The benefits and costs of copyright
an economic perspective

Discussion Paper
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Postscript

After this paper was written, the Intellectual Property and Competition Review Committee issued an *Interim Report* on the effects on competition of Australia's intellectual property laws pursuant to a reference from the Minister for Industry, Science and Resources and the Attorney-General (for details see the committee's web site at <http://www.ipcr.gov.au/ipcr/index.htm>). The Interim Report makes limited proposals concerning some of the reform issues canvassed in this paper. The final report of the committee is due on 30 June 2000.

Centre for Copyright Studies Ltd

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Preface

In writing this paper, we are motivated by a concern that insufficient attention has been given to economic issues in evaluating the efficacy of copyright law. In the information age it is intellectual property that is often the basis of the modern commercial enterprise's success or failure. Similarly, our access to many products that we value — including books, magazines, games, art works, films, plays, music and computer software — depends on innovative activities of enterprises and the individuals they employ. The economic rationale for copyright law is to promote innovative activity and to ensure that those who value information products have reasonable access to them. Finding an optimal balance between the interests of copyright owners, users and the public defines the economic strength of copyright law.

Along this same theme, we are concerned that the current debate about the future of copyright law has failed to acknowledge the importance of economic considerations. An example is the Copyright Law Review Committee's important report on *Simplification of the Copyright Act 1968* (Part 1, 1998; Part 2, 1999). A particular feature of this report is that, while it makes recommendations for simplification and, inevitably, reform of the law, there is little (if any) discussion of their economic or broader social consequences. Similarly, Australian courts have recently made some important decisions about the scope of copyright law and its application to newer technologies, but generally without exploring the economic implications of their decisions or the policies that might lie behind them. This is not to say that economic considerations do not implicitly underlie the judicial decisions as to the scope of the law. Nor does it mean that the legislative reform proposals could not in some cases bring real improvements. There are, we believe, good economic justifications for simplifying and updating the law to take better account of modern innovation and dissemination practices (most specifically the change from paper products to software products and from physical markets to exchanges over the Internet). But in our view, explicit acknowledgement of the economic policies behind copyright law and the standards it employs can only assist a rigorous discussion about the appropriateness of the law and its standards in the current world.

Our intention in writing this paper is to promote better understanding and debate concerning the economic policies of relevance to copyright law and their implications for the proper scope and limits of the law. The paper is not definitive — nor could it be. Rather, it is hoped this will be another voice in a series of efforts by economists and lawyers in Australia to address the economic considerations that properly lie behind copyright law for now and the future.

We wish to acknowledge the contributions made to the writing of this paper by our colleagues David Brennan, Andrew Christie, David Lindsay and Janice Luck at the University of Melbourne who gave useful comments and advice on earlier drafts and preliminary texts for this paper. We are also very grateful for the thoughtful comments of Henry Ergas and Warwick Rothnie as we began formulating our ideas. Finally, we would like to thank Mary Wyburn for her determination in commissioning this paper and her dedication to ensuring that our arguments were clearly and fairly made and that the detail was accurate. Of course, any responsibility for mistakes or oversights is our own.

4 April 2000

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Introduction

The lawyer-economist Ronald Coase once said that "the law" is a giant filing system,[1] and this is certainly true for intellectual property law. Economists may observe that the function of intellectual property law is to grant exclusive property rights over innovation — rights that can be traded in the market — and that it is the possibility of reward to be obtained through the market that provides the financial incentives for investment in innovation. But for lawyers there is no intellectual property *law*, as such. Rather, there is a set of laws, each with its own boundaries. A particular innovation needs to be slotted into an intellectual property system if it is to be protected. For instance, patent law extends to inventions, design law to design features of industrial articles, trade mark law to trade marks, and copyright law to works and related subject matter. From a legal perspective, if a particular innovation does not fit within these boundaries, it cannot be protected. Nor are the boundaries *necessarily* particularly coherent in policy terms; in some cases they may *appear* to be quite out of date with the realities of innovation practices. The last point has sometimes been made quite forcefully for copyright law, particularly with respect to digital innovation, which only uneasily fits under the copyright umbrella.[2]

Nevertheless, we believe there is an economic logic to copyright law that explains its continuing importance as a dominant intellectual property paradigm in the 21st century.

This paper is structured to, in turn:

- provide a brief outline of the copyright system and its boundaries;
- consider the benefits and costs of copyright;
- identify the optimal scope and limits of copyright.

The Copyright System and its Boundaries

The current terms of copyright law are set by the *Copyright Act 1968* (Cth), as amended and supplemented. Many readers will be familiar with copyright law, but a particular purpose of including the following brief overview of the law is to stress, even at this early stage, the way in which the law functions as a system of rights and exceptions balancing the interests of a range of parties.

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[1] *The Future of Law and Economics*, Panel Discussion, First Meeting of the American Law and Economics Association, Illinois, 1990.

[2] See Australian Copyright Council, *Copyright in the New Communications Environment: Balancing Protection and Access* (Centre for Copyright Studies Ltd, 1999).

The rights granted under copyright

Copyright comprises a bundle of exclusive rights granted to copyright owners.[3] The rights can be licensed or assigned, in whole or in part.[4] Clearly they are property rights in the economic sense discussed at the beginning of this paper.[5]

Copyright in works: reproduction, distribution and moral rights

First, copyright includes the right to prevent unauthorised copying — "reproduction in material form" — of "original"[6] literary, dramatic, musical or artistic works[7] for a period of (in general) 50 years after the year the author died.[8] "Reproduction" is a broader concept here than physical or literal copying. It encompasses the making of substantially similar reproductions of the whole or a substantial part of the work,[9] and takes account of subconscious reproductions.[10] "Literary works" are defined to include computer programs and have been since the Copyright Amendment Act 1984.[11] But, even before that, the High Court took the view that computer programs, at least in source code form, could be "literary works" and therefore protected from unauthorised reproductions.[12] Soon new legislation, introduced in the form of the Copyright Amendment (Digital Agenda) Bill 1999 (Cth), will strengthen the reproduction right for computer programs by targeting efforts to circumvent technological measures to protect the information — and, in particular, efforts by commercial providers to facilitate unauthorised reproductions by others.[13] This may seem an extension of the core reproduction right in the Copyright Act. But the Act already provides for certain extended rights: for instance rights of "authorisation" of

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3 CA s 13(1). The rights are granted in the first instance to the author or, if the work is made under a contract of employment, to the author's employer: CA s 35.

4 CA s 13(2). Exclusive licensees can exercise the rights of owners (CA s 119). For the purposes of this paper the term "owner" is extended to these licensees, who effectively function as owners vis-à-vis third parties.

5 See also CA s 196(1).

6 The standard has been interpreted to require a level of skill and effort: see, for instance, *Data Access Corp v Powerflex Services Pty Ltd* (1999) 45 IPR 353.

7 CA ss 31(1)(a)(i); 31(1)(b)(i). For the "material form" requirement for a work see s 22.

8 See especially CA ss 33, 34 and below n 33 and accompanying text.

9 CA s 14.

10 *Frances Day & Hunter Ltd v Bron* [1963] Ch 587; *Autodesk Inc v Dyason* (1992) 22 IPR 163; *Data Access v Powerflex* above n 6.

11 CA s 10(1). The provision implements international standards set by the Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPs) (1994) Art 10.

12 *Computer Edge Pty Ltd v Apple Computer Inc* (1986) 161 CLR 171.

