



Sustaining creation and a competitive content business in the EU:

What is the role of
copyright levies?

Copyright needs modernizing for the digital age

Legal digital content sales are vital for rights holders and for the health and growth of the whole digital ecosystem. Our economic future depends on this converging world of creativity technology. Our recent work has looked at how to make the content ecosystem as dynamic as possible.

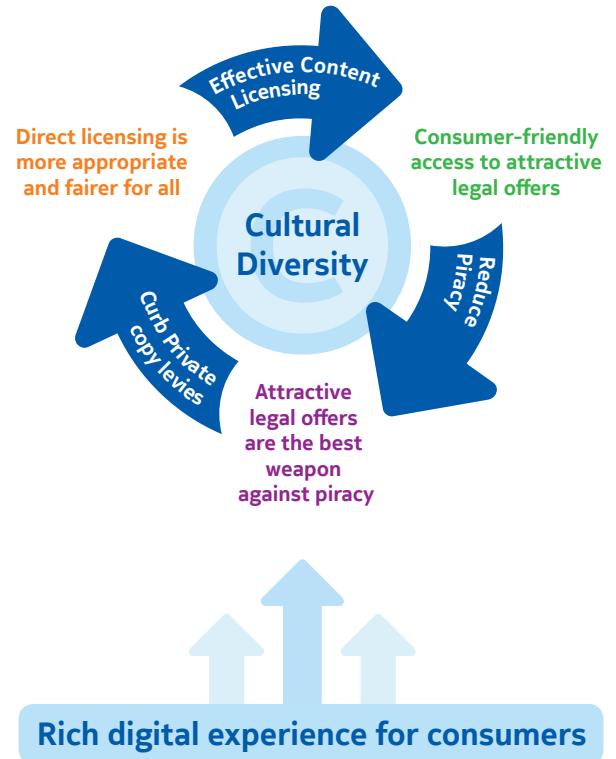
Digital content sales must be made easier and more attractive across a Digital Single Market. Digital copyright policy should foster a vibrant and thriving market for the distribution of legitimate digital content through innovative services, where right holders are fairly compensated, in support of Europe's unique cultural wealth and intolerant of unauthorised copying.

A holistic approach to copyright reform in the EU is needed. Policymakers should explore the correlation between Content Licensing, Private Copy Levies, and Reducing Piracy, in order to provide a rich digital experience for consumers, while enhancing Cultural Diversity.

As research by both the Université Libre de Bruxelles and Oxera show, reform of the copyright levy system is urgent. This analogue system is holding back all participants in the digital ecosystem: consumers, manufacturers, services providers and rights holders.

**Esko Aho, Executive Vice-President,
Corporate Relations and Responsibility, Nokia**

Digital copyright ecosystem A holistic approach to change



The economic case for reform

Oxera has conducted ground-breaking economic analysis of the impact of the levies in the EU. Looking at the picture with levies today, and what could happen if levies were removed, they found a compelling economic case to reform the copyright levy system in Europe. Oxera's key conclusions include:

- 1. Removing copyright levies would make all stakeholders better off and generate additional **welfare for the EU economy of up to €1,880m per year.**¹**
- 2. From an economic perspective, the copyright levy system is not well suited to the digital age because it creates distortions and inefficiencies affecting consumers, device manufacturers and rights holders. Levies hinder innovation, investment and the development of a European digital market.**
- 3. Rights holders can make significant gains from the removal of copyright levies** because levies hold back the development of new digital services thus limiting the growth of digital music sales and the effective compensation that rights holders can extract. **Oxera calculates that rights holder remuneration could increase by up to €626 million per annum in the EU, should levies be removed.**
- 4. An increased offering of innovative digital services would contribute to the reduction of piracy.**
- 5. Countries with high copyright levies collections have worse performing music industries and do not enjoy greater production of domestic content.**
- 6. Copyright levies reduce the uptake of devices capable of purchasing legal digital music and offering innovative music/content services (e.g. sophisticated smartphones). This reduces potential revenue for content consumption, limits opportunities for new digital services and holds back consumption of new content.**

¹ Oxera, "Is There a Case for Copyright Levies", April 2011 – Oxera's analysis shows that consumers gain economically as they buy devices at lower prices and consume more legal digital music, that manufacturers gain by selling more devices and can more easily engage in new models to distribute music and that rights holders could gain as a more dynamic market could drive growth in legal music sales and the effective compensation of rights holders.

