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Private Copying and Fair Compensation:
A comparative study of copyright levies in Europe

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2 The research was funded by the Economic & Social Research Council (ESRC grant: RES-173-27-0220) as part of an academic fellowship at the UK Intellectual Property Office (IPO). A summary of the findings as well as the underlying empirical data were made available to the Hargreaves Review of Intellectual Property and Growth, and published in April 2011 as a working paper on the website of the Centre for Intellectual Property Policy & Management (CIPPM). The Hargreaves Review cites the research in developing a recommendation to introduce a limited private copying exception without compensation. Digital Opportunity, A Review of IP and Growth, section 5.30: “As right holders are well aware of consumers’ behaviour in this respect, our view is that the benefit of being able to do this is already factored into the price that right holders are charging. A limited private copying exception which corresponds to the expectations of buyers and sellers of copyright content, and is therefore already priced into the purchase, will by definition not entail a loss for right holders.” However, it should be noted that this academic research, and the Hargreaves Review commissioned by the UK government were entirely separate processes. Whilst this report indeed deplores the incoherence of the EU concept of fair compensation based on harm, and advances a de minimis interpretation for a narrowly conceived private copying exception, it also finds that there may be an economic case for statutory licences with levy characteristics. Opinions expressed in the report are purely those of the author.
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.

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.
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 “Framework for analysis” reviews possible rationales for state regulated levy systems. These supporting documents are made available as separate files:


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].”

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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) Participation in file sharing networks / sharing digital storage facilities
(v) Online publication, performance and distribution within networks of friends
(vi) 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).

3. Implementation of the private use exception in EU countries
Under the Information Society Directive, only activities (i), (ii) and (iii) 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);\(^4\)
- 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.

\(^4\) 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.
4. Aggregate revenues, levy scope and levy density

The 2001 Information Society Directive introduced the requirement of “fair compensation” for statutory “private copying” exception 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 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.
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.

* 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. Bulgaria
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 taxation (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).\(^5\)

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

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\(^5\) The methodology for product and country selection, as well as the process of data collection is explained in detail in Study II.
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 taxes; 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 taxes, 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”. 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. 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. In total, 1.63

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6 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.

7 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).

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 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.
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 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”) 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.”

(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.


10 Varian, ibid. p. 130.
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 (vi)] 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.\footnote{See Supporting Study III.}
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 interoperability 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 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 Apple’s agreement with right owners are not known. 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. This is in urgent need of further empirical research prior to legislative action on copyright levies.

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