13 The Bill, introduced into the House of Representatives on 2 September 1999, responds to the Attorney-General's Department and the Department of Communications and the Arts Discussion Paper on *Copyright Reform and the Digital Agenda* (AGPS, 1997) and international standards in the World Intellectual Property Organization (WIPO) Copyright Treaty 1996. For further changes proposed to the Bill, see also House of Representatives Standing Committee on Legal and Constitutional Affairs *Advisory Report on the Copyright Amendment (Digital Agenda) Bill 1999* (6 December 1999) at http://www.aph.gov.au/house/committee/laca/digitalagenda/contents.htm.

reproduction, and of "adaptation" for literary, dramatic and musical works.[14] The adaptation right is an extended version of the reproduction right, allowing for transformations into alternative forms: for instance, from a literary into a dramatic version of the work, or from one version of a computer program into another.[15]

Second, the copyright owner has certain exclusive rights to distribute the work by way of publication, public performance (except in the case of artistic works), broadcast, and transmission to subscribers to a diffusion service (again, not for artistic works), and to authorise others to do so.[16] The courts have interpreted the publication right narrowly, to mean first publication.[17] The Act provides for secondary rights against unauthorised dealings with or imports of articles that infringe the copyright in a work or would if the articles were made in Australia.[18] But with recent amendments regarding parallel importation of books and sound recordings, these are increasingly being placed on restricted terms.[19] It is also not infringement of the copyright in an artistic work to apply a "corresponding design" to articles if a corresponding design has been registered under the *Designs Act 1906* (Cth) or industrially applied and used in commercial dealings by or with the authority of the copyright owner.[20] The principle is subject to exceptions, excluding, for instance, two-dimensional surface designs, but provides an important limitation on the scope of copyright for artistic works.[21] Once the Copyright Amendment (Digital Agenda) Bill 1999 is enacted into law, the distribution rights will be supplemented by a technology-neutral right of "communication" to the public (which will actually replace the current broadcast and cable diffusion rights).[22]

Moral rights are a third set of rights that attach specifically to authors of copyright material, protecting both their personal integrity, and — of more specific interest to economists — their valuable reputation.[23] Currently the Copyright Act only makes limited provision for moral rights, most importantly with respect to false attribution of authorship of a work.[24] New provisions planned under the Copyright Amendment

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[14] CA ss 13(2); 31(1)(a)(vi); 36. See also s 21(3), allowing for reproduction of artistic works in another dimension — but the effects of this have been ameliorated somewhat by the design-copyright overlap provisions in ss 74 – 77: see below n 20.

[15] For a definition of "adaptation", see s 10(1).

[16] CA ss 13; 31(1)(a)(ii) – (v); 31(1)(b)(ii) – (iv); 36. For the application of the broadcast and diffusion rights, see *Telstra Corp Ltd v APRA* (1997) 38 IPR 294.

[17] *Infabrics Ltd v Jaytex Ltd* [1982] AC 1; *Avel Pty Ltd v Multicoin Amusements Pty Ltd* (1991) 18 IPR 443.

[18] CA ss 37; 38 (although subject to a requirement of knowledge or reasonable knowledge of the infringement). As to the exception for authorised uses, see *Interstate Parcel Express Co Pty Ltd v Time-Life International (Nederlands) BV* (1977) 138 CLR 534 at 556 – 7; *Computermate Products (Australia) Pty Ltd v Ozi-Soft Pty Ltd* (1988) 12 IPR 487.

[19] CA ss 44A – C. There has been ongoing discussion about new provisions for computer software after reports by the Prices Surveillance Authority (see especially reports 44, 46).

[20] CA ss 74 – 77 (ameliorating the effect of s 21(3), which allows for reproduction of an artistic work in another dimension: discussed above n 14).

[21] For some proposed reforms to ss 74 – 77 see ALRC, *Designs* (Report No 74, 1995) pp 321 – 43 and the Government's response at http://www.ipaustralia.gov.au/news/govreslaw.htm.

[22] For the Bill and its background see above, n 13.

[23] For the economic arguments for moral rights protection, see R Van Den Bergh, "The Role and Justification of Copyright:– A 'Law and Economics' Approach" (1998) 1 *IPQ* 17.

[24] CA Part IX.

(Moral Rights) Bill, introduced at the end of 1999, will go further in encompassing both attribution and false attribution and a right of integrity to prevent derogatory treatment of the subject matter (including both works and cinematographic films).[25] As with all copyright, it is anticipated that the exercise of moral rights will be subject to contrary agreement, although here the possibilities for agreement are limited to consent to a use that would otherwise breach the rights.[26] Where consent (which can presumably be in exchange for money or other rights) is not given the new moral rights will provide a source of control over the future use of the subject matter by successive copyright owners where these uses are seen as likely to affect the author's interests.

Subject matter other than works and performances

In addition, certain rights regarding copying and distribution apply to related subject matters such as published editions, sound recordings and films (interpreted recently to include a computer video game, paving the way for multimedia works to be covered under this category if not as "literary" or "dramatic" works),[27] and television and sound broadcasts which are assumed not to entail sufficient skill and labour to qualify as "original" works in their own right or are too ephemeral to satisfy the material form requirement for a "work".[28] Further limited rights apply to performances of works, acknowledging the separate contribution of performers to the final product as received in the public domain.[29] These supplementary rights, which are granted to publishers, "makers" of sound recordings and films (subject to contrary agreement in the case of commissioned sound recordings and films), broadcasters and performers, facilitate the reproduction and distribution of works and other material in the public domain.[30] But they are more narrowly framed than the core copyright rights of reproduction and distribution of original works.[31] In particular, the exclusive copying right for subject matter other than works extends only to literal copying of the physical subject matter or a direct or indirect sound recording or film of the performance.[32]

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[25] Copyright Amendment (Moral Rights) Bill 1999. Films have always been only debatably "other subject matter": see Berne Convention for the Protection of Literary and Artistic Works Arts 6bis and 4.

[26] Copyright Amendment (Moral Rights) Bill cl 195AW.

[27] *Galaxy Electronics Pty Ltd v Sega Enterprises Ltd* (1997) 37 IPR 462.

[28] CA Part IV: there is no requirement of originality or material form for the protection of this subject matter, although some of the subject matter (eg published editions) embody their own requirements for material form.

[29] CA Part XIA.

[30] CA ss 97 – 100; 248J.

[31] For equivalent parallel import and secondary dealing rights, see ss 102 – 3; 112A – C.

[32] CA ss 85 – 88; 248G. As with copyright works, acts done with respect to a substantial part of the other subject matters are deemed to be done in relation to the whole: CA s 14.

Limited scope of copyright protection

The discussion so far has been concerned with the range of rights provided for under the broad umbrella of copyright. But there are significant constraints as well, as discussed briefly below.

Term of protection

Among the most obvious limits are that, with the exception of unpublished works, copyright is subject to a limited term of protection, even if this is, in the case of original works, generally defined as 50 years from the year the author died.[33] (The term for other subject matter and performances is generally 50 years from the year of publication of the subject matter, or 20 or 50 years from the performance.)[34] Even moral rights will be subject to a term of protection under the Bill: defined as the life of the author in the case of the integrity right; and the copyright term for the work in the case of the other rights.[35] Although 50 years may seem a very long time for newer information products (such as computer software), whose commercial life may be very short, there are advantages in having one standardised term for the wide range of works and other subject matter that may exist.[36] That said, other exceptions and limits in copyright law are generally more important for balancing the interests of the copyright owner and those of users and the public than the term of protection.

Fair dealing, statutory licences and other exceptions

Further, the Act permits "fair dealings" for the purposes of research or study, criticism or review, reporting news and professional advice.[37] Also permitted under the Act are backup copying of a computer program and, as a result of recent amendments, decompilation for purposes of interoperability and error correction.[38] In addition, there is an array of statutory licences under which, for instance, educational institutions can, in exchange for a standard fee (or no fee in the case of "insubstantial amounts"), copy limited amounts of copyright material for restricted purposes.[39] These provisions do not derogate from the powers of collecting societies to set their own licence terms for their members, which many of them have done.[40] It

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[33] CA s 33; see also ss 32(2); 34. In the case of works which have not been published, performed in public, broadcast or subject to sales of records before the death of the author, the term dates from when these events first occur or else is indefinite.

[34] CA ss 93 – 96; 248CA — for certain of the performers' rights the term is now 50 years (but otherwise the term is 20 years): see s 248CA(2) implementing the TRIPs Agreement.

[35] Copyright Amendment (Moral Rights) Bill 1999 cl 195AM.

[36] Van den Berg above n 23 pp 27 – 28.

[37] CA ss 40 – 43; 103A – 104; 248A (definitions of "exempt recording" and "recording").

[38] CA ss 47B – G (the provisions are in general not subject to contrary agreement: s 47H).

[39] CA Part VB.

[40] For instance, the Copyright Agency Ltd licences for educational photocopying are more widely used than the statutory licences: see further S Simpson, *Review of Australian Copyright Collecting Societies* (AGPS, 1995).

is debatable whether a residual common law exception applies for publication in the public interest, but the Constitution mandates freedom of political discussion.[41]

Limits within copyright: independent development, reproduction distinguished from productive uses, the "originality" threshold, the idea/expression dichotomy

General limitations derive from the nature of copyright itself. For instance, the exclusive reproduction and copying rights that lie at the core of copyright do not prevent independent development and use of the material. There must also be overall similarity between the original and the copy for "reproduction" or "copying" to be found. If a derivative work is sufficiently dissimilar it may not constitute a reproduction of the original work even if use was made of the work. The copying right for other subject matter is even narrower, requiring literal and even physical copying. Another limitation that derives from the (current) nature of copyright is the "originality" standard. In requiring the exercise of skill and labour before copyright will be available to a work,[42] this provides a potentially quite significant threshold that must be met in order for protection to be granted. And although more limited protection is also available to other subject matter if it falls within a requisite category, these categories are dependent on there first being a copyright work, or have their own requirements for expression and fixation.[43]

Finally, copyright is designed to protect "works" and related subject matter; not information or ideas *per se*. This sets an important limitation on the scope of copyright protection over information.[44] The courts have generally held that if only one expression of an idea is possible, that cannot be protected.[45]

Summary

As even the above brief overview shows, copyright provides a complex mixture of rights and limitations aimed at balancing the interests of owners, authors, users and the public. It is very important to understand this in assessing the benefits of copyright and the costs, an issue discussed below.