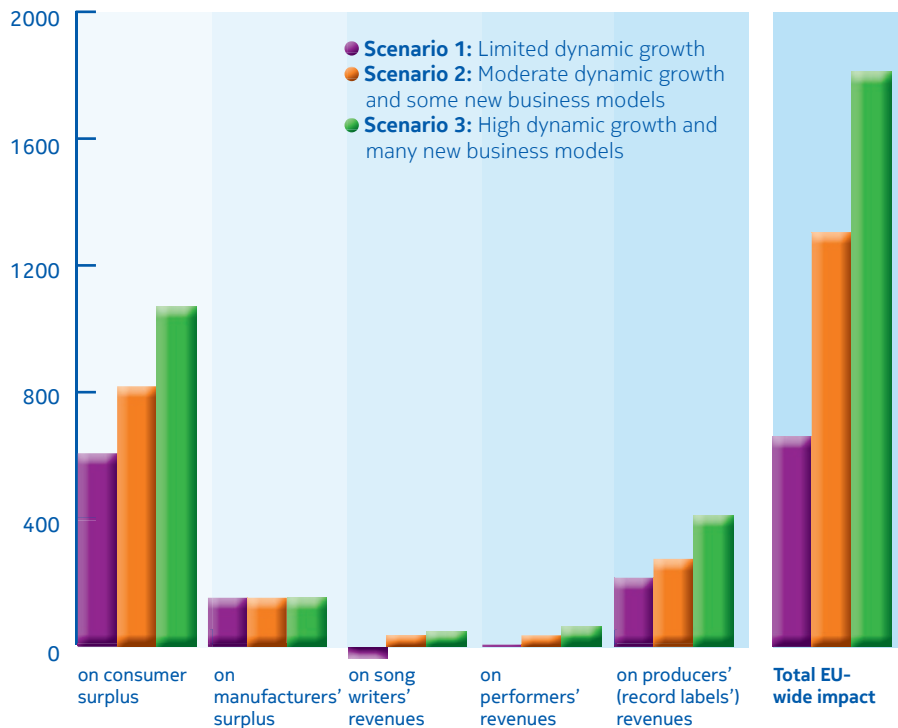
“ Copyright levies on hardware may hurt sales of licensed content, harm new creators and artists, and reduce the incentives to invest in new business models such as subscription models ”

Patrick Legros and Victor Ginsburgh of the Université Libre de Bruxelles



Effect of removing copyright levies

(€m per year)



Source: Osera, "Is There a Case for Copyright Levies", April 2011

Licensing not levies

Licensing revenue is aligned with usage and is a more profitable and fairer way to reward – and encourage – content creation.

A further economic rationale for licensing-based models stems from the usage-based nature of licence income. If rights holders' revenue streams are linked directly to the sales of music, they have stronger incentives to distribute content to as wide an audience as possible. This contrasts with the current copyright levy system where (part of) the income is correlated with sales of hardware, rather than sales of music. Increasingly significant business models such as streaming allow the consumption, without possession, of music.²

Multiple payments for licensed music – the levy system results in some consumers or service providers paying repeatedly. Many music distributors negotiate with rights holders or collecting societies to obtain licences that cover the full scope of the uses made available to consumers. Thus, usage of such files in accordance with the licence should not result in any private copy levies. However, with the co-existence of a levy placed on all devices capable of copying music, consumers end up paying multiple times – even more if they change their devices: which is clearly a disincentive to renew old devices and obtain new functionalities for legal content consumption. Similarly, levies tax consumers who do not copy music on their devices at all or who copy with negligible economic impact.³

² Oxera, "Is There a Case for Copyright Levies", April 2011

³ Oxera, "Is There a Case for Copyright Levies", April 2011

Though their purpose is to compensate copyright holders (creators, artists) for any losses resulting from copying, levies on hardware may reduce sales of licensed content from their potential thereby artificially limiting the size and revenues of the licensed content market.

