup> The intention of the Recommendation was to encourage right owners to find ways to license individually, and perhaps over time phase out levies.<sup>7</sup> Consumers should not be charged twice, once for copy-protected individually licensed content, and once for private copying (that may, or may not be permitted under the licence).<sup>8</sup> The Recommendation was blocked from leaving the Commission reportedly by French opposition. There was concern about the loss of an income stream of collecting societies that was said to be an important component of creator remuneration and also a source of socio-cultural subsidies.<sup>9</sup>

In July 2008, the European Commission set up a Stakeholder Platform including collecting societies, industry representatives and consumer organisations with the aim to negotiate a consensus about modernising the system of private copy levies. Little progress was made, and in January 2010, representatives of the information technology, consumer electronics and telecommunications sectors (coordinated under the Digital Europe umbrella) withdrew from the talks. ICT firms have since focussed on challenging levy tariffs through the court system, while calling for a regulation of levies as part of a Directive on Pan-European Licensing.<sup>10</sup>

In May 2011, The European Commission published an intellectual property strategy paper announcing “comprehensive legislative action” regulating levy systems by 2012, following a further period of attempted mediation. Section 3.3.4 is headed “Private copying levies”:<sup>11</sup>

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6 This reasoning is sometimes extended to all exceptions: they should be eliminated where transaction costs between owner and users become low enough for negotiations to occur (the transaction cost rationale for copyright exceptions is discussed in Study III: Framework for analysis).

7 For a comprehensive analysis of the “phase out” agenda of the Information Society Directive, see P.B. Hugenholtz, L. Guibault, S. van Geffen (2003), *The Future of Levies in a Digital Environment*, Amsterdam: Institute for Information Law (IViR).

8 Green Paper - Copyright and Related Rights in the Information Society, COM/95/0382, at 50 (emphasis added by 2006 Impact Evaluation, at 14): “where there is the technical means to limit or prevent private copying, there is *no further justification for what amounts to a system of statutory licensing and equitable remuneration*”<sup>8</sup>. 2006 Impact Evaluation for Recommendation, at 58: “Where a rightholder has authorised an activity in exercising his exclusive rights, no claim for compensation should arise as the person performing the activity, i.e. the consumer, is a licensee here and not a beneficiary of the exception.”

9 “Industry Condemns Commission Backdown on Reform: Reform of Copyright Levies Abandoned Following Opposition From France”, Statement by Copyright Levies Reform Alliance (13 December 2006, [http://www.eicta.org/fileadmin/user\\_upload/document/document1166542590.pdf](http://www.eicta.org/fileadmin/user_upload/document/document1166542590.pdf)). According to French lobby platform copie privée (<http://www.copieprivee.org>, accessed May 2011) levies contribute to artistic vitality “by remunerating the creators we love and by helping nearly 5,000 cultural events we enjoy attending all over France. Private copy is necessary for music, cinema, theatre, dance, television, radio, photography, circus acts and literature to live.” In France, 25% of collected revenues (in 2010, just under €50m) are used to fund cultural events (cf. discussion of levies as an “off balance sheet tax” in Study III below).

10 Statement by Digital Europe on the Collapse of Stakeholder Platform on Private Copy Levies (7 January 2010): [http://www.digitaleurope.org/index.php?id=32&id\\_article=404](http://www.digitaleurope.org/index.php?id=32&id_article=404). Digital Europe advert in *European Voice* (10 July 2010): “The announced Collective Rights Management Directive provides the perfect opportunity to modernise the EU levies regime.”

11 *A Single Market for Intellectual Property Rights: Boosting creativity and innovation to provide economic growth, high quality jobs and first class products and services in Europe*, Communication from the European Commission (COM(2011) 287 final).

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The proper functioning of the internal market also requires conciliation of private copying levies with the free movements of goods to enable the smooth cross-border trade in goods that are subject to private copying levies. Efforts will be redoubled to kick-start a stakeholder agreement built on the achievements of a draft Memorandum of Understanding (MoU) brokered by the Commission in 2009. A high level independent mediator will be appointed in 2011 and tasked with exploring possible approaches with a view to harmonising the methodology used to impose levies, improve the administration of levies, specifically the type of equipment that is subject to levies, the setting of tariff rates, and the inter-operability of the various national systems in light of the cross-border effects that a disparate levy system has on the internal market. A concerted effort on all sides to resolve outstanding issues should lay the ground for comprehensive legislative action at EU level by 2012.

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## Sources of data

In Europe, the political economy of levy lobbying divides roughly along the following lines:<sup>12</sup>

Collecting societies: strongly in favour

ICT sector (including Amazon, Apple, Dell, HP, Nokia, RIM): strongly against

Major music right holders (including Universal, Sony, Warner, EMI): ambivalent (may benefit from “licensing through”)

Music SMEs: in favour

Artists’ representatives: in favour

Consumer organisations: against

Interested parties have commissioned consultancy reports, providing supporting evidence. Key submissions reviewed include:

- ICT sector: Nathan Associates 2006 (commissioned by CLRA)<sup>13</sup>, Copyright Levy Reform Alliance (CLRA) 2006<sup>14</sup>, Ferreira 2010 (commissioned by HP)<sup>15</sup>, Oxera 2011 (commissioned by Nokia)<sup>16</sup>;
- Collecting Societies: EconLaw 2007 (commissioned by GESAC)<sup>17</sup>;
- Artists: YOUNISON 2010<sup>18</sup>;
- Consumers: Rogers/Tomalin/Corrigan 2009<sup>19</sup>.

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12 As part of the research for this report, the UK Intellectual Property Office facilitated a stakeholder workshop on copyright levies on 1 December 2010 which was attended by a cross-section of interested parties, including Owen Atkinson (Authors’ Licensing and Collecting Agency), Alan Dearling (Author), Martin Delaney (Copyright Licensing Agency), Karen Fishman (MCPS-PRS Alliance Ltd), Tim Frain (Nokia), Tuomas Haanpera (Oxera), Sam Ingleby (representing Apple), Peter Jenner (Music Managers’ Forum), Jim Killock (Open Rights Group), Florian Koempel (UK Music), Victoria Lustigman (Publishers’ Association), Amanda Russell (Producers’ Alliance for Cinema and Television), Laura Sallstrom (Dell), Nicola Searle (ESRC/IPO Fellow, University of Abertay), Saskia Walzel (Consumer Focus).

13 Economic Impact Study: Private Copying Levies on Digital Equipment and Media – Direct Effects on Consumers and Producers and Indirect Effects on Sales of Online Music and Ringtones, report prepared by Nathan Associates for Copyright Levies Reform Alliance (May 2006).

14 Analysis of National Levy Schemes and the EU Copyright Directive, EICTA/BSA/European-American Business Council/RIAE/EDIMA (April 2006).

15 José Luis Ferreira (2010), “Compensation for Private Copying: An Economic Analysis of Alternative Models”, ENTER–IE Business School.

16 Is There a Case for Copyright Levies? An economic impact analysis (report prepared for Nokia), Oxera Consulting Ltd (April 2011).

17 Economic Analysis of Private Copy Remuneration, Report prepared by EconLaw Strategic Consulting for Groupement Européen des Sociétés d’Auteurs et Compositeurs (GESAC) (September 2007).

18 Transparency & Accountability in Collective Rights Management, YOUNISON (2010).

19 Mark Rogers, Joshua Tomalin and Ray Corrigan (2009), “The Economic Impact of Consumer Copyright Exceptions: A literature review”, Oxford: Harris Manchester College. This paper contains a pertinent critique of the economic assumptions of the studies by Nathan Associates (2006) and EconLaw (2007).

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Many of these submissions bear out the adage that he who pays the piper calls the tune. However, several studies contain verifiable data and credible analytical tools.

In addition, annual reports of national collecting agencies are an important source of data. Dutch collecting agency *de Thuis kopie* publishes consolidated annual surveys on global levy tariffs, revenues and distribution, now in their 21st edition. These reports are generally regarded as reliable.<sup>20</sup>

Lastly, the European Commission has conducted several consultations on copyright levy reform. In preparation for the legislative instrument of a Commission Recommendation, a Stakeholder Consultation took place in 2006 (“Copyright Levies in a Converging World”), and an Impact Evaluation was drafted (“Fair Compensation for Private Copying in a Converging Environment”). In 2008, The Commission consulted again (“Fair Compensation for Acts of Private Copying”, European Commission Background Document to questionnaire, DG MARKT, 14 February 2008). All these Commission documents as well as Stakeholder and Member State submissions were examined.<sup>21</sup>

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20 International Survey on Private Copying Law & Practice, Stichting de Thuis kopie ([www.thuiskopie.nl](http://www.thuiskopie.nl)).

21 They are publicly accessible at the portal of the Internal Market Directorate: [http://ec.europa.eu/internal\\_market/copyright/levy\\_reform/index\\_en.htm](http://ec.europa.eu/internal_market/copyright/levy_reform/index_en.htm)

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# Implementation of levy schemes

## A. Tariffs and revenues

22 out of 27 European Union members have chosen to meet the requirement of “fair compensation” for “private copying” through a levy system. The exceptions are the UK and Ireland (only time-shifting of broadcasts permitted)<sup>22</sup>, Malta, Cyprus and Luxembourg (private copying permitted but fair compensation treated as *de minimis*)<sup>23</sup>. Within the 22 countries who provide for a compensated private copying exception, levy schemes vary widely. The following table captures key variations among these levy systems:

- levies apply to different media or equipment that can be used to make copies (e.g. recordable carriers, MP3 players, printers, PCs);
- levies differ in tariffs for the same media or equipment, and apply different methods of calculation (e.g. memory capacity, % of price);
- levies differ in beneficiaries (music, audio-visual, reprographic rightholders; wider cultural or social purposes).

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22 UK: The Copyright, Designs and Patents Act 1988 permits fair dealing “for the purposes of private study” (s. 29), but only in relation to literary, dramatic, musical and artistic works (i.e. not sound recordings, films, broadcasts), and only in very narrow circumstances (not by a third party). Under section 70, the recording of a broadcast for the purposes of timeshifting “in domestic premises for private and domestic use” is permitted. Under section 50, lawful users of computer programs are permitted to make back up copies (s. 50A), and certain other acts, such as decompiling (s. 50B), and observing, studying and testing (s. 50BA). The Gowers Review of Intellectual Property (HM Treasury, 2006) recommended (unsuccessfully): “Recommendation 8: Introduce a limited private copying exception by 2008 for format shifting for works published after the date that the law comes into effect. There should be no accompanying levies for consumers; Recommendation 9: Allow private copying for research to cover all forms of content. This relates to the copying, not the distribution, of media.”

23 Luxembourg: Amendment of the Act on Copyright, Neighbouring Rights and Databases (18 April 2004, Memorial A, 2004, no. 61) implementing the Information Society Directive permits private copying and provides for fair compensation but not through a levy scheme (Article 10(4)); Cyprus: The Copyright and Related Rights (Amendment) Law of 2004; Malta: Copyright Act (Act XIII of 2000, as amended by Act IX of 2003), Article 9(1) (c): Copyright in an audiovisual work, a database, a literary work other than in the case of a computer programme, a musical or artistic work shall not include the right to authorise or prohibit – reproductions on any medium made by a natural person for private use and for ends that are neither directly nor indirectly commercial, on condition that the rightholders receive fair compensation which takes account of the application or non-application or technological measures to the work or subject-matter concerned.

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**Table 1 Levies in EU Member States (2009)  
[plus Iceland, Norway and Switzerland]**

Member State	Revenue per capita (€)	Levies applied to recordable media	Levies applied to equipment			Distribution		
			CD-R, DVD	MP3 Player	Printer	PC	Audio	Video
Austria	1.4	€0.34 (700MB) -0.54 (4.7GB)	✓	✓	-			✓
Belgium	1.2	€0.12-0.40 per unit	✓	✓	-	43.59% 1/3 authors 1/3 performers 1/3 producers	56.41% 1/3 authors 1/3 performers 1/3 producers	-
Bulgaria	?	5% of manufacturing or import price	✓	✓	-	1/3 A-P-P	1/3 A-P-P	✓
Cyprus	-	-	-	-	-	As transferred from "sister" collecting societies in levy countries		
Czech Republic	0.7	€0.008-0.021 per unit	✓	✓	✓	½ authors ½ performers /producer	60% authors 40% performers /producers	-
Denmark	0.7	8% of manufacturing or import price	-	-	-	1/3 A-P-P	1/3 A-P-P	33%
Estonia	0.1	8% of manufacturing or import price	✓	-	-	1/3 A-P-P	63% a 27% perf 10% prod	10%
Finland	1.6	€0.6 per 4.7GB	✓	-	-	49% authors 51% prod+perf	80.8% auth+perf 19.2% prod	✓
France	2.6	€1.0 per 4.7GB	✓	-	✓	½ authors ½ performers /producers	1/3 A-P-P	25%
Germany	1.5	€0.271 per 4.7GB	✓	✓	✓	42% GEMA 42% perf/prod 16% reprograph	21% GEMA 21% perf/prod 8% repro 50% film producers	-
Greece	0.13	6% of manufacturing or import price	✓	✓	-	55% creators 25% perf 20% prod	55% creators 25% perf 20% prod	-
Hungary	0.9	€0.27 per 4.7GB	✓	✓	-	45% authors 30% perf 25% prod	62% authors 13% prod 25% perf	3.3-10%
Iceland	0.6	€0.11<2GB; €32 ≥ 2GB	✓	-	-	46% auth 54% perf /prod	✓	15%
Italy	0.7	€0.41 per 4.7GB	✓	-	✓	50% authors 25% perf 25% prod	30% authors 23% perf 47% prod	✓ 50% of video
Ireland	-	-	-	-	-	As transferred from "sister" collecting societies in levy countries		

**Table 1 Levies in EU Member States (2009)  
[plus Iceland, Norway and Switzerland] Continued**

Member State	Revenue per capita (€)	Levies applied to recordable media	Levies applied to equipment			Distribution		
			CD-R, DVD	MP3 Player	Printer	PC	Audio	Video
Latvia	0.16	€0.14-0.28 per unit	✓	-	-	40% auth 30% perf 30% prod	1/3 A-P-P	10%
Lithuania	0.2	6% of manufacturing or import price	-	-	-	40% auth 30% perf 30% prod	40% auth 30% perf 30% prod	✓
Luxembourg	-	-	-	-	-	As transferred from "sister" collecting societies in levy countries		
Malta	-	-	-	-	-	As transferred from "sister" collecting societies in levy countries		
Netherlands	0.9	€0.4 per 4.7GB	-	-	-	40% auth 30% perf 30% prod	33.75% auth 25.5% perf 40.75% prod	-
Norway	0.9	€4.32m raised through direct taxation	-	-	-	Distributed through collecting societies		
Poland	0.07	1.72-2.53% of sale price	✓	✓	-	50% auth 25% perf 25% prod	35% auth 25% perf 40% prod	-
Portugal	0.3	€0.05-0.14 per unit	-	-	-	40% auth 30% perf 30% prod	40% auth 30% perf 30% prod	20%
Romania	0.02	3% of sale price	✓	✓	-	40% auth 30% perf 30% prod	✓	-
Slovakia	0.1	6% of manufacturing or import price	✓	✓	-	40% auth 30% perf 30% prod	✓	-
Slovenia	0.5	€0.03 per GB (max. €16.69)	✓	✓	-	40% auth 30% perf 30% prod	-	-
Spain	1.7	€0.17-0.44 per unit	✓	✓	-	50% auth 25% perf 25% prod	1/3 A-P-P	20%
Sweden	1.1	€0.06 (900MB) - 0.26 (4.7GB)	✓	-	-	1/3 A-P-P	✓	✓
Switzerland	2.1	€0.03 (525MB) - 0.23 (4.7GB)	✓	-	-	75% auth 25% prod/perf	23% auth 77% prod/perf	10%
United Kingdom	-	-	-	-	-	As transferred from "sister" collecting societies in levy countries		

Source: Annual reports of collecting agencies; European Commission, Background Document: "Fair compensation for acts of private copying" (2008); de Thuiskopie, *International Survey on Private Copying Law & Practice* (21st revision 2010). Summaries of tariffs and distributions are approximations. Tariffs may distinguish between DVD-R/RWs, CD-R/RW (data discs), CD-R/RW (audio discs), minidisks, USB-sticks, cassettes (audio tape), cassettes (VHS), audio players with integral storage, video players with integral storage, harddisks. The precise formula for distribution may allocate percentages to writers, translators, journalists, directors, set designers, choreographers, actors, dancers, composers/songwriters, musicians/conductors, singers/artists, cameramen, editors, photographers, publishers and producers (text, music, film).