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41 See further M Richardson, "Freedom of Political Discussion and Intellectual Property Law in Australia" (1997) 19 *EIPR* 631.

42 As, for instance, in the *Data Access* case, where copyright protection was denied to the plaintiff's Dataflex computer language on the basis, *inter alia*, of insufficient originality: see above n 6, at pp 374 – 6 especially.

43 Published editions and performances presuppose a prior work, while sound recordings, films and broadcasts entail their own forms of expression and fixation.

44 For some economic rationales for these limitations which are inherent in copyright law, see further below n 98 ff and accompanying text.

45 See *Autodesk v Dyason* (1992) IPR 163 at 171 – 2; *Data Access* above n 6.

Benefits and Costs of Copyright

As noted at the beginning of this paper, the economic argument for copyright law is that it provides incentives for innovation. Copyright owners have the power to exclude potential consumers from "consuming" copyright material. This exclusionary power is important in permitting those who produce copyright material to earn rewards in the market. This increases incentives for innovation, with broader social benefits of fostering copyright-related industries and increasing the range of goods and services traded in the market.

Most of the criticisms of copyright law are qualifications of or direct attacks on this basic argument. The criticisms raise three basic questions about the economic benefits and costs of copyright, which will be considered in turn:

- whether material incentives provided by copyright are relevant to the innovative process behind copyright works and other subject matter;
- whether, given that we import more copyright material than we export, Australia is a net loser from a copyright system that rewards innovation;
- whether the costs associated with granting proprietary rights over information outweigh the benefits of copyright.

Are the material incentives provided by copyright relevant to the innovative process behind copyright material?

The argument that property rights may not be needed to provide incentives for the production of copyright material is hardly a new one. In 1928, in response to suggestions that artists were largely Bohemians to whom money meant nothing, the English art historian Roger Fry said that the reality was to the contrary. In general, artists tended to be economically conventional and, without the possibility of patronage by the Church or the State or wealthy individuals, they depended on the market for their income:

> Almost all artists who have done anything approaching first-rate work have been thoroughly bourgeois people — leading quiet, unostentatious lives, indifferent to the world's praise or blame, and far too much interested in their job to spend their time kicking over the traces.[46]

Nonetheless, it is sometimes suggested that sufficient personal incentives for innovative work may exist without copyright; or that innovators can find other ways of reaping monetary rewards from their labour, including commercial lead time.[47] Alternatively, it may be suggested that copyright protection may not be needed for *certain* new activities such as publication on the Internet, which often seems to function without any reference to copyright. So, the Office of Regulation Review

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[46] R Fry, "Introduction" to *A Record of the Collections in the Lady Lever Art Gallery* (London, 1928) cited in C Goodwin, *Art and the Market: Roger Fry on Commerce in Art*, (U of Mich Press, 1998).

[47] CLRC, *Copyright Reform: A Consideration of Rationales, Interests and Objectives* (1996) at p 18. See also Office of Regulation Review, *An Economic Analysis of Copyright Reform* (1995) at p 4 and *passim*.

(ORR) observes, "digital works are part of a booming industry — new magazines and newspapers appear almost daily on the Internet, and multimedia works are flooding the market."[48] The implication here is that copyright law, by seeking to raise the monetary rewards for those who produce copyright material, is (to the extent it succeeds) merely distributing those rewards from users and not assisting in bringing the level of innovation to a socially optimal level.

But the difficulty with proffering particular examples where innovative activity flourishes with no apparent need for copyright is that this does not address the overall significance of the incentives that copyright does provide for innovation. As Fry understood, the importance of these incentives is not diminished by there being a few people who appear not to care about money (or find alternative ways of reaping financial rewards from their activities). The economist's proposition that copyright is necessary in order to promote certain types of valuable innovation is concerned with ensuring an *efficient* amount of innovative activity. A logical implication of that proposition is that innovators should be placed in a position where they can capture a reward equal to the total benefit that they generate for society. Only then may we be sure that their risk-adjusted investment costs can fully be recovered.[49] Copyright, by granting exclusive rights that can be traded in the market, makes this possible. That some innovation may take place without apparent reference to the material incentives that copyright provides does not mean that an efficient extent of innovation can occur without them. In fact, even the experience of the Internet supports this argument. Although there may be a small but high-profile gift economy that flourished especially in its early experimental days, and a second wave of Internet "trading" in which companies were prepared to wait to see profits generated from their activities after markets could be established, the current reality of the Internet is that much of the material that is *now* being published and traded there relies very strongly on copyright.[50]

What then is the most likely implication of no copyright protection for works and related subject matter? A possible scenario — assuming first that no other intellectual property rights could be claimed for the material — is that many literary, artistic, dramatic and musical works and other subject matter which currently form the basis of industries that are important to the Australian economy would not be produced or would be severely diminished in the quantity and quality that is produced.[51] For without intellectual property rights there is no guarantee that those who now depend

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[48] ORR above n 47 p 4. For earlier arguments regarding books and computer software, see also S Breyer, "The Uneasy Case for Copyright: A Study of Copyright in Books, Photocopies and Computer Programs" (1970) 84 *Harv L Rev* 281.

[49] It is notoriously difficult to provide an accurate valuation of risk-adjusted investment costs (including opportunity costs) associated with innovation; although accounting methods are now being devised to provide better methods of valuation than previously existed, there still is a significant degree of speculation involved: see further L Edvinsson and M Malone, *Intellectual Capital* (HarperCollins, 1997).

[50] For figures on the rapidly expanding European and American Internet retail trade in traditional and other copyright products (including computer software), see M Symonds, "The dot.com Imperative" *The World in 2000* (Economist Group, 1999) pp 104 – 5.

[51] For some attempts to estimate the monetary value of Australian copyright industries, see H Guldberg, *Copyright: An Economic Perspective* (Australian Copyright Council, 1994) pp 9 – 10; J Revesz, *Trade-Related Aspects of Intellectual Property Rights* (Productivity Commission, 1999) pp 72 – 4.

on copyright would end up profiting in the long term.[52] The same goes for new information products which conceivably could come within the copyright umbrella.[53] As Teece has demonstrated with reference to numerous industry case studies, a new innovator's likelihood of success in the market will depend on the ability to offer collateral skills and resources, and in practice competitors often win out. "Situations where firms were first to commercialize a new product, but did not participate in the profits that were subsequently generated from the new product, are increasingly common."[54] The example of Xerox as the original developer of the computer in the early 1980s (before the possibility of copyright protection had been established for computer programs) is a case in point. For here "Xerox failed to succeed with its entry into the office computer business with its 'Star' system, even though Apple succeeded with the MacIntosh, which contained many of Xerox's key product ideas, such as the 'mouse' and 'windows'."[55]

A second possibility is that if copyright were not available, innovators would simply turn to alternative intellectual property systems: trade secrecy and/or contract on the one hand, or patent and/or design law on the other.[56] (Trade mark law provides a third alternative for at least some of the material now covered by copyright.)[57] The alternative systems may suit innovators' interests — provided they can satisfy their preconditions — but they offer a new range of costs for users and the public. For instance, trade secrecy rights depend on the information being secret: the owner's incentives are therefore to limit public access if the risk is that otherwise secrecy would be destroyed. And contractual measures to protect the information may look appealing for information "owners", but have the downside that owners may have little interest in contracting for rights that balance the interests of users and the public.[58] The registered patent and design systems, in turn, grant exclusive rights over the information products which are subject to their protection (they are not limited to merely reproductive uses),[59] are not confined to a particular expression — although design law comes closer than patent law in requiring this,[60] and cover even the use of

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[52] Technical self-help measures by themselves are often insufficient: see, for instance, (unsuccessful attempt to "lock" a computer program) *Autodesk v Dyason* above n 45; (unsuccessful encryption of an EEPROM) *Mars v Teknowledge* (2000) 46 IPR 248. See also K Dam, "Self-Help in the Digital Jungle" (1999) 28 *J Leg Stud* 393.