Additionally, levies may harm new creators or artists while they provide a greater benefit to those who are already established; this is likely to hurt creation.

Copyright levies decrease the incentives to introduce new digital business models (such as subscription models) despite the fact that these may reduce piracy and increase revenues; the higher the levy the greater the disincentive.

The parallel between copyright levies and "Pigouvian Taxes" suggests untargeted levies on a wide range of digital products reduce demand for sophisticated hardware (that also serves as a content consumption platform) thus constraining the potential of digital consumption and therefore rights holder revenues. The negative effects dominate the positive effects. By contrast, levies targeted at media whose main function is copying, may yield a more balanced effect.

Patrick Legros and Victor Ginsburgh
Professors of Economics
ECARES, Université Libre de Bruxelles



Sustaining creation

1. Levies do not support new creation; their withdrawal would not impact the incentive to create – only a small fraction of musicians receive any significant revenues from copyright levies. These are established, rather than new, rights holders whose marginal incentives to produce new audio content are unlikely to be driven by copyright levies. **The available evidence is indicative of a very uneven distribution of income across all creators – where the top 10% of creators account for around 80% of total income, and around 60% of creators collectively earn less than 2% of total income.**⁴

2. Levies may harm new creators and artists seeking to develop their reputation in order to enhance lifetime earnings and who would benefit from a dynamic commercial environment to drive sales, reputation and to “break through”. A remuneration system that includes levies rewards established participants and makes it harder for new creators to break through. The amount of levies paid to new creators is too small to make up for the decrease in sales revenues. Established (successful) creators/artists will rationally seek to maximize revenues no longer needing to build reputation.⁵

Incentives of the levy system⁶

- 1. Copyright levies ‘crowd out’ licensing** – Removal of copyright levies would incentivise rights holders to engage in alternative business models because:
- a. Collecting societies may perceive copyright levies to be a more lucrative and simpler mechanism to generate revenues than licensing and may view licensing as a threat to the generation of revenues from copyright levies. Such decision-making is similar to a monopolist who shelters from innovation that would cannibalize its current rents by investing in preserving barriers to entry. As a result, they may have limited incentives to engage in innovative digital licensing models. This contrasts with licensors that seek to embrace innovation and be amongst the first to license new business models.
 - b. Some collecting societies wish to license digital services only in part. Consequently, collecting societies can attempt to claim additional compensation for the same digital services by means of copyright levies, on the basis that they are not within the scope of the licence. This practice effectively impedes digital licensing and the development of new business models.
- 2. Consumer perception** – consumers may perceive that they are eligible to make private copies due to the levy payment and may prefer “private copying” by acquisition of free content from any sources (legal or illegal) over digital models of music distribution.

⁴ Monopolies and Mergers Commission (1996), ‘Performing Rights’. SABIP (2010), op. cit., p. 64.

⁵ Legros and Ginsburgh, “The Economics of Copyright Levies on Hardware”, April 2011

⁶ Oxera, “Is There a Case for Copyright Levies”, April 2011

Combating piracy

1. An increased offering of innovative digital services would be expected to **contribute to the reduction of piracy**. Even a small reduction in piracy achieved through the new business models would have a significant positive effect on overall remuneration to rights holders, given the size of the illegal 'market'.⁷

2. **There is evidence to suggest that lack of supply is correlated with piracy**; the levies system contributes to lack of online supply and there is little substitution between online content and content distributed physically (on CD or DVD).⁸

Fair and attractive consumer offerings

The consumer perspective

Nokia's own research shows that very few of the major online music services are available in more than a handful of European member states. This snapshot shows that something is impeding the spread of offerings to many markets across Europe. A closer look shows that there is a de facto discrimination against Central and Eastern European consumers who have access to many fewer services and therefore to much less of Europe's cultural richness.