The results of these variations are different levels of levy density, i.e. how many transactions are involved in raising and distributing monies, as well as different levels of overall indirect taxation on manufacturers, importers, distributors or consumers of media and equipment (see Study II for empirical data on who pays for the levy).

Regulatory structures also differ considerably. Are tariffs and distribution set in law or subject to negotiations? Are there appeal procedures? What are the required standards of governance and supervision of collecting agencies? These questions go beyond the scope of this report but would have to be addressed in any meaningful Europe-wide regulation of the system.

Following the 2001 Information Society Directive, total revenues from levy systems in the EU increased from €172 million in 2001 to €567 million in 2004. Collection plateaued around the €500 million mark between 2004 and 2008, and is now beginning to fall as blank tapes, CDs and DVDs are disappearing from the market, and levies on new products are increasingly contested, resulting in considerable uncertainty. There is an increasing gap between claimed (but unpaid) and paid (but contested) tariffs.

Recent regulatory interventions varying scale and scope of copyright levies include:

- 1 January 2008: Amendment to German copyright law (*UrhG 2. Korb*): Tariffs in law replaced by negotiated tariffs between manufacturers and collecting agency ZPÜ; about €20m of fees withheld by manufacturers.
- 24 February 2009: Decision by highest Austrian court (OGH, 4 Ob 225/08d); PC levy cancelled; compensation can only be due on equipment that is designed for copying.
- 21 October 2010: Padawan SL v Sociedad General de Autores y Editores de España (SGAE), Case C-467/08, ECJ: Business media and equipment not leviable; Spanish collecting societies may have to return certain fees collected under Art. 25 of the *Ley de Propiedad Intelectual*.
- 11 April 2011: Dutch State Secretary for Public Safety and Justice Fred Teeven announces phasing out of levies (levies on recordable CDs will not be replaced by schemes on new media or equipment).

Across the EU, there are currently nine countries where levies for mobile phones are claimed but contested, amounting to about €192 million in 2010 which may or may not become payable.<sup>24</sup>

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24 Information from Digital Europe. For this report, the author made a sample calculation of potential liability for one manufacturer (Nokia) in the German market: Latest published levy tariffs (July 2010): Mobiles with touchscreen: €11, without touchscreen €4. Old tariffs (prior to 1 Jan 2008): Phone with music recording: €2.56 or €1.28 per phone plus €1,02 per 1GB memory capacity. Nokia's market share in 2009 was about 35% (of 51m mobile phone users = 17.85m). 17.85m x €2.56 (basic old tariff) makes a conservative liability exceeding €45m. Given that every fourth mobile sold in Germany in 2010 is a smart phone (= 6.5m of a total of 26m), and that Nokia had a market share of 28-29% (= 1.8m), that would incur a potential liability of close to €20m for 2010 for smartphones alone. In November 2009, 21% of German mobile subscribers used the phone for online music via application or browser (ComScore, 26 January 2010).

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The following table captures the evolution of total collected revenues from levy schemes since the introduction of the requirement of “fair compensation” in the 2001 Information Society Directive.

**Table 2 Aggregate Revenues from Copyright levy schemes in the EU (2002-2009)**

Year	Total Revenues (in € million)
2001	172.63
2002	291.34
2003	376.47
2004	567.77
2005	562.19
2006	548.01
2007	549.41
2008	526.28
2009	414.93

Source: For 2005-2009, data collated by de Thuiskopie (*International Survey on Private Copying Law & Practice*, 21st revision 2010) was used to calculate aggregate revenues. For 2001-2004, figures communicated in European Commission documents were used, credited to de Thuiskopie and Business Software Alliance. Countries included are Austria, Belgium, Czech Republic, Denmark, Estonia, Finland, France, Germany, Greece, Hungary, Italy, Latvia, Lithuania, The Netherlands, Poland, Portugal, Romania, Slovakia, Slovenia, Spain and Sweden. Bulgaria has a levy scheme by statute but no reported collection. Cyprus, Ireland, Luxembourg, Malta and the United Kingdom have no copyright levies.

## B. Distribution

Revenues from private copying levies account for varying parts of the income of European collecting societies. The formula for distribution differs between audio and video schemes (see table in previous section). The following table indicates the percentages of levy income for a selection of music (mechanical and performing rights) societies:

**Table 3 Levy income as percentage of total collecting society revenues (2009)**

	<b>STEMRA</b> (Netherlands)	<b>SABAM</b> (Belgium)	<b>SGAE*</b> (Spain)	<b>SACEM</b> (France)	<b>GEMA**</b> (Germany)
<b>Total revenues (€000)</b>	40,680	192,434	333,936	762,309	862,961
<b>Levy revenues (€000)</b>	3,533	7,697	16,000	55,041	49,098
<b>Levy as % of total revenues</b>	<b>8.7%</b>	<b>4%</b>	<b>4.8%</b>	<b>7.2%</b>	<b>5.7%</b>

Source: Annual reports (latest available): \*SGAE 2008; \*\*GEMA 2010

YOUNISON, a European lobby platform for artists (<http://www.younison.eu>), has analysed the accounting statements of six Belgian authors, as received from the main music collecting society SABAM (mechanical and performing rights of songwriters and music publishers). The authors' distribution share of levy income appears to be less than 0.65%. Prospective levy remuneration is unlikely to contribute to authors' decisions to write new music.<sup>25</sup>

**Table 4 Music authors' share of levy income in Belgium (SABAM, 2009)**

Description of Author	Physical Sales (albums/	Digital	Total	Levy	Levy as % of Total Authors' Rights Revenue	Levy Revenue
Top dance charts USA	650,000	24,689	164,497	582	0.35%	0.00090
Pop band highest position 1997: 17 <sup>th</sup>	95,000	1,200	11,955	60	0.50%	0.00063
DJ/producer Label owner	106,000	800	14,217	27	0.19%	0.00025
Author/producer 35 <sup>th</sup> Belgian charts 2004	32,000	450	7,737	50	0.65%	0.00156
Singer/author popbands werchter Top 10	35,000	1,500	10,071	35	0.35%	0.00100
Top 10 British Charts	185,000	750	14,350	65	0.45%	0.00035

Source: YOUNISON (Transparency & Accountability in Collective Rights Management, 2010).

25 For further discussion of inventive and reward rationales for levy schemes, see Study III.

## C. Consumer permissions

The previous two sections explained the unusual structure of a complex system of indirect remuneration of creators and investors, as well as (in some countries) of funding for wider social and cultural purposes. This section deals with the consumer permissions associated with these payments for “private copying”.

The narrow focus of private copying exceptions does not map well onto typical copying behaviour in digital networks. Users may consider activities under the following headings to be private:

- (i) Making back-up copies / archiving / time shifting / format shifting
- (ii) Passing copies to family / friends
- (iii) Downloading for personal use
- (iv) Uploading to digital storage facilities
- (v) File sharing in digital networks
- (vi) Online publication, performance and distribution within networks of friends
- (vii) User generated content / mixing / mash-up (private activities made public)

In the analogue world, the private copying exception was aimed to permit discrete copies for non-commercial use in categories (i) and (ii). In digital networks, the distinction between private and public spheres has become blurred. Regularly, new services are invented that challenge earlier divisions (P2P, social networks, cloud lockers).

Under the Information Society Directive, only activities (i), (ii) and (iii) can possibly fall under the reproduction right (and therefore be eligible for a compensatable exception as private copying). Even within these groups of activities, the scope and legal construction of private copying differs considerably between countries. In some countries, sources need to be lawful, in others not; in some countries, there are a set number of permitted copies specified<sup>26</sup>, in others there are definitions of private circles<sup>27</sup>; in some countries, the levy is constructed as a statutory licence, in others as a debt.

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26 For example, German case law indicates (BGH, GRUR 1978, 474) that making up to seven copies for non-commercial purposes remains within the ambit of “private copying”.

27 In most countries, the private sphere for the purposes of the exception is limited to a natural person, their family and close circle of friends (not a “friend” in an online social network). For example, Denmark’s 2003 amendments of her copyright law, implementing the Information Society Directive, narrowed the private copy exception to apply only strictly within the family circle, and no longer available for borrowed or rented media (p. 56, n. 57, EC 2006 Impact Assessment).

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There is a vigorous academic debate whether “private copying” could be conceived as a user right, i.e. as something that could be asserted against the copyright owner, or if the exception is derived from a lack of enforceability, and can be overridden by contract and/or technological measures.<sup>28</sup> These legal arguments reflect the overall policy uncertainty about the levy system: What is the policy designed to achieve? Is state regulated compensation an alternative, or a complement to private enforcement? In many countries, there is a confusing reluctance to acknowledge that any consumer permissions are associated with levy payments.

This ambiguity has been particularly acute in a widely reported recent case from the Netherlands. In *ACI et al. v Stichting de Thuiskopie*, the Court of Appeal of The Hague argued that the legitimate interests of the right holders are more adequately protected in a regime that allows downloading from unlawful sources.<sup>29</sup> Across Europe, there is a trend by legislators and courts to remove all copies from unlawful sources from the scope of the private copy exception.<sup>30</sup>

Consider evidence on the extent of private copying presented to the Copyright Board in Canada (where evidence is compiled and scrutinised in a transparent manner). It shows that in 2006-2007, portable music players (such as iPods) contained on average 497 tracks of music, of which 96% were copied. In total, 1.63 billion copies of tracks were being made in Canada from July 2006 to June 2007. Of these, about half (808 million) were copied on digital recorders; of these 808 million, about 345 million (42%) came from the Internet. Only 20% of these tracks were authorised downloads (e.g. from iTunes). Thus, from July 2006 to June 2007, there were

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28 According to Article 6 of the Information Society Directive, there must be legal sanctions against the circumvention of anti-copying measures (“effective technological measures”). Section 6(4) then offers muddled wording that encourages Member States to ensure that copyright exceptions remain available “where the beneficiary has legal access to the protected work or subject matter concerned”. With respect to private copying, this is qualified: “unless reproduction for private use has already been made possible by rightholders to the extent necessary to benefit from the exception or limitation concerned and in accordance with the provisions of Article 5(2)(b) and (5), without preventing rightholders from adopting adequate measures regarding the number of reproductions in accordance with these provisions”. In the *Mulholland Drive* test case, a French consumer sought to transfer a copy protected DVD into VHS format to watch it at his mother’s house. The French Supreme Court (Court de cassation, case 05-15824, 28 February 2006) held that the exception for private copying could not be invoked against effective technological measures if the act of copying would conflict with the so-called “three step test” (Art. 9(2) Berne Convention, incorporated into Art. 5(5) of the Information Society Directive). Cf. Christophe Geiger (2008), “The Answer to the Machine Should Not Be the Machine: Safeguarding the Private Copy Exception in the Digital Environment”, *European Intellectual Property Review* (EIPR) 121. Switzerland has adopted a different implementation: Copyprotection measures cannot be enforced against users if circumvention serves only to exercise an act permitted in law (Urheberrecht 1992, Art. 39a). Under this interpretation, private copying is close to a user right. For a survey of the landscape, see Kretschmer, Derclaye, Favale, Watt (2010), *The Relationship between Copyright and Contract Law: A Review commissioned by the UK Strategic Advisory Board for Intellectual Property Policy*, London: SABIP (2010).

29 Cf. English summary of the case by Vivien Rörsch at <http://the1709blog.blogspot.com/2010/11/copyright-owners-better-off-in-regime.html>.

30 2008 amendment to German copyright law (*UrhG 2. Korb*) excludes copies from “evidently unlawful sources” (“offensichtlich rechtswidrig öffentlich zugänglich”). France: Copies from illegal sources (including those “uploaded” in breach of the making available right) do not fall under the exception for private copying (EC 2006 Impact Assessment, p. 57).

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646 million copies being made from unauthorised Internet sources that found their way on the typical portable music player.<sup>31</sup>

In most European countries, despite operating a system of fair compensation, these 646 million tracks could not be covered by levy payments. By focusing on sources rather than consumer activities, the copyright system becomes hard to understand.

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31 Exhibit CPCC-3: *Étude de marché sur la copie privée d'enregistrements musicaux au Canada 2006-2007* (11 January 2008); 695pp report prepared by Réseau Circum for Société canadienne de perception de la copie privée (CPCC). The methodology is based on monthly telephone surveys of about 1,000 Canadians (above the age of 12), a sample representative of all Canadians. The data in the report are based on 12,011 "entrevues" between July 2006 and June 2007. Many thanks to Gilles McDougall, Copyright Board of Canada, for correspondence on the matter.

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# Study II: Empirical effects of Copyright levy schemes

As an empirical starting point for assessing the economic effects of levy schemes, three product level studies were conducted, plotting retail prices against levy and VAT rates in a selection of 20 countries. This data should help to establish who is paying for the system (consumers, retailers, manufacturers), whether there are implications for product innovation and launch, and if there are trade effects (cross border arbitrage, pan-European price points regardless of levies).