[53] As observed by Ergas, among others, the trend towards codified information products provides some explanation: "Changes in the Science and Technology System and Some of their Implications for the Protection of Intellectual Property" (1999) 39 *IP Forum* 28.

[54] D Teece, "Profiting From Technological Innovation: Implications for Integration, Collaboration, Licensing and Public Policy" in D Teece (ed), *The Competitive Challenge: Strategies for Industrial Innovation and Renewal* (Ballinger Publishing, 1987) p 185.

[55] D Teece, "Capturing Value from Innovation" (1991) *Les Nouvelles* 21 at p 21.

[56] They already are seeking to use them: see (trade secrecy) *Mars v Teknowledge* above n 52, (patent) *CCOM Pty Ltd v Jiejing Pty Ltd* (1994) 28 IPR 481.

[57] Most obviously advertising material, which currently accounts for 10 – 30% of estimated copyright industries: Revesz above n 51 p 74.

[58] There is a substantial US literature on the risks of contract as an unfettered mechanism for extending the boundaries of copyright law: see, in particular, L Lessig, "Commentary On The Law of the Horse: What Cyberlaw Might Teach" (1999) 113 *Harv L Rev* 501.

[59] Section 13 *Patents Act* 1990 (Cth); s 38 *Designs Act* 1906 (Cth).

[60] See DA s 4 (definition of a "design"), and (distinguishing this from the "fundamental form" of an article) *Firmagroup Australia Pty Ltd v B & D Doors (Vic) Pty Ltd* (1987) 9 IPR 353.

independently developed information products if otherwise they would infringe.[61] The possibilities for derivative innovation and competition in downstream markets are therefore limited under these laws. Not surprisingly, they have received a narrow reading in cases in which they come to be applied.[62] Here it seems that the high level of security afforded by the protection is seen as best suited to high level and high cost innovation (reflected also in the standard of "inventiveness" needed for a patent to be granted).[63] Copyright, mediating between the interests of owners, users and the public[64] — offering a hypothetical contract under which all parties can be conceived of as agreeing to the terms — seems well adapted both for high level and the sorts of low level, incremental innovations which are typically subject to its protection.

Does copyright, in rewarding innovation, benefit exporting countries at the cost of countries like Australia which are net importers of copyright material?

Although most economists would acknowledge that the incentives provided by copyright are important if a society is to ensure an efficient extent of innovative activity, some argue that one should be very careful about the word "society". In particular, it has been suggested that since Australia has a net deficit of copyright royalty flows out of the country,[65] we might — to put it baldly — benefit by free-riding on the innovative activity of the rest of the world. The ORR, for instance, has argued that Australia should not extend copyright protection beyond that actually demanded by our international treaty obligations because of the net costs of such protection.[66] Is the implication here that the "society" which benefits most from copyright protection would be the Western industrialised society of copyright exporters (primarily the United States and Europe)? Certainly, the ORR posits that Australia has little or nothing to gain from granting copyright beyond the extent necessary to meet its existing commitments under international law — although it is conceded that these at least should bind.[67]

It is interesting to observe the concession made for existing obligations, since they already cover most of the field. The treaty obligations include both the Berne Convention for the Protection of Literary and Artistic Works (1886)[68] and the Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPs),

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61 Although see a limited defence for prior continuous use in PA s 119.

62 See M Richardson and S Macchi, "Intellectual Property Cases in the Australian High Court: An Economic Reappraisal" [1997] 3 *EIPR* 4.

63 But see proposals for a new "innovation patent" with a lower inventiveness threshold than the current threshold for petty patents (the proposals have been accepted by the Government): ACIP, *Review of the Petty Patent System* (1995).

64 Cf K Dam, "Some Economic Considerations in the Intellectual Property Protection of Software" (1995) 24 *J Leg Stud* 321.

65 Revesz above n 51 p 125 records exports of copyright material in 1996 – 7 as worth $1240 million; compared with imports of copyright material worth $3258 million.

66 ORR above n 47 ch 5. See also, for earlier arguments to the same effect in the patenting context, T Mandeville, D Lamberton and E Bishop, *Economic effects of the Australian Patent System* (AGPS, 1982).

67 ORR above n 47 p 39.

68 *Berne Convention for the Protection of Literary and Artistic Works* (Paris, 1886).

annexed to the GATT trading agreements concluded at the end of the Uruguay Round.[69] Berne sets minimum standards of protection for copyright works and other subject matter and establishes a fundamental principle of equal treatment for participating members of the union. TRIPs makes clear that participation in international trade as a member of the World Trade Organization is subject to acceptance of Berne's standards for copyright, with equal treatment to be accorded to all Member States. The minimum standards for copyright imposed under Berne and TRIPs include:

- the right to reproduce or authorise the reproduction of a protected work,[70] with computer programs specifically designated literary works by TRIPs;[71]
- rights to make or authorise a translation or adaptation;[72]
- rights relating to public performance and communication;[73]
- broadcasting and transmission and related rights;[74]
- derivative rights for performers, producers of sound recordings and broadcasting organisations.[75]

As the ORR understands, there are clearly pragmatic reasons for Australia to maintain the general scale of copyright protection currently provided.[76] To reduce the scope beyond the minimum standards provided in Berne and TRIPs would entail costs to reciprocal treatment of Australian copyright producers under those conventions and the generally good reputation that Australia has as an active and responsible member of the international community of nations. It would also, obviously, place at risk our participation in the GATT free trade agreement, which covers a wide range of goods and services among over 130 Member States.[77] Further, there are labour market implications for copyright industries which, being highly mobile industries, can easily move aspects of their operations offshore if better facilities are provided elsewhere.[78] An internationally competitive system of copyright

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69 *Agreement on Trade-Related Aspects of Intellectual Property Rights*, Appendix 1B, Final Agreement of the GATT Uruguay Round reported at [1994] 33 *ILM* 1197.

70 Berne Art 9(1) and Arts 2 and 4 (for "protected works"); see also Art 9(1) of TRIPs: "Members shall comply with Articles 1 through 21 of the Berne Convention …"

71 TRIPs Art 10(1). The Berne Convention covers "literary" and "artistic" works (broadly defined to include dramatic and musical works) as well as films: Arts 2, 4.

72 Berne Convention Arts 8, 12; TRIPs Art 9(1).

73 Berne Arts 11 (covering dramatic and musical works), 11*ter* (public recitation of literary works); TRIPs Art 9(1).

74 Berne Art 11*bis*.

75 TRIPs Art 14.

76 See, generally, Department of Foreign Affairs and Trade, *Intellectual Property Rights: A Guide to the GATT Uruguay Round* (1990).

77 So, as DFAT says (ibid), "It is generally accepted that maintenance of such a regime has served to attract state-of-the-art technology and overseas copyright works" to Australia.

78 For some estimated figures for employment in Australian copyright industries (now rather dated), see Guldberg, above n 51 p 14.

protection is now an important part of the infrastructure which Australia offers to copyright industries considering establishing or remaining here.[79]

But what those who argue against expanding Australia's level of copyright protection beyond the scale of existing commitments under Berne and TRIPs fail to appreciate is that similar, if not the exact same, considerations guide the development of new standards for copyright protection as well. International pressures have driven the recent reforms to our copyright law. For instance, the Copyright Amendment (Digital Agenda) Bill's provisions for anti-circumvention and a technology-neutral right of communication will implement the World Intellectual Property Organisation's Copyright Treaty 1996 once the Convention comes into force.[80] The moral rights provisions in the Copyright Amendment (Moral Rights) Bill 1999 reflect new international norms for the appropriate level of moral rights protection (as well as longstanding provisions in Berne Convention).[81] It is simply not practically possible, if it ever was, to consider copyright law reform as an Australian issue divorced from considerations of what is happening in the rest of the world.

The deeper economic issue at stake in these arguments is the benefits and costs of protectionism versus free trade, which TRIPs and WIPO have been so concerned to promote. Are these only or mainly for the benefit of the exporting nations? There are good economic reasons for Australia to support the direction being adopted. The supposed benefit of free-riding which the ORR points to is misconstrued in at least two important respects. In the first place, it reveals the old mercantilist fallacy that exports are good and imports are bad which was roundly attacked by Adam Smith in his *Wealth of Nations* (1776).[82] What Smith convincingly showed is that mercantilism provides a vehicle for subsidising the inefficient efforts of local producers, who seek to prevent competition from cheaper imports to the ultimate detriment of consumers. Conversely, Smith's point was also that efficient local producers, who can effectively compete against the rest of the world, can only gain from a system that rewards their efforts (as ultimately can users, who stand to benefit from lower prices and greater choice).[83] Economists have accepted for over 200 years that mercantilism is a fallacy when applied to industries such as textiles and shoes and meat. The logical and rational position with respect to copyright industries is exactly the same. Australia does (and, indeed, should) produce some specialist types of copyright material and import others. A copyright system which limits the scope of copyright protection in order to promote free-riding on the rest of the world runs the distinct risk of promoting the second at the expense of the first.

