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### Copyright Levies

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## Copyright levies

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Copyright levies on recording equipment or blank media exist in many countries to compensate copyright holders for the effects of private copying. In 1965, Germany was the first country to introduce a private copying levy on sound and video recording equipment, following two decisions by the German Federal Supreme Court. The German collecting society GEMA had 'asked the Supreme Court to order that producers of recording equipment be obligated, upon delivery of such recording equipment to wholesalers or retailers, to request from the latter that they communicate the identity of the purchasers to the GEMA' (Hugenholtz et al., 2003, p. 11). The court ruled that this would be a violation of privacy in conflict with the German Constitution. Subsequently, a levy was introduced to compensate copyright holders for the supposedly detrimental effects of copyright infringement using tape recorders.

In the ensuing decades, many countries followed suit and levies were introduced on a variety of recording or copying devices and blank media. At the present day, most countries within the European Union have copyright levies, as well as the United States, Canada, Russia and several countries in Latin America and Africa. In Asia, Japan is the only country with copyright levies (WIPO, 2012, p. 3).

The general idea behind copyright levies is the following. Consumers often make copies for personal use of copyright protected material such as music, films, tv-shows, or books. For instance, they copy a CD to play it in their car or vacation home or to give it to a friend. Or they record a television show to watch it another time. Under strict application of copyright laws, these acts of reproduction would be an infringement. However, strict enforcement in these circumstances would be both too costly and too intrusive vis-à-vis rights of privacy and freedom of expression. Hence, legislators in many jurisdictions have introduced exceptions, which allow various forms of private copying, provided a levy is paid. This levy aims to compensate copyright holders for harm caused by the reduced sales or licensing opportunities as a result of private copying. Levies are collected by a collecting society or some general office and redistributed amongst copyright holders.

This chapter deals with the law and economics of copyright levies. It first discusses the legal framework for private copying, focussing on the European Union, where the bulk of copyright levies are collected. Second, it presents data on the heights of levies and the amount collected in various countries. Third, this chapter analyses the economics of copyright levies. Fourth, it briefly discusses proposals to extend copyright levies to cover unauthorised file sharing over the internet.

### **Legal background in the US and the EU**

In the United States, home video recording was ruled to be non-infringing under the fair use doctrine by the Supreme Court in 1984. Eight years later, in 1992, the Audio Home Recording Act (AHRA) was adopted, which imposed a levy on equipment and media primarily designed to make digital copies of music for personal use (Netanel, 2003). Levies are set by the AHRA at 2 or 3% of the price of devices and media, up to a maximum of \$ 12 (WIPO, 2012). Since the introduction of the AHRA, however,

few new devices or media have been subjected to levies. Devices primarily used for copying audio-visual works, spoken word, software, and databases are exempted. Moreover, CD burners used with computers, blank CDs not specifically sold for music use and most MP3-players were considered computer peripherals and as such were exempted from the levy. As a consequence, the total revenues from levies are very modest at € 2.3 million in 2011 (WIPO, 2012).

The legal issues at stake in the European Union (EU) touch upon all the key economic issues with copyright levies that will be dealt with in the following sections. In the EU, the legal basis for private copies and copyright levies is found in Article 5(2)(b) of the Copyright Directive, also referred to as the *Information Society Directive* or *InfoSoc Directive* (2001/29/EC). It states that:

*'[... M]ember 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 nor 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 to the work or subject-matter concerned.'*

Hence, private copying can be allowed, provided authors receive fair compensation. In recital 35 of the preamble of the Directive, 'the possible harm to the rightholders resulting from the act in question' is proposed as a 'valuable criterion' for fair compensation. However, no payment may be due in case private copying is paid for as part of a licence fee, or if this harm is minimal (*de minimis*).