## Methodology

### A. Selection of products

Product selection was governed by two criteria. (1) There should be clear variations between the national levy tariffs applying to the selected products, so that cross border effects may become visible; (2) Products should include commoditised goods, and devices at the edge of fast moving technology, so that innovation effects may become visible. In addition, we tried to select products for which the manufacturers were prepared to assist with verifying tariffs (as levy setting and administration is far from transparent in many countries).

The following products were researched:

- Printer: Hewlett Packard Officejet 4500 AIO; Laserjet M1132
- Music/video/game device: Apple iPod Touch (8, 32 & 64 GB)
- Tablet computer: iPad1, Samsung Galaxy, iPad2

### B. Selection of countries

Country selection was governed by the following criteria. (1) We selected the four countries that account for about 75% of levy revenues in the EU: France, Germany, Spain and Italy. (2) We then added countries where crossborder effects with these large markets should be most prominent, because of market integration and common languages: Belgium, Netherland, Luxembourg, Austria, Switzerland, Poland. (3) Two more EU countries were included which have no levies at all: Ireland and the UK. (4) We added the home markets of major new technology used in the products: USA, Japan, Korea. (5) We added several countries with special characteristics: Sweden (as early adopter of technology); Norway (because of its unique "alternative compensation" system under which direct tax revenues provide "fair compensation" for private copying: see Study III); Latvia (as a recent Eastern European member of the EU where the author had some market knowledge from an earlier study for the European

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Commission); Canada (because of market integration with the US, and because its system of levy administration is uniquely transparent, governed by a Copyright Board: see Study III); and India (as a major new market where one of the researchers had detailed market knowledge).<sup>1</sup>

## C. Data Collection

**VAT Rates:** Since there is no unified VAT in the USA & Canada (with every state having a varying system of General Sales Tax), an average VAT equivalent was calculated to assist in comparison with the majority of countries under consideration having a unified VAT system.

**Exchange Rates:** The following exchange rates were used to report all price data in Euros: 1 Euro = 0.88 British pound, 7.85 Norwegian krone, 9.02 Swedish krona, 3.95 Polish zloty, 0.71 Latvian lats, 1.44 US dollars, 1.39 Canadian dollars, 120.63 Japanese yen, 64.81 Indian rupees, 1.29 Swiss francs, 1585.84 Korea won (Source: [www.oanda.com](http://www.oanda.com) using historical rate search interface for 15 April 2011)

**Levy Rate:** The levy tariffs for various product categories were initially gathered from de ThuisKopie (International Survey on Private Copying Law & Practice 2010). Precise levy rates were then validated through direct communications with HP (for printers) and Apple (for iPods and tablets).

**Tablet Launch Dates:** Most of the launch dates for the iPad were sourced from Apple.com's PR Library (with the exception of Norway, Sweden, Poland, Latvia, India and Korea). All launch dates for the iPad2 are from Apple.com's PR library. All launch dates for the Samsung Galaxy Tab were sourced from a general internet search.

**Price Data:** A structured approach was followed for establishing retail prices. The following methodological decisions were taken:

(i) A VAT inclusive price for each product was sourced. The lowest available price was taken, using price comparison sites as well as Google Product Search (where available). Prices were sourced in April 2011.

(ii) A distinction was made between Online and Physical Prices. Online price refers to the price of a product in store which sells only online (and where delivery is direct to a customer by courier). In many cases across Europe, these retailers happened to be one of the large consolidated retail houses such as Amazon or DSGI). The physical price refers to the price of a product either in a physical store environment, or where a product may be booked online and then needs to be picked up from a physical location. In a few instances where a physical price was unavailable for specific product (mostly for the iPad), the price mentioned on Apple's country specific site was taken to be the physical price, the rationale being that that Apple usually sold at the recommended or suggested retail price.

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1 Although it would have been desirable to add China, it was not possible to source consistent data.

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(iii) The exact model (and generation of the product) was searched. For example, the Apple iPod Touch is available in several generations. For the purposes of this research, only the 4th generation product was tracked. Similarly, the Galaxy Tab prices are of the P1000 model. In Japan, the printer Officejet 4500 was deemed not available for sale and the closest model available was Officejet 6500.

(iv) The prices are of brand new products available to consumers through retailers. Refurbished and/or auction site products were not taken into consideration.

## D. Data analysis

- The first table and graphic for each product group represent the relation of retail price and levy, with descending levy tariffs from left to right.
  - The second table and graphic for each product group represent the relation of retail price and VAT, with descending VAT rates from left to right.
  - The third table and graphic for each product group represents the relation between retail price and “aggregate indirect charges” (i.e. levy + VAT).
  - For tablet computers, an additional table of launch dates was compiled, in order to explore the effect of levies and VAT on launch decisions of innovative products.
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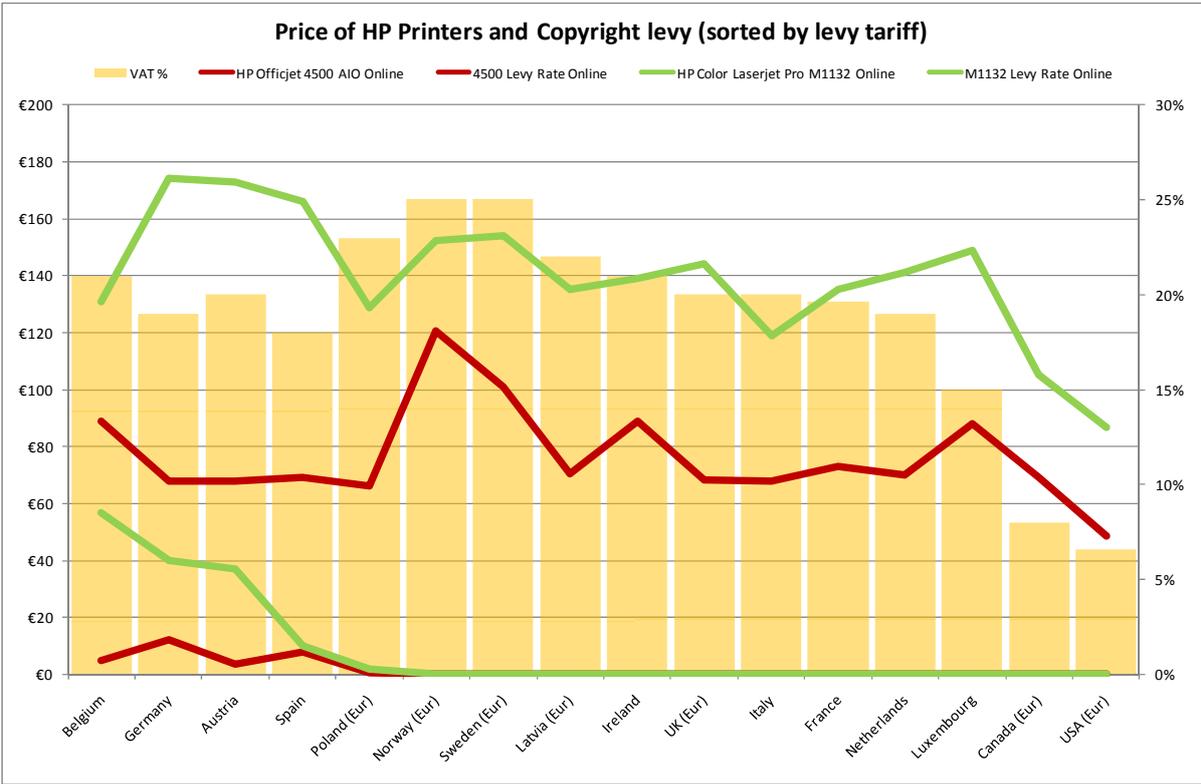
## Product Study 1: Printers

**Table 1 Price of HP Printers & Copyright levy (sorted by levy tariff)**

	VAT %	Officejet 4500 AIO Online	Officejet 4500 AIO Physical	Levy*	Color Laserjet M1132 Online	Color Laserjet M1132 Physical	Levy*
Belgium	21%	€ 89	€ 70	€ 4.70	€ 131	€ 180	€ 56.54
Germany	19%	€ 68	€ 65	€ 12	€ 174	€ 199	€ 40
Austria	20%	€ 68	€ 90	€ 3.67	€ 173	€ 185	€ 36.85
Spain	18%	€ 69	€ 69	€ 7.95	€ 166	€ 167	€ 10
Poland	23%	€ 66	€ 69	€ 0.72	€ 129	€ 159	€ 1.75
Norway	25%	€ 120	€ 127	€ 0	€ 152	€ 158	€ 0
Sweden	25%	€ 101	€ 100	€ 0	€ 154	€ 155	€ 0
Latvia	22%	€ 70	NA	€ 0	€ 135	NA	€ 0
Ireland	21%	€ 89	€ 87	€ 0	€ 139	€ 142	€ 0
UK	20%	€ 68	€ 80	€ 0	€ 144	€ 142	€ 0
Italy	20%	€ 68	€ 70	€ 0	€ 119	€ 150	€ 0
France	19.6%	€ 73	€ 79	€ 0	€ 135	NA	€ 0
Netherlands	19%	€ 70	€ 70	€ 0	€ 141	€ 139	€ 0
Luxembourg	15%	€ 88	€ 172	€ 0	€ 149	€ 191	€ 0
India	12.5%	€ 117	€ 116	€ 0	NA	NA	€ 0
Korea	10%	€ 79	NA	€ 0	€ 105	NA	€ 0
Switzerland	8%	€ 78	€ 78	€ 0	€ 124	€ 124	€ 0
Canada	8%	€ 69	€ 72	€ 0	€ 105	€ 143	€ 0
USA	6.6%	€ 49	€ 49	€ 0	€ 87	€ 118	€ 0
Japan	5%	€ 132	NA	€ 0	NA	NA	€ 0

\* The levy rate has been calculated for the online price.

Graphic 1

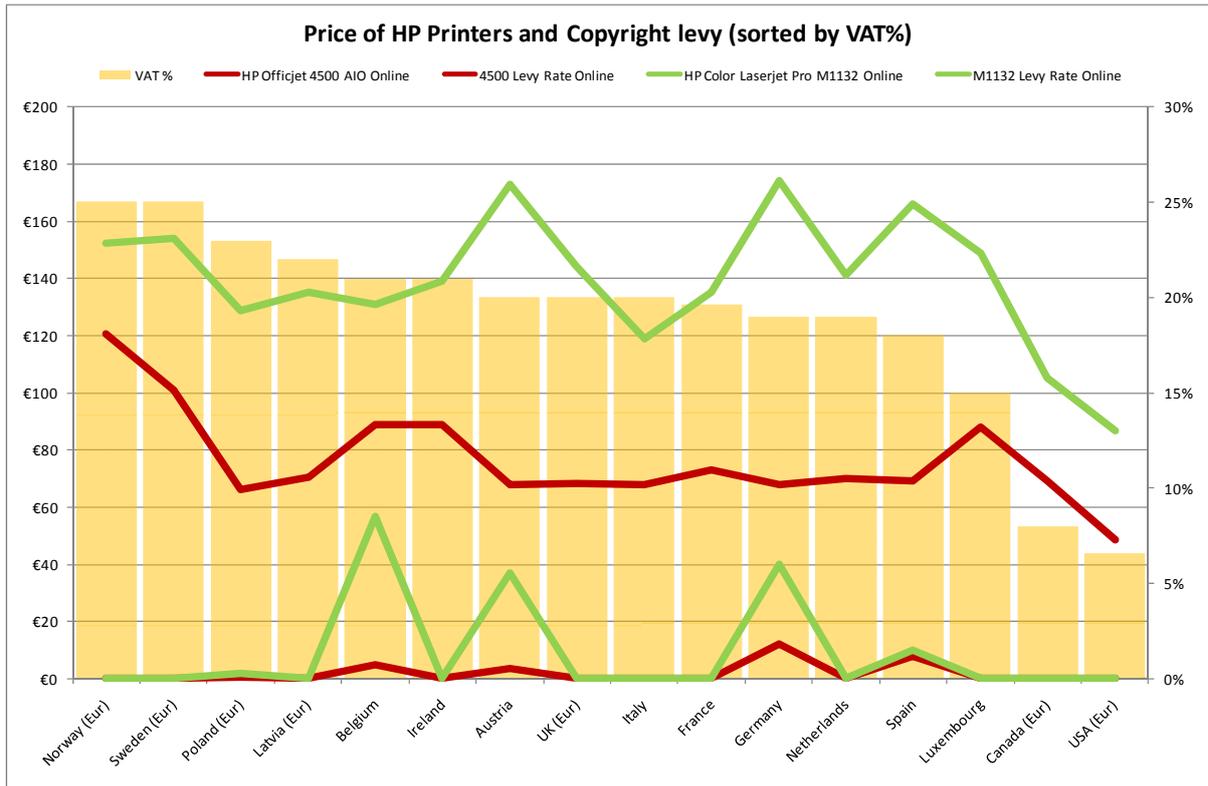


**Table 2 Price of HP Printers & Copyright levy (sorted by VAT%)**

	VAT %	Officejet 4500 AIO Online	Officejet 4500 AIO Physical	Levy*	Color Laserjet M1132 Online	Color Laserjet M1132 Physical	Levy*
<b>Norway</b>	25%	€ 120	€ 127	€ 0	€ 152	€ 158	€ 0
<b>Sweden</b>	25%	€ 101	€ 100	€ 0	€ 154	€ 155	€ 0
<b>Poland</b>	23%	€ 66	€ 69	€ 0.72	€ 129	€ 159	€ 1.75
<b>Latvia</b>	22%	€ 70	NA	€ 0	€ 135	NA	€ 0
<b>Belgium</b>	21%	€ 89	€ 70	€ 4.70	€ 131	€ 180	€ 56.54
<b>Ireland</b>	21%	€ 89	€ 87	€ 0	€ 139	€ 142	€ 0
<b>Austria</b>	20%	€ 68	€ 90	€ 3.67	€ 173	€ 185	€ 36.85
<b>UK</b>	20%	€ 68	€ 80	€ 0	€ 144	€ 142	€ 0
<b>Italy</b>	20%	€ 68	€ 70	€ 0	€ 119	€ 150	€ 0
<b>France</b>	19.6%	€ 73	€ 79	€ 0	€ 135	NA	€ 0
<b>Germany</b>	19%	€ 68	€ 65	€ 12.00	€ 174	€ 199	€ 40.00
<b>Netherlands</b>	19%	€ 70	€ 70	€ 0	€ 141	€ 139	€ 0
<b>Spain</b>	18%	€ 69	€ 69	€ 7.95	€ 166	€ 167	€ 10.00
<b>Luxembourg</b>	15%	€ 88	€ 172	€ 0	€ 149	€ 191	€ 0
<b>India</b>	12.5%	€ 117	€ 116	€ 0	NA	NA	€ 0
<b>Korea</b>	10%	€ 79	NA	€ 0	€ 105	NA	€ 0
<b>Switzerland</b>	8%	€ 78	€ 78	€ 0	€ 124	€ 124	€ 0
<b>Canada</b>	8%	€ 69	€ 72	€ 0	€ 105	€ 143	€ 0

\* The levy rate has been calculated for the online price.