In any event, it is clear from the simplest of indicators that our system does not offer its most significant rewards to foreign innovators. One somewhat imperfect indicator of this (since not all copyright owners belong to collecting societies) is the percentages of the amounts collected and distributed by collecting societies that are remitted overseas. These show that on average less than 20% of total funds distributed are remitted overseas.[84] The remainder is distributed to domestic

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[79] Cf DFAT above n 76.

[80] See above n 13.

[81] Berne Art 6*bis*.

[82] A Smith, *An Inquiry Into the Nature and Causes of the Wealth of Nations* (1776).

[83] Cf Revesz above n 51 p 81.

[84] The following table shows percentages remitted overseas by Australian collecting societies for amounts collected in 1993 and subsequently distributed:

producers of copyright material whose trade is in the domestic market. A particular risk of seeking to free-ride on the rest of the world by reducing or not expanding the scope of copyright protection to meet the needs of new innovation practice is that this would come at a cost to domestic activities which economically, in the current climate, are far more important to Australia.

Do the costs of copyright outweigh the benefits?

All rights have costs,[85] and there are two clear costs to copyright. First there are transaction costs entailed in creating and enforcing property rights which make exclusion possible for innovators.[86] Second, exclusion undermines the "public good" character of the information that is subject to copyright protection. Unlike physical resources, information is non-rival in character. If one user "consumes" an information product, this does not prevent others from also doing so. So, for instance, large numbers of virtually perfect copies of a book, or compact disc, or computer disc can be made with the additional costs of each extra unit being the physical costs of manufacture, which may be as little as a few cents.[87] Similarly, with access to the Internet, the costs of reproducing and disseminating software and other material that can be downloaded is close to zero. If a copyright owner does prevent some users from having access to copyright material, there is a loss in social value created. This loss is a cost of copyright law: a necessary consequence of allowing the creator or producer of information to earn a return.

The desirability of copyright law is therefore intimately tied to the question of whether the benefits — promoting innovative activity through monetary rewards — outweigh the costs — transaction costs and the possibility of inefficient diffusion of the material produced.[88] For most economists the efficiency of providing incentives so that initial innovation may occur overrides any consideration of residual diffusion costs (and the transaction costs of a copyright system are seen as generally cost-effective). As Ordover and Baumol state:

Funds Distributed Overseas as a Percentage of Total Funds Distributed (collected 1993)

Collecting Society	Percentage remitted overseas
AMCOS	16.8
APRA	18.0
AVCS	21.0*
CAL	8.9

Source: Simpson, above n 40 pp 147 – 8; Bureau of Transport and Communication Economics, *Economic Effects of Extended Performers' Rights* (1996) p 14.

*Information supplied by the AVCS.

85 S Holmes and C Sunstein, *The Costs of Rights: Why Liberty Depends on Taxes* (Norton,1999).

86 Ibid pp 66 – 67 ("Private property is not only protected by government agencies … It is more generally a creation of State action. Legislators and judges define the rules of ownership, just as they establish and interpret the regulations governing all of our basic rights.").

87 Michael Ellis, the Motion Picture Association's Director of Anti-Piracy For the Asia-Pacific Region, in "NZ tipped as Target for 'Pirates'", *The Dominion* (Wellington), 1 October 1999.

88 Cf J Ordover and W Baumol, "Antitrust Policy and High-Technology Industries" (1988) 4 *Ox Rev Econ Pol* 13 at 14.

> Knowledge (information) is quite unlike any other productive asset because of its public goods character, with all the well-known problems of such goods. Low diffusion costs for the knowledge asset suggest that public policy should encourage its wide-spread use, and hence suggest that there should be a minimal amount of property right in the asset. But if the owner of the knowledge asset has only minimal property rights, she may not be able to appropriate the initial investment costs. As a result, the initial investment may not be undertaken. This argues for public policies that make exclusion cheap, to the detriment of diffusion.[89]

But others have disagreed, at least for some copyright material,[90] or expressed an uneasy neutrality on the issue. The Copyright Law Review Committee is particularly cautious in this regard. In a recent paper on copyright policy it raised the question of whether "the public interest [is] best served by production inducements or by consumption inducements", only to leave this important issue unanswered.[91] Ideally, the question of the costs versus the benefits of copyright — and by implication of copyright law — should be addressed *and resolved*.

Three comments can be made here. First, what is often forgotten when considering the trade-off between the benefits of exclusion in promoting innovation and the detriment that may be suffered to diffusion is that the loss in social value that may arise when copyright owners attempt to earn a profit represents a cost also for them. This simplistic exclusionary view comes from the notion that a copyright owner would charge the same price to all users. This need not be the case. An efficient pricing model is rather one that would permit copyright owners to charge different prices corresponding to the different values that different users or classes of users apparently place on the use.[92] Low value as well as high value users can gain access to the information product when under a single price model the high value users would have been prepared to pay more and the low value users would be excluded.[93] While no pricing model can capture all the social benefits associated with the use of copyright material (and the risk is that in seeking to do so some valuable uses may actually be precluded), it is feasible to construct a model which can distinguish between high and low value uses and price accordingly.[94]

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89 Ibid.

90 See, for instance, ORR above n 47.

91 CLRC above n 47.

92 See, generally, C Shapiro and H Varian, *Information Rules* (Harvard Business School Press, 1998).

93 Cf *ProCD Inc v Zeidenberg* 86 F 3d 1447 (1996, US Court of Appeal): different prices charged to commercial and private users of a shrinkwrapped computerised database were enforceable under the Uniform Commercial Code. Easterbrook J said at 1149:

> The database in SelectPhone™ cost more than $10 million to compile and is expensive to keep current. It is much more valuable to some users than to others ... If ProCD had to recover all of its costs and make a profit by charging a single price — that is, if it could not charge more to commercial users than to the general public — it would have to raise the price substantially over $150. The ensuing reduction in sales would harm consumers who value the information at, say, $200. They get consumer surplus of $50 under the current arrangement but would cease to buy it if the price rose substantially. If because of high elasticity of demand in the consumer segment of the market the only way to make a profit turned out to be a price attractive to commercial users alone, then all consumers would lose out — and so would the commercial clients, who would have to pay more for the listings because ProCD could not obtain any contribution towards the costs from the consumer market.

94 See J Gans, P Williams and D Briggs, *Clarifying the Relationship Between Intellectual Property Rights and Competition* (Report prepared for the National Copyright Industry Alliance, submission to the Review of Intellectual Property and Competition, Dec 1999).

Second, those who stress that copyright imposes costs to diffusion often exaggerate the market power vested in a copyright owner. In most cases this can be quite limited. A copyright owner may in practice have no more market power than a restaurant located on a street. There are often substitute products available that limit a copyright owner's ability to raise prices and exclude use. Consequently, copyright owners may at best seek to cover the risk-adjusted costs associated with producing copyright material. But in the long term they are unlikely to earn more than "normal" economic profits.[95] In fact, as the limited number of competition cases involving copyright indicates, there does not appear to be a significant problem of copyright ownership *per se* giving rise to more than transitory market power. In particular cases where this may occur, competition law provides a vehicle for targeting abuses. The broadly framed provisions on restrictive dealing and misuse of market power in the *Trade Practices Act 1974* (Cth) enables the Australian Competition and Consumer Commission, the Competition Tribunal and courts to actively address anti-competitive behaviour by copyright owners, including efforts to keep competitors at bay or to use existing market power to leverage into new markets.[96]

Third, copyright law itself provides a vehicle for addressing the costs of copyright: promoting diffusion *as well as* exclusion and establishing relatively clear and simple standards and limits that, from a transaction cost perspective, maintain a low level of friction in actual cases.[97] For instance, that copyright does not extend to ideas avoids transaction costs of identifying and maintaining exclusive rights over ideas and diffusion costs for information that may be exceptionally valuable to users (both in terms of the potential for derivative innovation and the possibility of uses that may be difficult to value in economic terms).[98] That infringement is defined in terms of reproduction, or copying, distinguishes and exempts productive uses. Even if this comes at the expense of exclusion for a copyright owner, diffusion here has a particular value in promoting derivative innovation and ensuring the user-innovator's investment costs can be recovered.[99] That independent development is not precluded increases the prospects for diffusion of the information (now coming

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95 Normal economic profits occur when revenue just covers the risk-weighted opportunity cost of the innovation.