⁷ Oxera, "Is There a Case for Copyright Levies", April 2011

⁸ Legros and Ginsburgh, "The Economics of Copyright Levies on Hardware", April 2011

Innovation and access to technology

Hindering the knowledge economy – Copyright levies may have the effect of raising the prices of electronic devices above the optimal price level. As a result, the quantity of these devices sold may fall below the level that would prevail in the absence of levies thus artificially limiting the take up of new technology in society.⁹

Hindering innovation in advanced technologies – The amount of the levy on a new device is difficult to forecast with an unknown proportion expected to be absorbed by the business. This places a financial strain on the manufacturer and its ability to fund the necessary investment for continuous innovation. This may result in sub-optimal levels of advanced devices brought into the market.

⁹ The device sales may not be at a competitive level even in the absence of levies, depending on firms' market power in various relevant product markets. Thus, the imposition of levies means that prices are distorted further above the competitive level.



Comparison between the European and US digital music markets

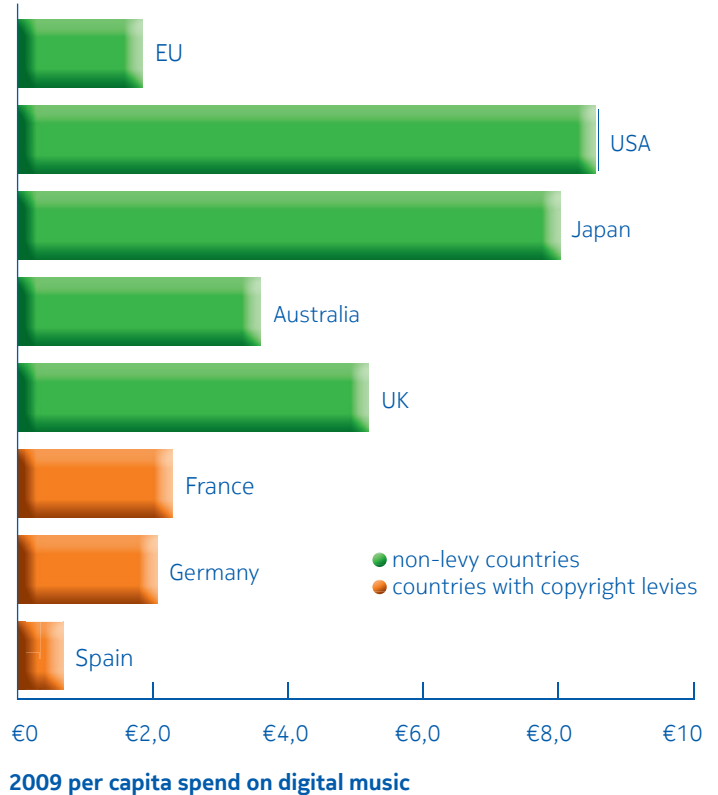
It is highly concerning that the EU, including its wealthiest countries, lags behind the US so significantly. An important indicator of the health of EU market for digital music and for future creation comes from analysis Nokia has prepared based on data from IFPI's 'Recorded Music Industry in Numbers 2009'.