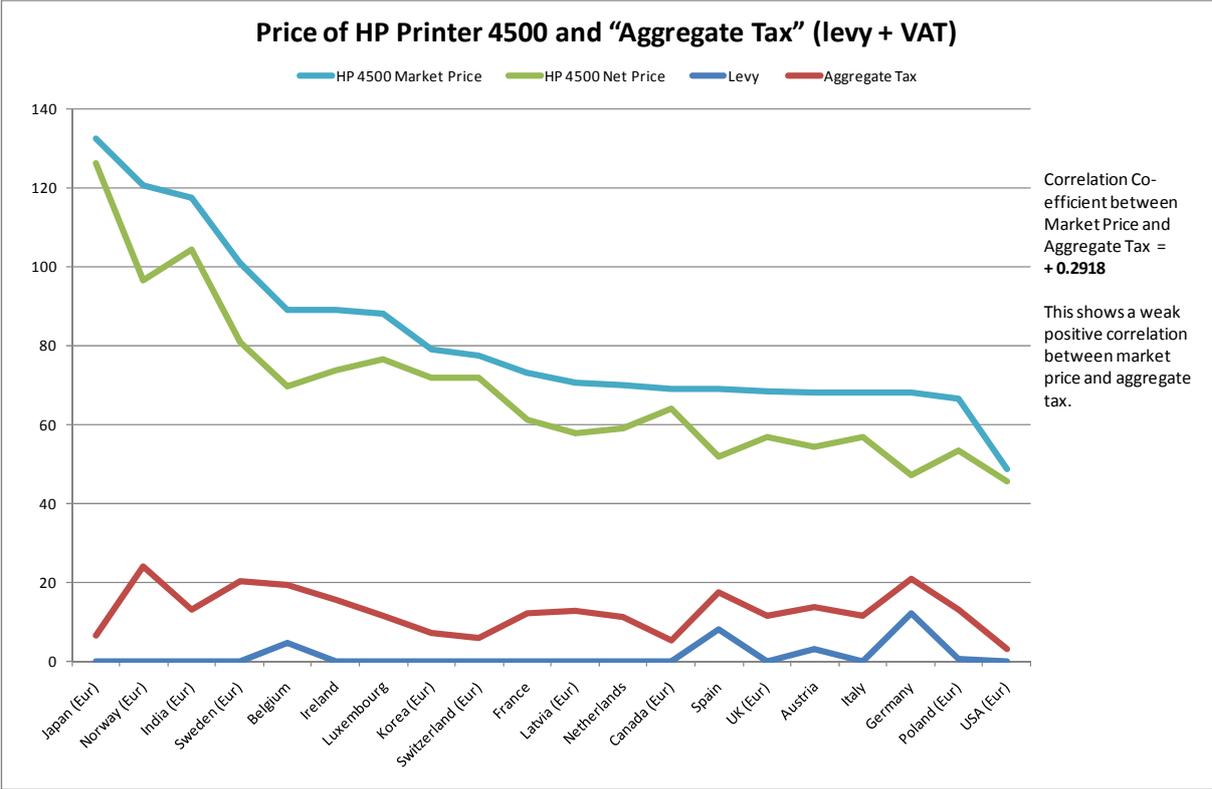
## Graphic 2



**Table 3 Price of HP Printer 4500 and “Aggregate Charges” (levy + VAT)**

	VAT %	HP 4500 Market Price	HP 4500 Net Price	VAT	Levy	Aggregate Charges
<b>Japan</b>	5.0%	€ 132.31	€ 126.01	€ 6.30	€ 0.00	€ 6.30
<b>Norway</b>	25.0%	€ 120.38	€ 96.31	€ 24.08	€ 0.00	€ 24.08
<b>India</b>	12.5%	€ 117.27	€ 104.24	€ 13.03	€ 0.00	€ 13.03
<b>Sweden</b>	25.0%	€ 100.89	€ 80.71	€ 20.18	€ 0.00	€ 20.18
<b>Belgium</b>	21.0%	€ 89.00	€ 69.67	€ 14.63	€ 4.70	€ 19.33
<b>Ireland</b>	21.0%	€ 89.00	€ 73.55	€ 15.45	€ 0.00	€ 15.45
<b>Luxembourg</b>	15.0%	€ 88.00	€ 76.52	€ 11.48	€ 0.00	€ 11.48
<b>Korea</b>	10.0%	€ 78.82	€ 71.65	€ 7.17	€ 0.00	€ 7.17
<b>Switzerland</b>	8.0%	€ 77.52	€ 71.78	€ 5.74	€ 0.00	€ 5.74
<b>France</b>	19.6%	€ 73.00	€ 61.04	€ 11.96	€ 0.00	€ 11.96
<b>Latvia</b>	22.0%	€ 70.42	€ 57.72	€ 12.70	€ 0.00	€ 12.70
<b>Netherlands</b>	19.0%	€ 70.00	€ 58.82	€ 11.18	€ 0.00	€ 11.18
<b>Canada</b>	8.0%	€ 69.06	€ 63.95	€ 5.12	€ 0.00	€ 5.12
<b>Spain</b>	18.0%	€ 69.00	€ 51.74	€ 9.31	€ 7.95	€ 17.26
<b>UK</b>	20.0%	€ 68.18	€ 56.82	€ 11.36	€ 0.00	€ 11.36
<b>Austria</b>	20.0%	€ 68.00	€ 54.23	€ 10.85	€ 2.93	€ 13.77
<b>Italy</b>	20.0%	€ 68.00	€ 56.67	€ 11.33	€ 0.00	€ 11.33
<b>Germany</b>	19.0%	€ 68.00	€ 47.06	€ 8.94	€ 12.00	€ 20.94
<b>Poland</b>	23.0%	€ 66.33	€ 53.45	€ 12.29	€ 0.58	€ 12.88
<b>USA</b>	6.6%	€ 45.61	€ 45.60	€ 3.01	€ 0.00	€ 3.01

Graphic 3

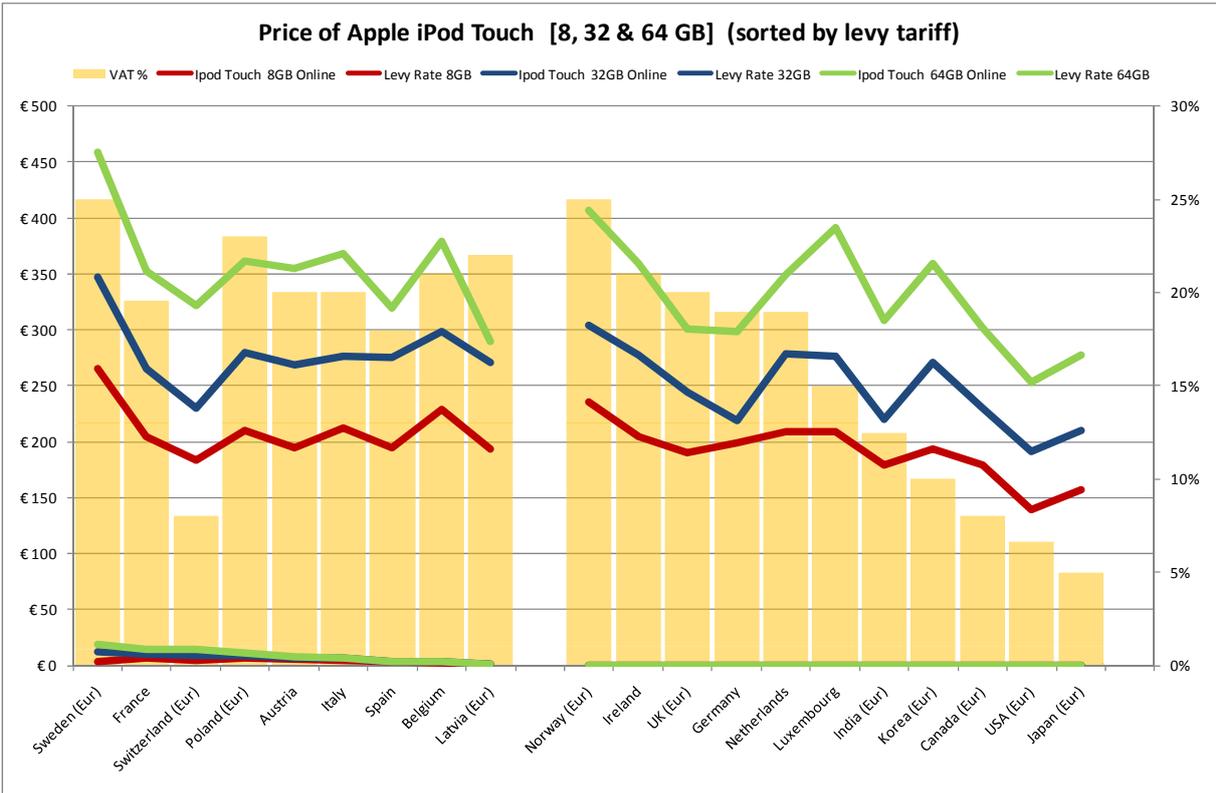


## Product Study 2: Music/Video/Game device

**Table 4 Price of Apple iPod Touch [8, 32 & 64 GB]  
(sorted by levy tariff)**

	VAT %	iPod Touch 8GB Online	Levy Rate 8GB	iPod Touch 32GB Online	Levy Rate 32GB	iPod Touch 64GB Online	Levy Rate 64GB
<b>Sweden</b>	25%	€ 266	€ 3.12	€ 347	€ 12.48	€ 459	€ 19.40
<b>France</b>	19.6%	€ 205	€ 7.00	€ 265	€ 10.00	€ 353	€ 15.00
<b>Switzerland</b>	8%	€ 184	€ 4.24	€ 229	€ 9.28	€ 322	€ 14.72
<b>Poland</b>	23%	€ 210	€ 6.29	€ 280	€ 8.41	€ 362	€ 10.85
<b>Austria</b>	20%	€ 195	€ 6.00	€ 269	€ 7.00	€ 355	€ 8.00
<b>Italy</b>	20%	€ 212	€ 4.51	€ 276	€ 6.44	€ 368	€ 6.44
<b>Spain</b>	18%	€ 195	€ 3.15	€ 275	€ 3.15	€ 319	€ 3.15
<b>Belgium</b>	21%	€ 229	€ 2.50	€ 299	€ 3.00	€ 379	€ 3.00
<b>Latvia</b>	22%	€ 193	€ 1.42	€ 270	€ 1.42	€ 290	€ 1.42
<b>Norway</b>	25%	€ 236	€ 0	€ 304	€ 0	€ 406	€ 0
<b>Ireland</b>	21%	€ 205	€ 0	€ 278	€ 0	€ 359	€ 0
<b>UK</b>	20%	€ 190	€ 0	€ 244	€ 0	€ 301	€ 0
<b>Germany</b>	19%	€ 199	€ 0	€ 219	€ 0	€ 299	€ 0
<b>Netherlands</b>	19%	€ 209	€ 0	€ 279	€ 0	€ 349	€ 0
<b>Luxembourg</b>	15%	€ 209	€ 0	€ 276	€ 0	€ 391	€ 0
<b>India</b>	12.5%	€ 179	€ 0	€ 220	€ 0	€ 309	€ 0
<b>Korea</b>	10%	€ 193	€ 0	€ 271	€ 0	€ 359	€ 0
<b>Canada</b>	8%	€ 179	€ 0	€ 229	€ 0	€ 301	€ 0
<b>USA</b>	6.61%	€ 139	€ 0	€ 191	€ 0	€ 253	€ 0
<b>Japan</b>	5%	€ 158	€ 0	€ 210	€ 0	€ 278	€ 0