96 Under s 46 the Act operates to restrain the use of market power to inhibit further competition (see also s 47). Further, under s 45 the Act prohibits copyright owners who individually do not have market power from eliminating competition by acting collectively. However, the Act recognises that there may be circumstances in which conduct that lessens competition is nevertheless of value to society. Part VII permits such conduct to be authorised, and so exempted from the prohibitions in the restrictive trade practices provisions of the Act. There is a separate regime in the Act for access to essential facilities — TPA Part IIIA — but this regime expressly does not apply to intellectual property: see s 44B (defining a service to exclude intellectual property).

97 Remedies for copyright infringement can also be tailored to promote diffusion and limit transaction costs: see, generally, G Calabresi and D Melamed, "Property Rules, Liability Rules and Inalienability: One View of the Cathedral" (1972) 85 *Harv L Rev* 1089.

98 Cf Dam above n 64 p 337. Cf Landes and Posner, claiming costs of non-exclusion are not particularly high for ideas since they are easy to come by: "An Economic Analysis of Copyright Law" (1989) 18 *J Leg Stud* 325 at p 349. Another view is that if investment costs are high, governments should provide support (preferably coordinating efforts at the international level): J Stiglitz, "Knowledge as a Global Public Good" in I Grunberg, and M Stern, *Global Public Goods: International Cooperation in the 21st Century* (1999) p 320.

99 Can derivative innovation also be facilitated under the private property pricing model referred to above n 92 ff? The situation posited here is more complicated than previously considered, but would not necessarily change the general conclusions.

from more than one source) and facilitates competition in the long term, with obvious benefits for consumers.[100]

Summary

Copyright, promoting exclusivity of copyright works and other subject matter, provides useful and beneficial incentives for innovation. Broader social benefits include fostering efficient copyright industries and facilitating trading markets internationally and domestically. There are also costs associated with copyright — particularly, transaction costs associated with defining and enforcing the rights and the possibility of more limited diffusion, undermining the essential "public goods" character of the information. These should be addressed directly. Competition and copyright laws provide vehicles for balancing the interests of copyright owners, users and the public so that social costs are kept to a minimum.

Optimising Copyright — Reform Issues

Even though, as argued above, there is an economic logic to copyright law and also competition law in addressing downstream costs of copyright protection, there are outstanding and unresolved issues of the optimal scope of these laws. In particular, it has been suggested that copyright law could be simplified and improved in various respects to find a better balance between the interests of copyright owners, users and the public. There have also been longstanding and ongoing arguments concerning the exact boundary between copyright law and competition law. These will be addressed in turn.

Optimal scope (and limits) of copyright law

One problem that needs to be addressed is simply the drafting and volume of the legislation that now grants and sets the limits on copyright protection. The *Copyright Act 1968,* as amended (and now to be amended under the Copyright Amendment (Digital Agenda) Bill) is certainly long, complex and piecemeal — especially in its treatment of new technologies such as computer programs and the Internet. The government has accepted the need for simplification of the law, and referred the matter to the Copyright Law Review Committee. In its report the committee has made far-reaching proposals with a view to simplification.[101] But inevitably, the proposals could not be confined to simplification.[102] They question some of the fundamental categories and standards used under the Act, their appropriateness in an environment dominated by new technologies that did not exist at the time the Act was drafted, and the optimal shape of copyright law for the 21st century. They provide a useful vehicle for considering reform of the law.

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[100] Cf Dam above n 64 p 337.

[101] CLRC, *Simplification of the Copyright Act 1968 (Cth),* Part 1 (1998); Part 2 (1999).

[102] As many commentators point out: see, for instance, S Ricketson, "Simplifying Copyright Law: Proposals From Down Under" [1999] 11 *EIPR* 537 at 543 – 4.

The CLRC's recommendations, which will be discussed in turn, include:

- abolition of the "material form" requirement for copyright works. Although expression, rather than ideas would still be the focus of protection, more ephemeral forms of expression would be protectible;[103]

- a higher standard of "originality", defined as "significant intellectual effort", required for copyright protection.[104] Now "creations" would have the full protection against reproduction (including adaptation) and moral rights. "Productions", which failed to meet the "significant intellectual effort" standard but did entail labour and effort, would have protection against literal copying ("exact reproduction"). The new categories would replace the current categories of works and other subject matter and performers' rights;[105]

- the Digital Agenda Bill's technology-neutral communication right to be accommodated under a broader right of "dissemination to the public", which would sit alongside the broader "reproduction right" (covering both exact and non-exact reproductions) and moral rights.[106] The dissemination right would be inclusively defined to cover also the current rights of first publication and performance as well as, possibly, a new distribution right[107] for articles which embody a creation or production.[108] The treatment of parallel imports is left open;[109]

- a general "fair use" exception with a non-exhaustive list of examples which would include but not be restricted to the current fair dealing provisions in the Copyright Act.[110]

Should the "material form" requirement be abolished?

The particular reason that the Copyright Law Review Committee puts forward for abolishing the material form requirement is the problem of accommodating new

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[103] *Simplification,* Part 2, pp 59 – 61.

[104] Ibid pp 54 – 7; 61 – 64; 64 – 8. The term of protection would generally be 50 years from the death of the person who undertakes a "creation"; the period for "productions" would generally be 50 years from the first dissemination: ibid p 75.

[105] Ibid pp 66 – 8. One member of the committee dissented in favour of more modest reforms: ibid pp 92 – 3.

[106] Ibid pp 68 – 74.

[107] The distribution right, which is limited to distributions by way of sale or other transfer of ownership, would implement Art 6 of the WIPO Copyright Treaty 1996, and that is the committee's main motivation for discussing it: ibid pp 36 – 7.

[108] The CLRC, however, recommended that the WIPO distribution right, if implemented, be restricted in accordance with the treaty provision to exclude published editions and tangible embodiments of a broadcast: ibid p 72 (one member dissenting on the issue). It was also suggested that, in accordance with the US "first sale" doctrine, the right should be exhausted by first sale or other transfer of ownership of the article with the authorisation of the owner: ibid pp 37 – 8. For the US "first sale" doctrine, see further MB Nimmer and D Nimmer, *Nimmer on Copyright* Vol 2 (Mathew Bender) at p 8 – 148 ff.

[109] Ibid p 38.

[110] *Simplification*, Part 1, pp 54 – 55.

types of technology, particularly computer software, within a definition focused on physical form.[111] In fact the problem is much broader. Copyright lawyers have long appreciated the problem of extempore speeches and impromptu performances which may be reproduced or copied by others (even in a material form) but fail themselves to satisfy the Copyright Act's formal requirement of "material form" and are therefore without protection.[112] Abolition of the material form requirement may increase transaction costs associated with identifying copyright material, but would have the advantage of applying the exclusion umbrella across a wider class of information products that otherwise satisfy the requirements of the law, including a degree of expression and originality.

Should the originality threshold be higher?

The current originality standard sets a relatively low threshold of skill and labour.[113] In the past the economist's view has commonly been that, provided not too much is expected of the skill element, this is broadly consistent with the economic idea that the protection encourages innovation not creativity *per se*.[114] But a higher standard of originality applies in the United States, where mere "sweat of the brow" productions are excluded,[115] and in Europe, where the standard is generally one entailing personal intellectual effort.[116] The CLRC's proposed reclassification into "creations" and "productions", defined in terms of whether intellectual effort was contributed or not, would have the benefit of offering a technology-neutral solution to the historical and artificial categories of works and other subject matter, the second enjoying much lesser protection on the perhaps mistaken premise that less originality is involved in their production.

But there are problems also associated with expecting courts to assess the significance of intellectual effort. The transaction costs associated with such a nebulous and subjective standard could be very high.[117] Secondly there is a real concern as to the desirability of offering a lower level of copyright protection to "productions", including, for instance, many databases, which while not satisfying any intellectual effort standard, may entail high investment costs and serve important utilitarian purposes.[118] That a higher originality standard applies under European civil law systems has little to do with economic arguments and more to do with the moral

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[111] Ibid ch 5.

[112] For a brief discussion, see S Ricketson, *The Law of Intellectual Property: Copyright Designs and Confidential Information* (Butterworths, 1999). For a different approach under European copyright systems, see G Metaxas-Maranghidis (ed), *Intellectual Property Laws of Europe* (Chancery Law Publishing Ltd, 1995).

[113] *Data Access v Powerflex*, above n 6.