	EU	USA
Amazon (USA)	Available in 4 Member States	Available
Apple iTunes (USA)	Available in 15 Member States	Available
Microsoft Zune (USA)	Available in 5 Member States	Available
Napster (USA)	Available in 2 Member States	Available
Pandora (USA)	Launched and closed	Available
Slacker (USA)	Not launched	Available
Vevo (USA)	Not launched	Available
Yahoo Music (USA)	Launched and closed	Available
Nokia Ovi Music (EU)	Available in 12 Member States	Not Available
Spotify (EU)	Available in 6 Member States	Not Available

	EU	USA	EU as % of USA
Population	501 million	310 million	162
GDP	€12.8 trillion	€11.1 trillion	115
Digital music market	€900 million	€ 2.7 billion	33
Digital share of the recorded music market	13%	43%	30

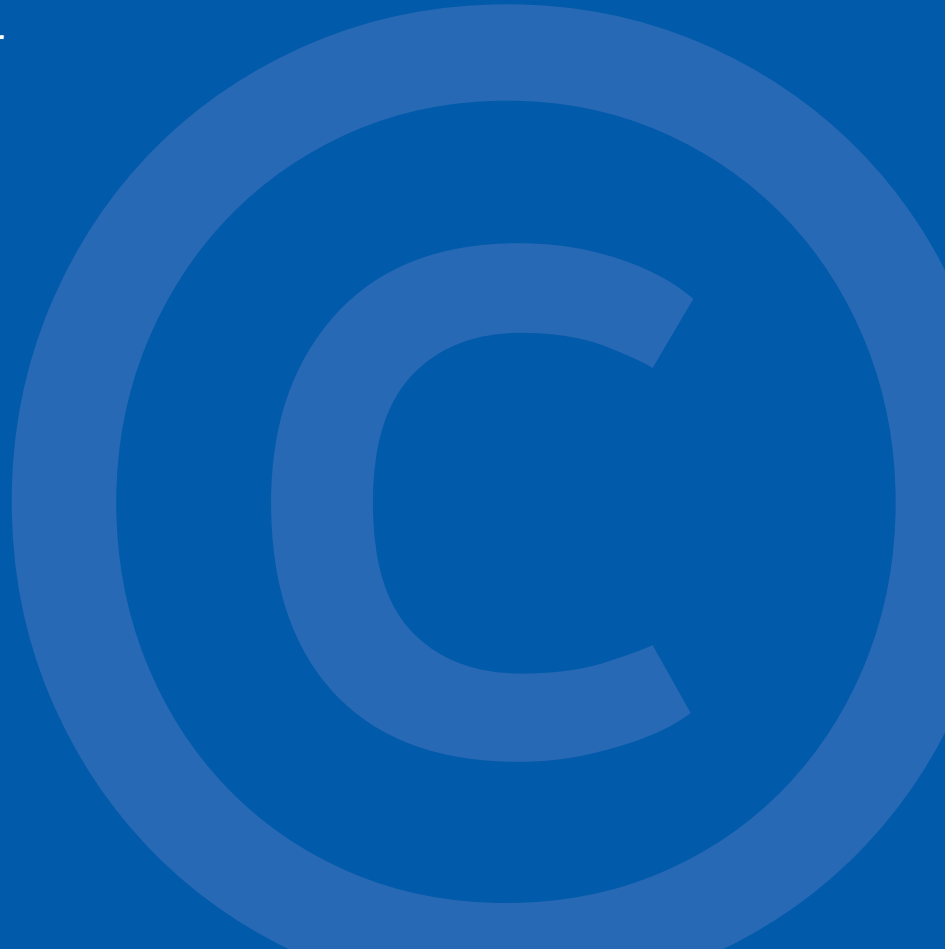
Source: Company websites

Comparison of per capita spend on digital music in key territories



Policy recommendations

1. Phase out **private copy levies for digital products** in favour of **fairer compensation** models which ensure rights holders and creators are properly paid
2. Promote **market-based licensing** as the most effective and fairest alternative to levies



The full length report by Oxera can be found at
www.oxera.com

The full length discussion paper by Patrick Legros and Victor Ginsburgh
from the Université Libre de Bruxelles can be found at
www.ecore.be/discussion_papers.php

NOKIA
Connecting People