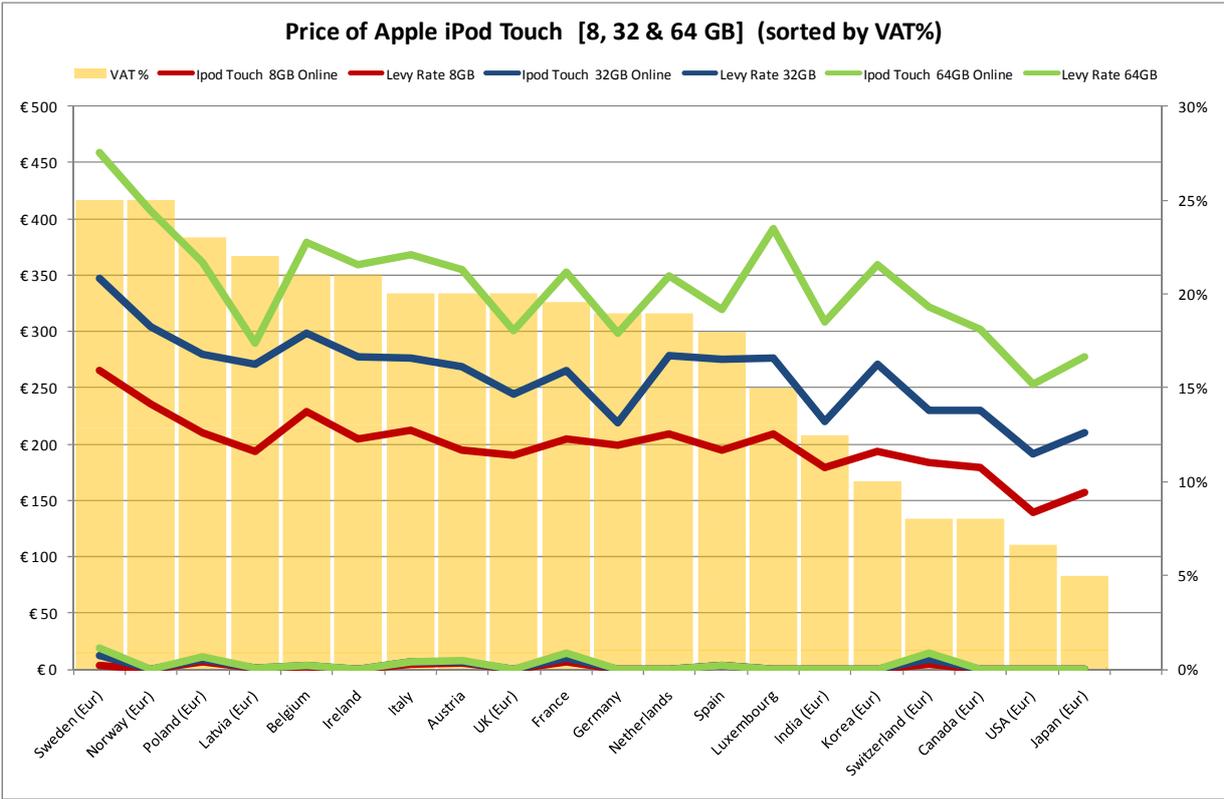
Graphic 4



**Table 5 Price of Apple iPod Touch [8, 32 & 64 GB] (sorted by VAT%)**

	VAT %	iPod Touch 8GB Online	Levy 8GB	iPod Touch 32GB Online	Levy 32GB	iPod Touch 64GB Online	Levy 64GB
<b>Sweden</b>	25%	€ 266	€ 3.12	€ 347	€ 12.48	€ 459	€ 19.40
<b>Norway</b>	25%	€ 236	€ 0	€ 304	€ 0	€ 406	€ 0
<b>Poland</b>	23%	€ 210	€6.29	€ 280	€ 8.41	€ 362	€ 10.85
<b>Latvia</b>	22%	€ 193	€ 1.42	€ 270	€ 1.42	€ 290	€ 1.42
<b>Belgium</b>	21%	€ 229	€ 2.50	€ 299	€ 3.00	€ 379	€ 3.00
<b>Ireland</b>	21%	€ 205	€ 0	€ 278	€ 0	€ 359	€ 0
<b>Italy</b>	20%	€ 212	€ 4.51	€ 276	€ 6.44	€ 368	€ 6.44
<b>Austria</b>	20%	€ 195	€ 6.00	€ 269	€ 7.00	€ 355	€ 8.00
<b>UK</b>	20%	€ 190	€ 0	€ 244	€ 0	€ 301	€ 0
<b>France</b>	19.6%	€ 205	€ 7.00	€ 265	€ 10.00	€ 353	€ 15.00
<b>Germany</b>	19%	€ 199	€ 0	€ 219	€ 0	€ 299	€ 0
<b>Netherlands</b>	19%	€ 209	€ 0	€ 279	€ 0	€ 349	€ 0
<b>Spain</b>	18%	€ 195	€ 3.15	€ 275	€ 3.15	€ 319	€ 3.15
<b>Luxembourg</b>	15%	€ 209	€ 0	€ 276	€ 0	€ 391	€ 0
<b>India</b>	12.5%	€ 179	€ 0	€ 220	€ 0	€ 309	€ 0
<b>Korea</b>	10%	€ 193	€ 0	€ 271	€ 0	€ 359	€ 0
<b>Switzerland</b>	8%	€ 184	€ 4.24	€ 229	€ 9.28	€ 322	€ 14.72
<b>Canada</b>	8%	€ 179	€ 0	€ 229	€ 0	€ 301	€ 0
<b>USA</b>	6.61%	€ 139	€ 0	€ 191	€ 0	€ 253	€ 0
<b>Japan</b>	5%	€ 158	€ 0	€ 210	€ 0	€ 278	€ 0

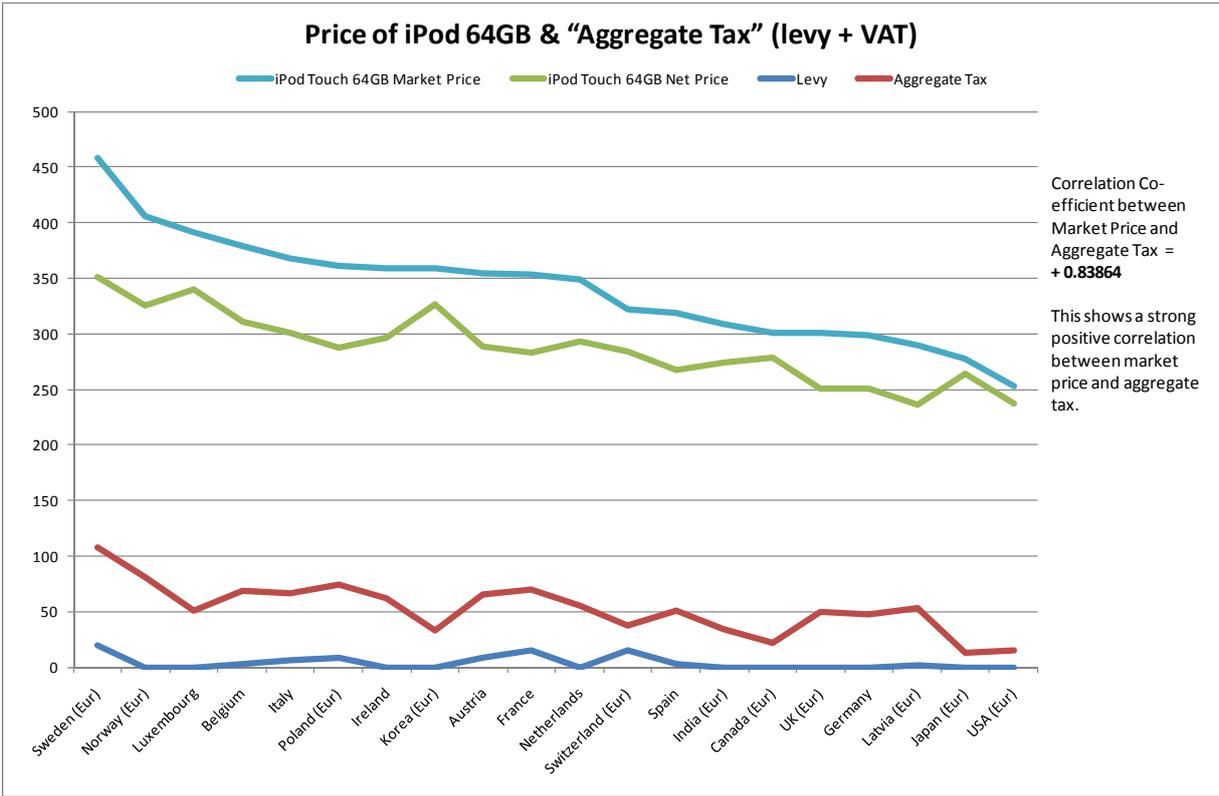
Graphic 5



**Table 6 Price of iPod 64GB & “Aggregate Charges” (levy + VAT)**

	VAT %	iPod 64GB Market Price	iPod 64GB Net Price	VAT	Levy	Aggregate Charges
<b>Sweden</b>	25.0%	€ 458.87	€ 351.58	€ 87.89	€ 19.40	€ 107.29
<b>Norway</b>	25.0%	€ 406.37	€ 325.10	€ 81.89	€ 0.00	€ 81.27
<b>Luxembourg</b>	15.0%	€ 391.00	€ 340.00	€ 51.00	€ 0.00	€ 51.00
<b>Belgium</b>	21.0%	€ 379.00	€ 310.74	€ 65.26	€ 3.00	€ 68.26
<b>Italy</b>	20.0%	€ 368.00	€ 301.30	€ 60.26	€ 6.44	€ 66.70
<b>Poland</b>	23.0%	€ 361.77	€ 287.12	€ 66.04	€ 8.61	€ 74.65
<b>Ireland</b>	21.0%	€ 359.00	€ 296.69	€ 62.31	€ 0.00	€ 62.31
<b>Korea</b>	10.0%	€ 358.80	€ 326.18	€ 32.62	€ 0.00	€ 32.62
<b>Austria</b>	20.0%	€ 355.00	€ 289.17	€ 57.83	€ 8.00	€ 65.83
<b>France</b>	19.6%	€ 353.00	€ 282.61	€ 55.39	€ 15.00	€ 70.39
<b>Netherlands</b>	19.0%	€ 349.00	€ 293.28	€ 55.72	€ 0.00	€ 55.72
<b>Switzerland</b>	8.0%	€ 321.71	€ 284.25	€ 22.74	€ 14.72	€ 37.46
<b>Spain</b>	18.0%	€ 319.00	€ 267.67	€ 48.18	€ 3.15	€ 51.33
<b>India</b>	12.5%	€ 308.59	€ 274.31	€ 34.29	€ 0.00	€ 34.29
<b>Canada</b>	8.0%	€ 301.44	€ 279.11	€ 22.33	€ 0.00	€ 22.33
<b>UK</b>	20.0%	€ 301.14	€ 250.95	€ 50.19	€ 0.00	€ 50.19
<b>Germany</b>	19.0%	€ 299.00	€ 251.26	€ 47.74	€ 0.00	€ 47.74
<b>Latvia</b>	22.0%	€ 290.14	€ 236.66	€ 52.06	€ 1.42	€ 53.48
<b>Japan</b>	5.0%	€ 277.61	€ 264.39	€ 13.22	€ 0.00	€ 13.22
<b>USA</b>	6.6%	€ 253.47	€ 237.76	€ 15.72	€ 0.00	€ 15.72

Graphic 6



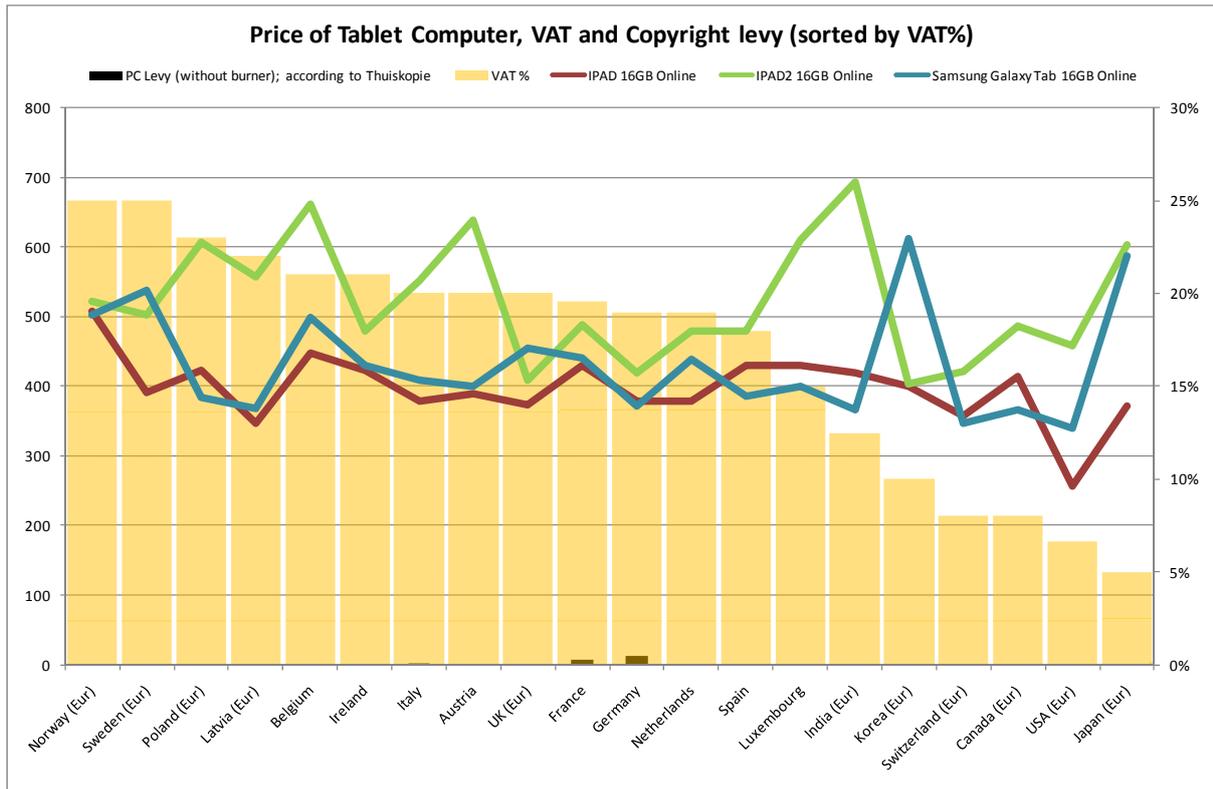
## Product Study 3: Tablet Computers

**Table 7 Price of Tablet Computer, VAT & Copyright levy (sorted by VAT%)**

	VAT %	iPad 16GB Online	iPad2 16GB Online	Samsung Galaxy Tab 16GB Online	PC Levy (no burner*)
Norway	25%	€ 508	€ 521	€ 503	€ 0
Sweden	25%	€ 390	€ 502	€ 538	€ 0
Poland	23%	€ 423	€ 607	€ 384	€ 0
Latvia	22%	€ 346	€ 556	€ 368	€ 0
Belgium	21%	€ 448	€ 662	€ 499	€ 0
Ireland	21%	€ 423	€ 479	€ 430	€ 0
Italy	20%	€ 379	€ 551	€ 408	€ 1.90
Austria	20%	€ 389	€ 639	€ 399	€ 0
UK	20%	€ 374	€ 409	€ 455	€ 0
France	19.6%	€ 429	€ 489	€ 441	€ 8.00
Germany	19%	€ 379	€ 419	€ 371	€ 12.15
Netherlands	19%	€ 379	€ 479	€ 439	€ 0
Spain	18%	€ 429	€ 479	€ 385	€ 0
Luxembourg	15%	€ 429	€ 610	€ 399	€ 0
India	12.5%	€ 420	€ 694	€ 366	€ 0
Korea	10%	€ 400	€ 404	€ 612	€ 0
Switzerland	8%	€ 357	€ 422	€ 347	€ 0
Canada	8%	€ 414	€ 486	€ 367	€ 0
USA	6.61%	€ 256	€ 458	€ 339	€ 0
Japan	5%	€ 371	€ 603	€ 587	€ 0

\* Tariff for PCs without burners; possible Tablet levies are under review.