[114] As pointed out by J Ginsburg, "Creation and Commercial Value: Copyright Protection for Works of Information" (1990) 90 *Col L Rev* 1865.

[115] *Feist Publications v Rural Telephone Services Co* 499 US 340; 113 L Ed 2d 358.

[116] For the Continental European standards (centred around personal intellectual effort), see Metaxas-Maranghidis above n 112. See also (adopting a copyright/sui generis dual system for databases, with the first restricted to databases which "by reason of the selection or arrangement of their contents, constitute the author's own intellectual creation"), *European Directive on the Legal Protection of Databases* (1996) *OJ L* 44.

[117] Cf (from a practitioner's perspective) K Klaric, "Editorial" (1999) 37 *IP Forum* 2.

[118] Cf D Karjala, "Copyright and Misappropriation" (1992) 17 *Dayton L Rev* 885.

arguments for copyright protection that historically have dominated there. These considerations are not irrelevant to moral rights protection, which finds a particular justification in the author's close connection with the material.[119] But for the "economic" rights, a simpler solution to the artificiality of categorising copyright material in terms of works and other subject matter would be to apply the same reproduction and distribution rights to all subject matter based on skill and labour (or perhaps just labour and effort).[120]

Should reproduction and distribution rights be extended? Should parallel imports be exempted from the scope of a copyright owner's control?

The current exclusive rights of reproduction and distribution represent an assessment that some uses — such as reproduction, (first) publication and performance — are high value, and therefore singled out as the owner's exclusively to keep or trade in the market. But the Copyright Amendment (Digital Agenda) Bill already recognises that the nature of the rights that may be valuable for an owner change with technology. The CLRC's proposed classification of copyright under broad categories of "reproduction" and "dissemination to the public" (and moral rights) would have the advantage of clarifying the essential nature and functions of the rights and enabling gaps created by new technology to be easily filled.[121]

But why are parallel imports treated as separate in the CLRC's proposals? There are some problems here. The recent reforms for books and sound recordings have less to do with simplifying and filling out a copyright owner's reproduction and distribution rights and more to do with, through a series of elaborate provisions, restricting them in favour of free importation (provided the articles made overseas do not infringe the owner's rights).[122] These reforms purport to respond to real problems of monopolistic and collusive practices that have emerged in the industries that they affect.[123] Economists have sometimes supported a general trend towards liberalisation of parallel imports, arguing that "[t]he prohibition on parallel importing, by preventing international price arbitrage, has allowed monopolistic price discrimination between national markets".[124] But another view is that the reforms *at best* provide a model for tailored responses to particular problems in those industries.[125] They need not be

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[119] Even the economic justification of moral rights is based on the effect of the use for the author's reputation as a creator: see Van den Berg above n 23.

[120] The "labour and effort" standard is the one favoured by the CLRC for "productions": see above n 105.

[121] Although, as noted above, the CLRC contemplates that the WIPO distribution right would be subject to the US first sale doctrine: see above n 108.

[122] In particular, with respect to books and sound recordings: see above nn 18, 19 and 31.

[123] See, for instance, T Papadopolous, *Copyright, Parallel Imports and National Welfare: The Australian Market for Sound Recordings* (Victoria University of Technology Department of Applied Economics, Working Paper No 2/99), with evidence of concentration in the sound recording market (over 80% of the market held by six companies). There have also been various reports on the book publishing, sound recording and computer software industries by the Prices Surveillance Authority.

[124] Revesz above n 51 p 50, (although adding that there may need to be "supplementary legislation to help combat IP piracy"). See also A Fels, "Repeal of Parallel Import Restrictions: A Step Forward for Copyright in Australia and New Zealand" (1998) 35 *IP Forum* 14.

[125] They may not be justified. Just as the *Trade Practices Act 1974* (Cth) no longer has special provisions relating to monopolistic price discrimination, so other instruments of public policy should be loath to attack price discrimination among the geographical regions of the world.

taken as a model for general restrictions on a copyright owner's rights. The overall efficiency of a pricing mechanism under which high value and low value users pay according to the value they place on the product applies across borders.[126] Australians stand to benefit from a system under which copyright owners can be guaranteed to recover all the benefits associated with the use. Then, as in the US (which generally bars "grey imports" manufactured abroad),[127] if there are particular problems of market power or restrictive practices that emerge in an industry, these can be targeted under general principles of competition law.[128]

Should "fair use" be an open-ended exception to infringement?

The CLRC's proposed expansion of the fair dealing defences into a general fair use exception follows the US model.[129] The benefits of the approach would be a more flexible exception that takes into account the quite diverse situations where users and the public interest may be at stake (for instance, including freedom of speech, a value which is hard to quantify in price terms and may benefit a broad and indeterminate class).[130] The cost is greater uncertainty and transaction costs of arguing around an uncertain and subjective standard in the courts.[131] With an unfettered discretion there is also a risk that some uses which could be subject to pricing in the market would be mandated as *free* use.[132] We have stressed in this paper that an ideal economic pricing model is one that captures all the benefits associated with a particular use[133] but if even some of the benefits can be captured under a standardised licence scheme this is preferable to one under which none can be. The CLRC has anticipated the problem, recommending that in assessing the "fairness" of the use, account should be taken of the effect of the use on the potential market for the copyright work or other subject matter.[134] Ideally this should be specified as a determinative consideration.[135] Courts would then be required to pay close attention to the availability or potential availability of individual licences, including standard licence schemes which reduce

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[126] See above at n 92 ff and accompanying text.

[127] The US first sale doctrine suggests that parallel imports cannot be prevented per se once articles have been sold with the authority of the copyright owner. But this assumes the articles were lawfully made. The last requirement has been construed by courts to mean lawfully made in the US: see Nimmer and Nimmer, above n 108 at pp 8-165 – 8-178.3.

[128] Cf W Rothnie, *Parallel Imports* (Sweet & Maxwell, 1993) pp 593 – 4.

[129] See discussion at CLRC, Part 1, ch 6.

[130] See also economic rationales for a fair use defence offered by W Gordon, "Fair Use as Market Failure: A Structural and Economic Analysis of the Betamax Case and Its Predecessors" (1982) 82 *Colum. L Rev* 1600.

[131] Cf Ricketson above n 102 at p 542. Here the role of courts in clarifying the new standard for the longer term becomes crucial, but even they can benefit from guidance.

[132] Cf J Spoor, "General Aspects of Exceptions and Limitations to Copyright: General Report", L Baulch, M Green and M Wyburn (eds) *The Boundaries of Copyright: Its Proper Limitations and Exceptions* (Australian Copyright Council, 1999) p 29.

[133] See above at n 92 ff and accompanying text.

[134] The criterion already applies to the research or study defence: CA s 40(2). The CLRC recommends it be extended to the proposed fair use exception: CLRC above n 129 p 54.

[135] In practice it is treated as such under US law, as the CLRC acknowledges: ibid pp 47 – 48.

transaction costs by setting standard terms and providing for collective administration of owners' rights.[136]

Optimal reach of competition law with respect to copyright

As pointed out earlier, most copyright owners are not in a position to exercise market power on a long-term basis, and this provides a restraint on the diffusion costs that may be associated with copyright. Competition law also provides an obvious and useful vehicle for targeting misuses of market power and other restrictive practices. But one of the extraordinary features of the Copyright Act and the Trade Practices Act is how little they have to say about each other. With limited exceptions,[137] there is no clear indication in either Act of which policies should prevail in the event that the exercise of a copyright owner's rights may have the effect of lessening competition in a market. By and large, competition authorities and judges have little guidance as to how to reconcile the apparently conflicting policies of copyright and competition law at the intersection.

Some examples of remaining areas of confusion and uncertainty are:

- difficulties associated with reconciling the Trade Practices Act's broad prohibition on misuse of market power, including refusal to deal, with the economic policies behind copyright law. In what circumstances should copyright owners who have market power be permitted to argue that exclusion of users is justified to provide incentives for innovative activity? Australian courts have not pronounced on that interface. Here they could go two ways. On the one hand, US courts have sometimes indicated that a rebuttable presumption operates in favour of a copyright owner's freedom to trade — or not — as the owner chooses.[138] On the other hand, the Australian Competition and Consumer Commission apparently sees its role as facilitating access to "essential" information.[139] No doubt, if and when cases come to court, copyright owners will contest any suggestion that the importance of information to a competitor should be sufficient *per se* for the application of competition law;

- the different treatment of terms and conditions of licensing under copyright law on the one hand (basically non-prescriptive, but with limited statutory exceptions) and the approach adopted under the Trade Practices Act.[140] The restrictive trade practices provisions appear to contemplate intervention on the basis that restrictions may be anti-competitive not only in the licensor's market

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[136] See further, on the efficiency of standard licences administered by collecting societies: Simpson above n 40 and Merges, R, "Contracting Into Liability Rules: Intellectual Property Rights and Collective Rights Organisations" (1996) 84 *Calif L Rev* 1293.