Graphic 7



**Table 8 Tablet Computer Launch dates**

Country	iPad	iPad2	Samsung Galaxy
	launch date	launch date	launch date
<b>USA</b>	03 - Apr - 10	11 - Mar - 11	14 - Nov -10
<b>Italy</b>	28 - May - 10	25 - Mar - 11	15 - Oct - 10
<b>UK</b>	28 - May - 10	25 - Mar - 11	01 - Nov - 10
<b>France</b>	28 - May - 10	25 - Mar - 11	01 - Nov - 10
<b>Germany</b>	28 - May - 10	25 - Mar - 11	11 - Oct - 10
<b>Spain</b>	28 - May - 10	25 - Mar - 11	15 - Oct - 10
<b>Switzerland</b>	28 - May - 10	25 - Mar - 11	01 - Nov - 10
<b>Canada</b>	28 - May - 10	25 - Mar - 11	16 - Nov - 10
<b>Japan</b>	28 - May - 10	28 - Apr - 11	26 - Nov - 10
<b>Belgium</b>	23 - Jul - 10	25 - Mar - 11	01 - Nov - 10
<b>Ireland</b>	23 - Jul - 10	25 - Mar - 11	25 - Oct - 10
<b>Austria</b>	23 - Jul - 10	25 - Mar - 11	01 - Nov - 10
<b>Netherlands</b>	23 - Jul - 10	25 - Mar - 11	01 - Nov - 10
<b>Luxembourg</b>	23 - Jul - 10	25 - Mar - 11	01 - Nov - 10
<b>Norway</b>	30 - Nov -10	25 - Mar - 11	01 - Nov - 10
<b>Sweden</b>	30 - Nov -10	25 - Mar - 11	01 - Nov - 10
<b>Poland</b>	30 - Nov -10	25 - Mar - 11	11 - Oct - 10
<b>Korea</b>	30 - Nov -10	29 - Apr - 11	14 - Nov - 10
<b>Latvia</b>	28 - Jan - 11	NA	NA
<b>India</b>	28 - Jan - 11	28 - Apr - 11	10 - Nov - 10

## Findings

1. The costs of indirect charges (including VAT and levy) may be passed on to consumers, or absorbed by manufacturers or distribution channels/retailers.
2. If products are sold via a distribution channel, the retailer is ultimately responsible for pricing.
3. Manufacturers of some premium products (Apple iPod Touch) with selective distribution channels appear to be able to pass on the full indirect tax burden to consumers.
4. Some manufacturers may absorb the levy for some products (where there is concentrated purchasing power of retailers). The costs will be carried as reduced profit by their shareholders. This appears to be the case for printers/scanners.
5. Where consumer markets are very competitive, and there are dispersed distribution channels lacking purchasing power, the cost of levies may be absorbed by the retailer.
6. There appears to be a pan-European retail price point for many consumer devices regardless of levy schemes (with the exception of Scandinavia where consumers are willing to pay a premium).
7. For the launch strategy of high value innovative products (tablet computers), manufacturers seem to ignore the levy. In a second phase, they may either decide to pass on, or absorb.<sup>2</sup>

The extent to which it is profit maximising to pass on the levy depends on a number of factors.<sup>3</sup> These may vary across different markets. Economists may consider the degree of competition, elasticity of demand, and if levies are applied uniformly to all manufacturers (firm-specific or industry-wide costs). It also matters that levies, as indirect charges, are not fixed costs but depend on sales. Unless added explicitly on the retail price (as prescribed only in Belgium), the extent of pass-on is difficult to establish given these factors. Making the levy explicit on consumer retail advertising and receipts may be explored as a policy solution, together with explicit consumer permissions “bought” with the levy.

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2 This interpretation was supported during an e-mail exchange with a tablet manufacturer.

3 The author has benefited from analytical tools for assessing “pass-on” summarised in a report for the European Commission: A. Komninos et al. (2009), “Quantifying Antitrust Damages: Towards non-binding guidance for courts”, available at: <http://www.oxera.com/cmsDocuments/Quantifying%20antitrust%20damages.pdf>.

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# Study III: Economic Rationales<sup>1</sup>

Study I reviewed the legal context and current implementation of existing copyright levy systems in Europe. Study II presented new empirical data on the price effects of levy schemes. Study III addresses the unresolved question what copyright levies are for, by reviewing possible rationales. The argument here should distinguish the case for an exception for private copying and the case for compensation. If a decision to compensate is made, additional economic questions arise: What is the appropriate amount of compensation? How can it be delivered efficiently?

International copyright law affords a special status to private copying.<sup>2</sup> But why? There could be doctrinal reasons, internal to copyright law, such that copyright law only protects authors against acts of unauthorised communication, not consumptive use.<sup>3</sup> Yet this begs the question why copyright law should not extend to consumptive use. Why should there not be, in Jessica Litman's provocative phrase, an "exclusive right to read"?<sup>4</sup> And why should the legislator intervene, by regulating indirect payments for acts undertaken in the private sphere?

In the policy debate four main rationales have been advanced for linking a form of remuneration to a statutory exception for "private copying", and typically, the arguments conflate points from legal doctrine, economics and arguments of a moral nature. The following analysis attempts to extract the key economic points.

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- 1 The author would like to thank the participants of a seminar on "the economics of copyright levies" convened on 14 October 2010 at the offices of the Intellectual Property Office in London: Tony Clayton (chief economist, IPO); Dr Christian Handke (Erasmus University); David Humphries (senior policy advisor, IPO); Dr Ben Mitra-Kahn (economic advisor, IPO); Prof. John Kay (economist, FT columnist); Nick Munn (deputy director copyright, IPO); Ed Quilty (director of copyright, IPO); Joost Poort (SEO economic research, Amsterdam); Dr Fabrice Rochelandet (Université Paris XI Sud); Dr Nicola Searle (Abertay University, AHRC/ESRC Fellow at IPO) and Prof. Ruth Towse (Erasmus and Bournemouth University). The published notes from the meeting (<http://www.cippm.org.uk/symposia/symposium-2010.html>) are cited throughout this study, and form an invaluable signpost in an often tortuous debate.
  - 2 When the so-called "three step test" was introduced as Art. 9(2) into the Berne Convention (at the Stockholm Conference 1967), it was assumed that copyright exceptions that existed at the time were "grandfathered" into the Convention, i.e. they are deemed not to conflict with the new "three step test", confining exceptions to (1) "certain special cases" that neither (2) "conflict with a normal exploitation" of the work nor (3) "unreasonably prejudice the legitimate interests". Cf. S. Ricketson (1987), *The Berne Convention for the Protection of Literary and Artistic Works: 1886-1986*, section 9.11. Broadly worded private copying exceptions existed prior to Stockholm 1967, and thus may comply (however, see discussion of the French case Mulholland Drive in Study I, footnote 28).
  - 3 N. Helberger and P.B. Hugenholtz ("No Place Like Home for Making a Copy: Private copying in European copyright law and consumer law [*Berkeley Technology Law Journal* (BTLJ) 2007]) cite Joseph Kohler's view (*Das Autorrecht*, 1880, p. 230) that the exclusive right of reproduction is implicated only when a copy of a work "is intended to serve as a means of communicating to others".
  - 4 J. Litman, "The Exclusive Right to Read" (1994), 13 *Cardozo Arts & Ent. L.J.* 29.
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## Framework for analysis

### Rationale 1: Transaction costs

There is an established literature that explains the emergence of non-market structures in the exploitation of intellectual property rights (such as copyright collecting societies, and copyright levies) as a response to the transaction costs of individual licensing, such as information costs, contract costs and governance costs. In the case of copyright, transaction costs may include (a) identifying and locating the owner, (b) negotiating a price (this includes information and time costs), (c) monitoring and enforcement costs.<sup>5</sup>

The Gowers Review of Intellectual Property argued that “one of the purposes of exceptions to copyright is to reduce burdensome transaction costs associated with having to negotiate licences.”<sup>6</sup> It might follow from such a position that copyright exceptions, as well as collective structures of management, should disappear where transaction costs between owners and users become low enough for negotiations to occur. If individual licensing were possible, there would be no need for a private copying exception, nor for levies.<sup>7</sup>

The European Commission has read such a transaction cost rationale into the language of the 2001 Information Society Directive which indeed requires that fair compensation for private copying “takes account of the application or non-application of technological measures”.<sup>8</sup> In subsequent communications, the Commission explained: “Where a rightholder has authorised an activity in exercising his exclusive rights, no claim for compensation should arise as the person performing the activity, i.e. the consumer, is a licensee here and not a beneficiary of the exception.”<sup>9</sup>

This line of argument also pervades submissions by firms in the ICT (Information, Communications, Technology) sector and by major right holders who believe that they are in a position to license all private user activities on a contractual basis (so called “licensing through”).<sup>10</sup> Since private copying can be permitted under contract, there is no need for an exception. The appropriate compensation is a licence fee which should be left to the market.<sup>11</sup>

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5 For an excellent survey of this field, see C. Handke and R. Towse (2007), ‘Economics of Copyright Collectives’, *International Review of Intellectual Property and Competition Law* 8(38), 937-57.

6 *Gowers Review of Intellectual Property* (2006), London, HM Treasury, p. 47.

7 Cf. N. Helberger and P. B. Hugenholtz (2007), ‘No Place Like Home For Making A Copy: Private Copying In European Copyright Law and Consumer Law’, *Berkeley Technology Law Journal* 22, 1061, n. 56: “The ‘market failure’ inherent in the absence of practicable licensing and enforcement mechanisms vis-à-vis consumers of copyright works has been a powerful argument in favor of statutory licenses permitting private copying. Concomitantly, the recent emergence of DRM systems that do allow copyright holders to engage in individual end-user licensing has cast into doubt the survival of private copying exemptions.”

8 Directive 2001/29/EC of the European Parliament and of the Council of 22 May 2001 on the harmonisation of certain aspects of copyright and related rights in the information society, Art. 5(2)(b).

9 Impact Evaluation for Proposed Recommendation, Fair Compensation for Private Copying in a Converging Environment (2006), p. 58.

10 The Digital Copyright Eco-System: A holistic approach to change, Nokia White Paper, September 2009.

11 Examples of licensed “all-you-can-eat” services include digital music services (such as Spotify), academic journal databases, and perhaps soon cloud computing services (such as Apple’s iCloud).

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Unfortunately, this analysis of copyright exceptions is reductionist, in that it assumes that the term and scope of current rights are economically efficient, and that there are no other reasons for limiting the reach of exclusive rights. Explaining copyright exceptions as market failure is problematic.<sup>12</sup> Economic analysis of copyright law has to start with the bigger picture of incentives to the supply of cultural goods and create new content: Is there an optimal amount of production?<sup>13</sup> If the current parameters of copyright law ignore “economic efficiency” (i.e. if copyright law under-protects or over-protects), the transaction cost approach does not fly, as we are minimising transaction costs towards a sub-optimal outcome.

## Rationale 2: Statutory licence

As mentioned in Study I, the intellectual roots of the European levy system lie in a decision of the German federal court (*Bundesgerichtshof*) in 1964.<sup>14</sup> GEMA, the collecting society acting for music composers and publishers, had tried to obtain an order against a manufacturer of tape recorders, recording and disclosing the identity cards of buyers (*Personalausweise beim Tonbandgeräteverkauf*), presumably in order to pursue an action of direct infringement. The court held that a prohibition against private copying was not enforceable against a higher constitutional norm protecting the private sphere, and suggested the payment of a fee by the manufacturer. The decision led to the introduction of the German levy system with the copyright law of 1965 (UrhG, § 53) which is generally understood to be “a system of statutory licensing and equitable remuneration”<sup>15</sup> – although, paradoxically, there appears to be no permission associated with the licence.

Brigitte Zypries, then Minister of Justice, discussed this in an interview about the implementation of the 2001 Information Society Directive:

No, German copyright law (*Urheberrecht*) does not recognise a right to private copying. There are only limits (*Schranken*) to copyright law, i.e. the right owner must tolerate copying for private use and, in return, participates in a collective remuneration scheme. Private copying is lawful under the rule: ‘Protection, where you can protect. Remuneration, where you can’t protect.’<sup>16</sup>

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- 12 W.J. Gordon (1982), “Fair Use as Market Failure: A Structural and Economic Analysis of the Betamax Case and its Predecessors”, 82 *Columbia Law Review* 1600. Gordon later clarified her position in “Market Failure and Intellectual Property: A Response to Professor Lunney”, 82 *Boston University Law Review* 1031 (2002), drawing attention to the “danger of propertarian models” that “will cause us to lose the promise that could otherwise inhere in inexhaustibility” (p. 1031). “To enquire into ‘market failure’ is simply to ask, when can we as a society not safely rely on the bargain between owner and user to achieve social goals?” (p. 1037).
- 13 C. Handke (2010), *The Economics of Copyright and Digitisation, A Review* commissioned by the UK Strategic Advisory Board for Intellectual Property Policy, London: SABIP.
- 14 BGH, NJW 1964, 2157; GRUR 1965, 104 – *Personalausweise*.
- 15 European Commission (1995), *Green Paper - Copyright and Related Rights in the Information Society*, COM/95/0382, p. 50. See also Aml. Begründung zum UrhG 1965, BT-Drucks. IV/270 S. 71.
- 16 R. Sietmann, C’t-Interview 16/2004, p. 158. “Nein, das Urheberrecht kennt kein Recht auf Privatkopie. Es gibt nur Schranken des Urheberrechts, das heißt, der Rechteinhaber muss Vervielfältigungen zum privaten Gebrauch dulden und bekommt im Gegenzug seinen Anteil an der Pauschalvergütung. Die Zulässigkeit der Privatkopie beruht auf einer staatlichen Lizenz nach dem Motto: Schützen, was man schützen kann. Vergüten, was man nicht schützen kann.”
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In *Canadian Private Copying Collective v Canadian Storage Media Alliance*<sup>17</sup>, the Canadian Federal Court of Appeal considered whether the levy on blank audio recording media to collect remuneration for private copying (ss. 79-88, Copyright Act, R.S.C., 1985) was a “regulatory charge” (which would fall under federal jurisdiction) or a “tax” (outside federal competence). Justice Noël held the former, and construed the law of private copying thus (at 3):

[T]he Act legalizes copying recorded music for private use and thus provides a statutory exception to the exclusive reproduction rights of eligible authors, performers and makers of recorded music (rightsholders). At the same time, it entitles rightsholders to compensation for their loss of exclusivity by imposing a levy on media used to record music.

In both the German and Canadian conception, levy compensation may be seen as constituting a contract term under which copyright material is made available to all takers for private use, in effect turning an exclusive right into a statutory licence. If the rationale for copyright levies is a policy decision to write a mandatory contract term into licences (which can no longer be refused), the policy goal has to be justified, and the scope of the statutory licence has to be communicated to the user as a permission.<sup>18</sup>

### Rationale 3: Consumer value

A third argument for a levy system of payments has been floated as a “value recognition right”.<sup>19</sup> It assumes that consumers’ freedom to copy increases the value of devices or services (such as MP3 players, or even broadband Internet access). The argument then claims that since right owners do not profit from this higher value, they do not receive the right economic signals to produce more copyright content. Sharing this higher value through a system of compensation to right owners would increase economic efficiency. The study by consultants EconLaw<sup>20</sup> (commissioned by GESAC) calls this a “sound economic justification”:

The private copying exception is a legal instrument that generates increased consumer value. This limit on the exclusivity of IPR increases consumers’ freedom of use of the intellectual works. From an economic perspective, this increased freedom automatically translates into a higher valuation of the IPR-protected goods –which gets expanded whenever technological or other developments allow new potential uses of the IPR-protected goods. The appearance of digital CE [consumer electronics] devices on which IPR-protected content already in the possession of consumers can be uploaded, stored

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17 2004 FCA 424 (CanLII).

18 Volker Grassmuck provides a useful collection of material supporting the proposal to extend the concept of a statutory licence to file sharing: “Sharing licence library”, <http://www.vgrass.de/?p=1048>.