[137] See in particular s 51, discussed below n 142 ff.

[138] See *Data General v Grumman's System Support Corp* 36 F3d 1147 (1st Cir, 1994).

[139] The Commmission has already gone some direction down this track, recently obtaining an undertaking from Telstra to give access to its subscriber database to firms who wish to produce directories that compete with Telstra: ACCC media release "Telephone directory data now accessible to all" 19/2/1997. See also ACCC media release "Weather court case settled" 21 May 1997 at http://www.acc.gov.au/archiv97/weather.htm.

[140] Note also the uncertain effect of TPA s 51AC (unconscionable conduct in business transactions) for licensing practices between copyright owners and users.

but also in the licensee's. Does this mean that copyright owners could be required to create competition in markets that use their technology, restricting their ability to subdivide their rights and to charge different prices for differently valued uses?[141] There is no clear answer, but the Act exempts at least some intellectual property licence conditions from some of the restrictive trade practices provisions of the Act.[142] There is a benefit here in identifying certain conditions in copyright licences that do no real competitive harm. The National Competition Council has recently reviewed the exemptions and recommended that in substance they remain.[143] It is hoped the government will accept the substantive recommendation;

- the potential for intervention in a copyright owner's practices under the authorisation procedures of the Trade Practices Act. The Act does not prohibit a copyright owner who has market power from charging a monopoly price and, generally, economists agree that monopoly pricing should not be regulated *per se* (if the only concern is distributional). However, if the conduct is subject to authorisation, the ACCC and the Copyright Tribunal have shown themselves willing to exercise a degree of control in the "public interest". [144] (Authorisation is permitted for conduct that otherwise would breach the anti-competition provisions of the Act.)[145] So in a recent case where authorisation was sought for the arrangements that make up the Australasian Performing Right Association's system of operations,[146] the Australian Competition Tribunal did not go as far as the Commission in refusing authorisation on the basis that the system permitted monopoly pricing.[147] Nevertheless the Tribunal required APRA, as a condition of authorisation, to put in place an informal dispute mechanism that might in the

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[141] The US Department of Justice rejects the appropriateness of such intervention, with reference to the following hypothetical example:

> ComputerCo develops a new software program for inventory management. The program has wide applications in the health field. ComputerCo licenses the program in an arrangement that imposes both field-of-use and territorial limitations. Some of ComputerCo's licenses permit use only in hospitals; others permit use only in group medical practices. ComputerCo charges different royalties for the different uses. All of ComputerCo's licenses permit use only in specified portions of the United States. None of the licensees are actual or likely competitors of ComputerCo in the sale of inventory management systems.

Antitrust Guidelines for the Licensing of Intellectual Property, US Dept of Justice and the Federal Trade Commission, 6 April 1995, pp 7 – 8.

[142] TPA s 51(3) exempts conditions which "relate to" the work or other subject matter in which copyright subsists (but does not extend to s 46). In *Transfield Pty Ltd v Arlo International Ltd* (1980) 144 CLR 83, Mason J said a condition did not "relate to" the intellectual property if it seeks to gain advantages collateral to the intellectual property.

[143] NCC, *Review of Sections 51(2) and 51(3) of the Trade Practices Act 1974* (AGPS, 1998).

[144] The Competition Tribunal has described "public benefit" as "anything of value to the community generally, any contribution to the aims pursued by society, including as one of the principal elements ... the achievement of efficiency. ... [C]ommonly efficiency is said to encompass allocative efficiency, production efficiency, and dynamic efficiency": *Re Seven-Eleven Stores Pty Ltd* (1994) ATPR 41-357 at 42,677.

[145] TPA Part VII permits authorisation of conduct which may be associated with a lessening of competition but is, on balance, beneficial to society.

[146] APRA's system includes arrangements under which APRA both acquires rights from Australia's composers and overseas societies and licenses users.

[147] *Re Application by Australasian Performing Right Assn* (1998) ATPR (Com) 50-256 at paras 8.2.20.

future become a basis for arbitrating on monopoly price issues (in the same way as the Copyright Tribunal does for large users);[148]

- the unfettered nature of the remedies available for competition law breaches and the residual potential that still exists for monopoly price regulation to occur in the future. For instance, will courts now take it upon themselves to regulate prices, say, in fashioning remedies for a refusal to licence? The precedents from overseas are mostly against this.[149]

Summary and implications

What are the best prospects for the interface between copyright and competition law? By and large, the trend among economists is to urge a light-handed approach to competition law in regulating practices adopted by innovators, pointing out the uncertain effects for innovation and potential competition in the long run (since today's innovators may be tomorrow's competitors) if a more restrictive approach is adopted. Ordover and Baumol elaborate as follows:

> [I]n high-technology industries, the relevant lines of inquiry would appear to be upon the following questions: (a) Does the dominant firm in the product market also currently dominate the R&D stage? (b) If it does, how likely is it that such dominance will persist? (c) Given that lowering entry barriers into the R&D stage tends to improve short-run and long-run efficiency, are there significant entry barriers into the relevant R&D stage, and can those barriers be raised strategically by the dominant firm? And, (d), Given the answers to questions (a) – (c), what trade-offs will antitrust intervention entail if incremental improvements in the current diffusion of the existing stock of knowledge alter the incentives for future investments in R&D?[150]

As the above statement makes clear, the case for intervention under competition law is strongest where an intellectual property owner uses market power to prevent or restrict competition in innovation markets. In the light of that, the recent US judgment which found that Microsoft had used its market power in operating systems to inhibit the development of Internet-based technologies that were threats to Microsoft's continued dominance[151] is interesting indeed. For the decision (although already subject to appeal) can be seen as both pro-competition and pro-innovation.[152] It may be hoped that future work on the interface between intellectual

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[148] *Re Application by Australasian Performing Right Assn* (1999) ACompT 3 at paras 312-5, 331. The Copyright Tribunal's powers are found in CA Pt VI.

[149] In the European *Magill* case, concerning a refusal to license television programming information for the purposes of a composite television guide, the Court of Justice held merely that the parties should negotiate "reasonable" terms: *Radio Telefis Eireann v Commission of the European Communities* (the Magill case) [1995] FSR 530. The Privy Council in *Telecom Corporation of New Zealand v Clear Communications* [1994] 1 NZLR 385 adopted an "efficient component pricing principle", but there was (in a separate part of the NZ Act) a procedure for regulation of prices in monopolised markets.

[150] Ordover & Baumol above n 88 at pp 15 – 16.

[151] *US v Microsoft Corporation*, findings of facts of Judge Jackson, US District Court for the District of Columbia, 9/12/1999; conclusions of law and order 3/4/2000. The findings of fact are published on the Internet at http://www.usdoj.gov/atr/cases/f3800/msjudgex.htm. The conclusions of law and order are available at http://usvms.gpo.gov/.

[152] See, for instance, Judge Jackson's characterisation at p 10 of the conclusions of law:

property and competition law will focus on the common purposes of, rather than the apparent differences between, these laws.

Conclusions

The message of this paper is generally positive for copyright. In our view, copyright has the benefit of promoting exclusivity of copyright works and other subject matter and providing important incentives for innovation. Both copyright and competition law provide vehicles for balancing the interests of copyright owners, users and the public so that social costs are kept to a minimum. In this light, some of the reforms proposed to copyright law should be viewed with caution, while others — particularly those that would simplify and clarify the law — are worthwhile. Ultimately, the success of these reforms, as of the current law, will depend on the expertise and responsiveness of judges to the economic as to other policy considerations that lie behind the law. Similarly, in the case of competition law, the expertise and responsiveness of decision-makers are crucial to achieving an optimal mix of innovation and competition objectives in the way the law actually operates.

> [Microsoft] mounted a deliberate assault upon entrepreneurial efforts that, left to rise or fall on their own merits, could well have enabled the introduction of competition into the market for Intel-compatible PC operating systems. While the evidence does not prove that they would have succeeded against Microsoft's actions, it does reveal that Microsoft placed an oppressive thumb on the scale of competitive fortune, thereby effectively guaranteeing its continued dominance in the relevant market. More broadly, Microsoft's anticompetitive actions trammeled the competitive process through which the computer software industry generally stimulates innovation and conduces to the optimum benefit of consumers.

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