19 The term “value recognition right” was coined in 2006 by a UK music industry grouping, including Aim, MCPS-PRS, British Music Rights, MMF, MPA, British Academy Of Composers And Songwriters and Musicians Union. Similar arguments are used by newspaper publishers in lobbying for a neighbouring right in news (*Presseleistungsschutzrecht*).

20 Economic Analysis of Private Copy Remuneration, Report prepared by EconLaw Strategic Consulting for Groupement Européen des Sociétés d’Auteurs et Compositeurs (GESAC) (September 2007), section 1.3, p. 7.

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and played has increased consumers' valuation of those IPR-protected goods. Were it not for PCR [private copying remuneration] charges, the additional social value created by the new use of IPR-protected works would be appropriated exclusively by consumers and the CE industry, while creators would remain uncompensated. Such regulatory insufficiency can, however, be easily corrected by extending PCR charges to digital CE devices.

In their analysis of consumer value and economic damage from consumer copyright exceptions, Rogers, Tomalin and Corrigan<sup>21</sup> argue, *au contraire*, that agents and creators automatically extract value from copyright exceptions: "the value of private copying is embedded in the demand for copyrighted work so a levy on consumer electronics is not necessary to equate price with demand". Ferreira<sup>22</sup> (in a study commissioned by HP) makes the same point with four telling examples:

Example 1: Consider a standard competitive market for screw-drivers and other tools, and that consumers find more uses for these goods as do-it-yourself books become more widely available. No one thinks that this new value for screw-drivers should imply some compensation from the editors of these books to screw-drivers manufacturers because they are selling more books as a result of the existence of screw-drivers. The reason is that the better value of the screw driver is reflected in a shift of the demand for this tool. Consumers demand more tools, and their prices would go up (in the short run), with higher profits to screw drivers manufacturers. This provides incentives for more manufacturers to enter the market until a new equilibrium is reached in the long run. In the new long run equilibrium the quantity will be higher, but the price can be lower or higher depending of the cost structure of the industry for screw-drivers. Typically a higher market allows for investments in better technology or for uses of economies of scale, and the price will be lower. If the economies of scale have been exhausted and no better technology is available, the price may go up. The bottom line is that the new situation would be efficient. The increase in the demand provided the (sufficient) incentive to serve the market. No extra compensation is needed to incentivise production of more screw-drivers.

Example 2: Consider the market for fiction books or music CDs [...]. Suppose now that books and CDs have more value to consumers because of increased rates of literacy or because new technologies allow for more leisure time. Or maybe consumers find new uses for recipe-books because it is now easier to find more ingredients in the local market due to an improvement in the transport technology. Again there is no reason for the book or the music CD industry to demand compensation for the increased value of their products. As before, the higher value of the goods is translated in a higher demand for them and that is enough to settle in a new equilibrium that is equally satisfactory to the old one from the economic perspective.

Example 3: Consider again the market for copies of intellectual works. Suppose now that the higher value of these copies comes from a new technology that allows them to be enjoyed in more circumstances. For instance, the invention of the electric bulb allows

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21 M. Rogers, J. Tomalin and R. Corrigan (2009), "The Economic Impact of Consumer Copyright Exceptions: A literature review", Oxford: Harris Manchester Colleg, p. 20.

22 J.L. Ferreira (2010), "Compensation for Private Copying: An Economic Analysis of Alternative Models", ENTER-IE Business School, pp. 19-20.

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the consumer to read at night, in her bed, and not only during the afternoon in the porch. Or a new portable device (e.g. a portable CD disc-man) is invented that allows for a music CD to be played anywhere in the house. The same argument as before applies. No compensation is necessary beyond what the market already does.

Example 4: Consider now that the new technology that allows for a time-shifting or a format-shifting requires making a copy of the legally-bought copy. For instance, a consumer can scan a book to save weight and read it as she travels, or a paid-for TV program can be recorded to watch it later, or a music CD can be converted into the MP3 format to be listened while exercising. From the economic point of view, this is the same case as the previous examples: an increase in value of the good that produces a shift in the demand that produces a new equilibrium as efficient as the old one. As in the previous examples, no extra compensation is needed to produce more books or music CDs.<sup>23</sup>

While “value recognition” remains an unorthodox economic concept, Dutch economist Joost Poort<sup>24</sup> has offered two different lines of reasoning focussing on externalities:

If the starting point is full enforceability of copyright law as a property right, file sharing and private copying may have negative externalities on copyright holders. This can be addressed with a Pigovian tax on the act of copying (which a levy tries to do, even though imperfectly) and a subsidy/compensation to the party that is harmed. The latter may not only be a matter of equity but also a matter of dynamic efficiency, giving the proper investment incentives in the light of externalities.

If the starting point is the absence of copyright protection, file sharing and private copying are probably positive externalities of creative production (or at least rents that are not appropriable). From this perspective, there is no case for a tax (why tax positive externalities?) but there is a case for subsidising the industry that creates these spillovers.

As in the discussion of Rationale 1 (reduction in transaction costs), it is difficult to assess these arguments without addressing the bigger picture of the justification for copyright protection in the first place. It has been argued that copyright, operating as a temporary exclusive right, already constitutes a trade-off between underproduction and underutilisation. The exclusion is also designed to maximise spillovers (beyond the benefits of direct use) serving a greater social goal (e.g. promoting innovation and learning through new digital services).<sup>25</sup> If these spillovers do not happen, the policy may be flawed. On this reading, levies do not operate within the

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23 It is an empirical question whether or not there is a price premium on goods which can be freely copied.

24 The economics of copyright levies, IPO / ESRC Seminar, 14 October 2010 (protocol available at <http://www.cippm.org.uk/symposia/symposium-2010.html>). A Pigovian tax attempts to correct the market outcome of a negative externality, for example by taxing polluters.

25 Economists use the term “spillover” (or “positive externality”) to capture the idea of economic benefits accruing to economic agents not involved in the action causing benefits. For R&D investment, Adam Jaffe identifies three kinds of spillovers: “First, spillovers occur because the workings of the market or markets for an innovative product or process create benefits for consumers and non-innovating firms (“market spillovers”). Second, spillovers occur because knowledge created by one firm is typically not contained within that firm, and thereby creates value for other firms and other firms’ customers (“knowledge spillovers”). Finally, because the profitability of a set of interrelated and interdependent technologies may depend on achieving a critical mass of success, each firm pursuing one or more of these related technologies creates economic benefits for other firms and their customers (“network spillovers”). Adam J. Jaffe (2008), “The importance of ‘spillovers’ in the policy mission of the advanced technology program”, *The Journal of Technology Transfer* 23(2), pp. 11-19.

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copyright system but offer an alternative way of financing desirable cultural production (directly, rather than via incentives), without restricting spillovers through exclusive rights. This rationale is discussed in the following section.

## Rationale 4: Taxation

A system of levies on copying media or services can be understood as the partial replacement of market forces because it is felt that the market would under-supply content if left alone. This is assumed because much copyright content exhibits the characteristics that they are non-rival – where one person reading a book does not prevent someone else from reading it later, or non-excludable – where one person can listen to a song without excluding someone else from listening in. The options available to policy makers for addressing the supply of so-called “public goods” or goods with similar characteristics are quite well understood:<sup>26</sup>

1. *The provision of the goods is left to the market.* In these circumstances free riding is assumed to create under-supply. However as Posner points out, absence of copyright, or of Moral Right, whilst perhaps leading to under-supply of original works, would also increase the supply of derivative works. In addition, works which were in fact protected by their uniqueness (great paintings) would still be supplied. Similar arguments might be applied to patents. Overall the net losses due to an absence of rights might not be as large as theory first suggests.
2. *The products could be funded by society or by a group out of a levy or taxation and then distributed without direct charge.* In these circumstances, although the products would not be under-supplied, the product mix is not necessarily the one desired by consumers. There would be a loss of allocative efficiency and in extreme cases a loss of freedom of thought where all intellect was centrally controlled.
3. *A device for exclusion could be created, and users would then pay for the product.* This is the intellectual property right option whereby a legal barrier is erected and potential users of the product must either buy the product outright under a property rule or pay for its use under a liability rule. The option looks attractive in that it prevents under-supply and links product to consumer, but it creates economic inefficiency in that additional consumers who could be added at almost zero cost and greater than zero benefit are excluded. Thus, there is an overall welfare loss to the community which is made worse if the barriers for exclusion are too high (thereby creating monopoly rents) and if administration and monitoring costs are too high. Administration and monitoring costs are particularly high where the costs of copying are low (as they are today) and the costs of detecting and preventing copying are high.

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26 C.W. Maughan (2004), “Property and Intellectual Property: Foundations in Law and Economics”, Prometheus 22(4), pp. 379-391, p. 386. Maughan also summarises the characteristics of products of the intellect as public goods. “They are not depletable: the amount available is the same for all consumers: exclusion of consumers is potentially difficult or costly: the marginal cost of producing the work is positive, but once produced the marginal cost of adding an extra ‘consumer’ is close to zero, whilst the marginal benefits are greater than zero.”

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4. *Various methods of financing the product without reference to the consumers can be used, e.g. patronage, sponsorship, advertising.* This method ensures the creation of the products, but produces a product mix determined by the sponsor not the consumer. Again allocative efficiency is impaired.

Stan Liebowitz's characterisation of levies as a form of taxation falls under option 2: "the basic idea is that a pool of money would be generated in a secondary market (presumably related to MP3s) and transferred to copyright owners. We are talking here about taxes on ancillary products, such as blank CDs, CD writers, ISPs, stereo equipment, and so forth. Although some commentators see a compulsory license as a supplement to the current copyright system, it is also viewed, particularly by its more passionate advocates, as a complete replacement of traditional copyright, at least for recorded music."<sup>27</sup>

Most economists think that taxation should only be considered if market mechanisms fail to produce socially desirable outcomes. It is also often assumed in the theory of public finance that systems of indirect taxation (such as taxes on the sale of goods or services), are less than optimal: the collected tax tends to be smaller than the reduction of the consumer's and producer's surplus.

Conceiving levies as taxes poses all the standard questions of taxation: Who should be charged? How much? Who should be the beneficiaries? Ruth Towse sums up these concerns:<sup>28</sup>

From an economic point of view, [the levy] is an even blunter instrument than the blanket licence or equitable remuneration schemes, because all who buy the equipment have to pay the levy whether or not they use it for copying purposes, and the revenues from the levy have to be distributed in a fairly arbitrary way between the different groups of rights holders, whose work may or may not have been copied (visual artists, authors and publishers, composers, performers, record labels, and so on).

Oxera Consulting (in a study commissioned by Nokia) models the welfare effects of levies as a system of indirect taxation from the following assumptions:<sup>29</sup>

- Consumers are affected by copyright levies insofar as hardware vendors pass the levies on in the form of higher retail prices. This in turn reduces the sale of electronic devices, and hence the demand for music downloads and other forms of music files.

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27 S. Liebowitz (2004), "Alternative Copy Systems: The Problems with a Compulsory License", *IPCentral Review* 1(2), May 6, p. 3; Liebowitz, S. (2006), "MP3 and Copyright Collectives: A cure worse than the disease?", pp. 37-59 in L. Takeyama, W.J Gordon, R. Towse (eds.) *Developments in the Economics of Copyright*, Cheltenham: Edward Elgar. In the US context, Liebowitz mainly addresses the "alternative compensation" proposals by Natanel (2003) and Fisher (2004): N.W. Natanel (2003), "Impose a non-commercial use levy to allow free peer-to-peer file sharing", *Harvard Journal of Law & Technology* 17(1): 1-83; W.W. Fisher (2004), *Promises to Keep: Technology, Law and the Future of Entertainment*, Stanford University Press.

28 R. Towse (2010), *A Textbook of Cultural Economics*, Cambridge: CUP, pp. 366-7.

29 Is There a Case for Copyright Levies? An economic impact analysis (report prepared for Nokia), Oxera Consulting Ltd (April 2011), p. iii.

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- Device manufacturers are affected because they absorb the levies as extra costs, or pass them on to retail prices, and hence make fewer sales. Either way, this diminishes their incentives to invest in, and introduce, new device models, and to launch new music distribution platforms. This in turn affects consumers as well.
- Rights holders receive a direct financial benefit from copyright levies (to the extent that collecting societies do indeed distribute their revenues to principal rights holders—this varies by country and plays a role in the model, but is not the main focus of this report). However, the higher device prices resulting from the copyright levies may diminish sales of digital content, and therefore also the overall revenues of rights holders.

While some countries have a ritual objection to taxation, other countries have been quite clear that they see copyright levies “as an important source of finance for cultural and social activities (alleviating demands on the State budget).”<sup>30</sup> France, in particular, seems to rely on a fundamental non-economic justification for levies, linking deeply engrained norms of “Privacy”, and “Fairness towards authors”.<sup>31</sup> French economists, such as Fabrice Rochelandet, thus seem inclined towards a pragmatic approach, taking these political premises as given: “If one wants to raise a fund for remunerating authors, levies are at least a reasonable policy option. The economists’ contribution here may be to make such a system more efficient, and perhaps link it with innovation promoting consumer permissions.”<sup>32</sup>

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30 European Commission (2006), *Impact Evaluation for Proposed Recommendation, Fair Compensation for Private Copying in a Converging Environment*, p. 42. In France, 25% of levy revenues are used for cultural purposes, such as funding performances and festivals. Socio-cultural deductions are also high in Denmark (33% of collected revenues), Portugal (20%) and Spain (20%). See Study I. Since levy charges are collected through collecting agencies, they do not appear in national accounts, and function in effect as an off-balance sheet tax (similar to national lotteries).

31 On the lobby platform “la culture avec la copie privée”, copyright levies are characterised as “a pact between creators and the public” (<http://www.copieprivee.org/-Homepage-.html>).

32 The economics of copyright levies, IPO / ESRC Seminar, 14 October 2010 (protocol available at <http://www.cippm.org.uk/symposia/symposium-2010.html>). Liebowitz and Watt discuss a range of options for paying creators: S. Liebowitz and R. Watt (2006), “Remuneration for Creators of Music”, *Journal of Economic Surveys* 20(4), pp. 513-33. José Luis Ferreira finds that current European levy systems waste 51.2% of each Euro collected and do not offer any incentives to creators. Eight possible improvements are reviewed: Europe-wide harmonisation administered at national level, payment at retail level (rather than manufacturer), Europe-wide harmonisation at EU level, free choice of collecting society, levy on copyright works, indirect tax (à la VAT), national fund (à la Norway), and clause in labour contract: J.L. Ferreira (2010), “Compensation for Private Copying: An Economic Analysis of Alternative Models”, ENTER–IE Business School (study commissioned by HP).

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# Solutions

## The concept of harm

In the 2010 *Padawan* decision, the European Court of Justice held that the concept of “fair compensation” “must be regarded as an autonomous concept of European Union law to be interpreted uniformly throughout the European Union”.<sup>33</sup> With reference to Recitals 35 and 38 of the Information Society Directive, the Court found (at 42) that “fair compensation must necessarily be calculated on the basis of the criterion of the harm caused to authors of protected works by the introduction of the private copying exception”.

Harm in law is typically interpreted as a lost licensing opportunity, i.e. a fee that could have been charged.<sup>34</sup> However, there is a circularity here: if there is a copyright exception, there is no infringement, and no licence could have been issued. Thus by definition there is no harm in law from a permitted activity.<sup>35</sup>

In economics, harm is usually considered as a lost sale, i.e. if copying replaces a purchase that otherwise would have been made,<sup>36</sup> but also encompasses the broader economic impact on consumers and producers. Normally, lost sales are not something to be compensated. If a second stall sets up in a market, it’s called competition. However, if competition arises from a lack of enforceability of contracts or rights, the issue becomes more complicated. John Kay gives the example of a manufacturer of lawn mowers who may want compensation for the perceived harm from people lending mowers to neighbours (who therefore do not have to buy their own). Kay argues that legislators should be reluctant to get involved in the enforcement of private rights: “If right owners struggle to enforce contracts, this is not normally a point of public policy.”<sup>37</sup>

So while the concept of harm is given by European law, its underlying economic assumptions are contested. For each of the four rationales discussed above, harm takes on a different meaning. It remains unresolved if a levy should be analysed as a (regressive) tax, or if there can be (transaction cost) efficiencies or dynamic effects (increased access to copyright materials for follow-on innovation). In addition, a number of non-economic arguments are frequently made, focussing on privacy, the reward of creators, and cultural aims.

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33 *Padawan SL v Sociedad General de Autores y Editores de España (SGAE)*, Case C-467/08, 21 October 2010. The intellectual origins of the concept of “fair compensation” can be traced to a decision of the German federal court in 1964 (BGH, NJW 1964, 2157; GRUR 1965, 104 – Personalausweise), and the copyright law of 1965 (UrhG). See Study I.

34 For example, in the common law jurisprudence on damages, payments shall put the claimant in as good a position as if no wrong had occurred: *Robinson v Harman* (1848); *Livingstone v Rawyards Coal Co* (1880).

35 Consumer initiatives believe that the freedom to make private copies cannot be a matter of a licensing arrangements. Just as with “free speech” based copyright exceptions, such as those for “review and criticism” or “parody”, private copying should be non-compensated, and non-overridable by contract. [reference Consumer Focus submission]

36 For a nice discussion of the substitution rate as the amount of legal product which will not be purchased as a result of copying, see B. Mitra-Kahn (2011), “Copyright, evidence and lobbyconomics: the world after Hargreaves”, Annual Congress of the Society for Economic Research on Copyright, 7-8 July 2011 (Bilbao, Spain).

37 The economics of copyright levies, IPO / ESRC Seminar, 14 October 2010 (protocol available at <http://www.cippm.org.uk/symposia/symposium-2010.html>).

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Good public policy should incentivise right owners to make copyright materials available in a form that enables private copying, since there are obvious benefits to innovation and learning if users have as wide access as possible to cultural materials (as long as the incentives to produce in the first place are sufficient). Yet, the European Commission has read the fair compensation provisions of the Information Directive in the opposite way. Right owners who give permissions for private copying (for example by using permissive settings in their DRM systems, or permitting non-commercial use under a Creative Commons licence) lose their entitlement to fair compensation.<sup>38</sup> Thus European policy, perversely, appears to incentivise right holders to apply restrictive settings which are then breached by users, allowing the right owners to claim harm that should be compensated.

A solution to this contradictory policy could be (i) to avoid the entitlement to compensation from narrowly conceived private copying activities, such as format shifting (through a *de minimis* interpretation of harm), and (ii) to convert a range of other private, non-commercial activities which would encourage consumer led innovation, and services that facilitate such innovation, into state regulated licences (which can be understood as “fair compensation” for harm). These options are explained in the next two sections.

## Priced into purchase: the “de minimis” interpretation

Hal Varian considers the situation where a publisher or producer “can completely determine the terms and conditions under which the products it sells can be consumed”.<sup>39</sup> Developing Liebowitz’ concept of “indirect appropriability”<sup>40</sup> Varian then distinguishes the number of works produced and the number of works consumed. If sharing is permitted, or takes place, the producer is likely to sell fewer units of the work, but since the consumer derives greater value from each unit, the producer’s profit may even increase (if pricing is right). However, if the availability of free copies pushes the retail price to marginal cost, the original seller will find it hard to raise the price to a level where he can recover the cost of production. The basic idea remains the same: “if the willingness-to-pay for the right to copy exceeds the reduction in sales, the seller will increase profit by allowing that right.”<sup>41</sup> In other words, a certain amount of copying can already be priced into the retail sale of the first copy if the consumer understands these benefits. Rogers, Tomalin and Corrigan call this the “first sale” argument.<sup>42</sup>

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38 Impact Evaluation for Proposed Recommendation, Fair Compensation for Private Copying in a Converging Environment (2006), p.58. “Where a rightholder has authorised an activity in exercising his exclusive rights, no claim for compensation should arise as the person performing the activity, i.e. the consumer, is a licensee here and not a beneficiary of the exception.” The non-commercial licence of the Creative Commons family (version 3.0, 4.d.) tries to avoid this implication by reserving the right to collect royalties from collective licence schemes (<http://creativecommons.org/licenses/by-nc/3.0/legalcode>). The space which may be non-commercial but compensatable remains unclear. Cf. Reference of the German Federal Court (BGH) to the ECJ in the case of *Drucker und Plotter* (VG Wort and Others, C-457/11 to C-460/11).

39 H.A.Varian (2005), “Copying and Copyright”, *Journal of Economic Perspectives* 19(2): 121-138; p. 129.

40 S. Liebowitz (1985), “Copying and Indirect Appropriability: Photocopying of Journals”, *Journal of Political Economy* 93(5): 945-57.

41 Varian, *ibid.* p. 130.

42 M. Rogers, J. Tomalin and R. Corrigan (2009), “The Economic Impact of Consumer Copyright Exceptions: A literature review”, Oxford: Harris Manchester College, p. 15.

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Joost Poort comments: “That is an attractive argument as far as ‘passing copies to friends’ is concerned. This would narrow down the debate to online file sharing. Only when file sharing (or at least downloading) is legalized as an exception to copyright, will there be a rationale for a levy. As long as it is not allowed, there is no case for such a ‘privatized fine for unlawful behaviour’.”<sup>43</sup>

## “Fair compensation” as a regulated licence

It is tempting to conceive growing digital consumer markets that rely on unauthorised copying (devices and services) as a potential source of finance for copyright content, rather than an infringement. This may come about through individual licences (such as those negotiated by digital services Spotify or Apple’s iCloud), or by collective licences or licences as of right (backed by statute), turning an exclusive right in effect into a right to receive remuneration (such as those that permitted radio broadcasting from the 1920s onwards).<sup>44</sup>

The legal technique of “fair compensation” may play a part in a wider overhaul of the copyright system, facilitating the growth of new services by making licensing more permissive, and subject to regulatory oversight. Non-economic arguments favouring such intervention include balancing the bargaining position of creators versus producers, and preserving fundamental rights of privacy.<sup>45</sup>

The scope of permissions associated with such compensation could go beyond the specific meaning of Art. 5(2)(b) of the 2001 Information Society Directive (which relates only to the reproduction right, i.e. not: communication to the public, distribution to the public, public performance or adaptation). Of the seven consumer activities distinguished in Study I, all have a non-commercial, consumptive orientation. (i) and (ii) are expected by all legitimate buyers, not enforced by right owners, and therefore priced into the purchase. (iii) and (iv) only involve reproductions, and could be permitted and compensated under existing European legislation at national level, even from “obviously illegal sources” since there is a lack of enforceability both on technical (e.g. identifying IP addresses of downloaders) and legal grounds (e.g. applicable law, enforcement across jurisdictional borders). However, a more elegant solution could wrap up all non-commercial activities, including (vii), into a licensing scheme.

- (i) Making back-up copies / archiving / time shifting / format shifting
- (ii) Passing copies to family / friends
- (iii) Downloading for personal use
- (iv) Uploading to digital storage facilities

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43 The economics of copyright levies, IPO / ESRC Seminar, 14 October 2010 (protocol available at <http://www.cipm.org.uk/symposia/symposium-2010.html>).

44 The Performing Rights Society issued the first licence to the BBC in 1923: G. McFarlane (1980), Copyright: *The Development and Exercise of the Performing Right*, London: CityArts, p. 111.

45 M. Kretschmer, E. Derclaye, M. Favale, R. Watt (2010), *The Relationship between Copyright and Contract Law: A Review commissioned by the UK Strategic Advisory Board for Intellectual Property Policy*, London: SABIP (2010).

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- (v) File sharing in digital networks
- (vi) Online publication, performance and distribution within networks of friends
- (vii) User generated content / mixing / mash-up (private activities made public)

Statutory licences are compatible with the international copyright framework in limited circumstances. The Berne Conventions explicitly allows “conditions on the exclusive right” with respect to broadcasting (Art. 11bis(2)) and for cover versions, i.e. the re-recording of musical works (Art. 13(1)). Other limitations or exceptions have to pass the three-step-test of Article 9 (TRIPS Article 13; Info Soc Directive Art. 5(5)) which confines limitations or exceptions to certain special cases which do not conflict with a normal exploitation of the work and do not unreasonably prejudice the legitimate interest of the right holder. The three-step-test is regarded as being consistent with quite far-reaching compulsory collective licensing schemes, such as the one devised for cable retransmission by Directive 93/83/EEC.<sup>46</sup> Compulsory licences are also possible where competition law comes into play. However, competition law normally addresses consumer issues only from the perspective of a dominant position, the ability of a supplier to act unilaterally.

There are numerous implementation options for such a licensing scheme. A fund may be created that functions both as “fair compensation” for private copying within the meaning of the Information Society Directive, and as an incentive for right owners to sign up to more permissive licence conditions.<sup>47</sup> For both right holders and users, access to the licence and payment of compensation could be voluntary. For example, consumers who do not sign up may have to warrant that their IP address would not be used for activities (iii) to (vii); while right owners explicitly prohibiting private copying beyond (i) and (ii) would be left to enforce their rights (with compensation only available as damages through the court system).<sup>48</sup>

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46 C. Bernault and A. Lebois (2005), *Peer-to-peer File Sharing and Literary and Artistic Property: A Feasibility Study regarding a system of compensation for the exchange of works via the Internet*, Institute for Research on Private Law, University of Nantes: <http://alliance.bugweb.com/usr/Documents/RapportUniversiteNantes-juin2005.pdf>.

47 Norway has created a €4m/year fund from direct taxation in order to satisfy the EU requirement of “fair compensation” (see Study I). This option is now also considered by Finland: A. Wessberg (2011), “An alternative arrangement for the copyright levy”, Helsinki: Ministry of Education and Culture. In this context, it is worth noting that the copyright enforcement provisions of the UK Digital Economy Act 2010, if implemented, are likely to cost £7.6m in the first year, roughly split between right holders (75%) and ISPs (25%). Impact Assessment of draft SI “The online infringement of copyright (Initial Obligations) (Sharing of Costs) order 2011” IA No: DCMS032, 29 June 2011. ISPs may pay Ofcom as part of their current levy.

48 A useful opt-in, opt-out proposal has been developed by A. Peukert (2005) : “A Bipolar Copyright System for the Digital Network Environment”, *Hastings Communications and Entertainment Law Journal* 28(1). Key issues of public finance remain unresolved: Who pays? How much? Who gets the revenues?

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## Conclusion

While it is important to be clear sighted about the constraints imposed by national, European and international law, this should be where the analysis starts, not where it ends. What the law currently says is not necessarily what the law will be. Reviews of the intellectual property system in the digital environment will not be successful until copyright practice meets with a minimum of acceptance. Economically and socially, minimum acceptance entails that creators are willing to create; that publishers and producers are willing to invest; and that consumers remain willing to buy (and that assumes that they understand some form of legal exclusion as justified).

For the UK, a key question is if new exceptions, or changes to the scope of exceptions and limitations, can be introduced without triggering the European requirement of fair compensation, and therefore an assessment of harm.<sup>49</sup> A second question relates to the effects of European levy schemes on the Single Market, and how the UK might respond to any proposed regulation of the European copyright system.<sup>50</sup>

There appears to be no economic case for adding another layer of licensing on copyright transactions if limited to the narrow meaning of private copying covered by the “first sale” argument. Within the constraints of EU law, the UK’s economically efficient option appears to be the *de minimis* argument (= no harm): a certain amount of copying in already priced into the first retail purchase.

The discussion of a statutory licence, or a voluntary licence under state supervision, moves beyond allocative efficiency to consumer issues (including higher norms of privacy), and the reward of creators (equity in distribution). The arguments for a levy scheme of fair compensation here are distinct, but overlap in complex ways with the justification for copyright itself.

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49 *Digital Opportunity, A Review of IP and Growth* (Hargreaves Review), London: May 2011, section 5.25-5.42: Copyright exceptions: UK options.

50 Within the European Commission, the communications emanating from the Copyright Unit (located in Commissioner Michel Barnier’s Internal Market Directorate, announcing “comprehensive legal action” regarding private copying levies for 2012; see Study I) show tensions with the Digital Agenda led by Commission Vice-President Nellie Kroes (who characterised the European copyright regime as a “dysfunctional system based on a series of cultural Berlin walls”). Nellie Kroes, “A digital world of opportunities”, speech at the Forum d’Avignon - Les rencontres internationales de la culture, de l’économie et des medias (5 November 2010): “Today our fragmented copyright system is ill-adapted to the real essence of art, which has no frontiers. Instead, that system has ended up giving a more prominent role to intermediaries than to artists. It irritates the public who often cannot access what artists want to offer and leaves a vacuum which is served by illegal content, depriving the artists of their well deserved remuneration. And copyright enforcement is often entangled in sensitive questions about privacy, data protection or even net neutrality. It may suit some vested interests to avoid a debate, or to frame the debate on copyright in moralistic terms that merely demonise millions of citizens. But that is not a sustainable approach. We need this debate because we need action to promote a legal digital Single Market in Europe. My position is that we must look beyond national and corporatist self-interest to establish a new approach to copyright. We want “*une Europe des cultures*” and for this we need a debate at European level.

The Commission will soon make legislative proposals on orphan works and on the transparency and governance of the collective management societies. We will examine again the problem of divergent national private copy levies. We will also look into multi-territorial and pan-European licensing. And we will not stop exploring ideas for as long as the system is not working. Instead of a dysfunctional system based on a series of cultural Berlin walls, I want a return to sense. A system where there is scope to create new opportunities for artists and creators, and new business models that better fit the digital age. We want to help you seize the opportunities of this age.”

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