The concepts of *fair compensation* and *harm* are further explicated in the Padawan decision of the EU Court of Justice, which ruled in 2010 that:

*'the concept of "fair compensation" [...] is an autonomous concept of European Union law which must be interpreted uniformly in all the Member States that have introduced a private copying exception, irrespective of the power conferred on them to determine, within the limits imposed by European Union law and in particular by that directive, the form, detailed arrangements for financing and collection, and the level of that fair compensation.'*  
(EU Court of Justice, 21 October 2010, Article 37).

The Court also ruled that '*fair compensation must 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*' (Ibid., Article 50). Furthermore, it ruled that '*a link is necessary between the application of the levy intended to finance fair compensation with respect to digital reproduction equipment, devices and media and the deemed use of them for the purposes of private copying*' (Ibid., Article 59).

Thus, according to EU Law, levies should be set based on the *harm* caused to copyright holders by the introduction of the private copying exception and should take the actual use of devices and media for private copying into account. Devices and media sold to commercial users and not used for private copying should not be levied. This does, however, still leave much room for many differences between EU Member States, as well as for lawsuits and controversy. In particular, this concerns the definition and calculation of harm, the status of copies from illegal sources and the consequences of use of encryption technology and digital rights management (DRM).

In an attempt to reach more concordance on such issues, EU Commissioner Barnier appointed António Vitorino as a mediator between stakeholders. With respect to private copies 'in the context

of a service that has been licenced by rightholders' (think of iTunes for instance) Vitorino concludes that these 'do not cause any harm that would require additional remuneration in the form of private copying levies' (Vitorino, 2013). In such cases, a levy would lead to double payments. This interpretation of the somewhat enigmatic phrase 'which takes account of the application or non-application of technological measures' in the Copyright Directive was already defended by Hugenholtz et al. (2003).

On the concept of harm, Vitorino proposes

*'to look at the situation which would have occurred had the exception not been in place. In particular, one needs to assess the value that consumers attach to the additional copies of lawfully acquired content that they make for their personal use. It would allow the estimate of losses incurred by rightholders due to lost licensing opportunities ("economic harm"), i.e. the additional payment they would have received for these additional copies if there were no exception.'* (Vitorino, 2013, p. 19-20).

Regrettably, Vitorino's attempt to contribute to more uniformity in the concept of harm seems to run astray, when he equates 'the value that consumers attach to the additional copies', which is in principle the entire consumer surplus of private copies, to 'lost profit' which is forgone producer surplus. Moreover, to 'look at the situation which would have occurred had the exception not been in place' introduces the question whether consumer behaviour would really be much different with or without a private copying exception. The exception was introduced in the first place because enforcement was problematic.

A final issue is the position of copies from *illegal* sources. Only in a few countries – The Netherlands, Russia, Switzerland, and Canada – all copies made for private use fall within the scope of the exception, irrespective of the source (WIPO, 2012, p. 4). This would mean that in all other countries, copies from illegal sources (such as file sharing on torrent networks, newsgroups, social networks or cyber lockers) are no private copies as meant by the private copying exception. It is an important question whether it would nevertheless be lawful to levy for harm caused by copies from illegal sources, even if such copying is itself illegal. Vitorino (2013) seems to imply it is not, when he refers to '*copies of lawfully acquired content*' in the quote above. Preliminary questions on the matter from courts in Denmark and The Netherlands to the EU Court of Justice are pending. In the academic literature, several proposals have been made to extend the reach of copyright levies so as to compensate for downloading from illegal sources. These are briefly discussed in the section 'Levies 2.0' in this chapter.

### **Copyright levies in practice in the EU**

Following the Copyright Directive, 22 out of 27 EU Member States have introduced a levy system.<sup>1</sup> As technology used for consuming and storing music and audio-visual material changes rapidly, so do the devices and media levied. All 22 EU countries that introduced copyright levies, apply these to blank CDs and DVDs. A majority also have levies on memory cards, MP3-players and hard disc DVD-recorders. A number of countries also have levies on external hard drives, PCs, tablet computers and

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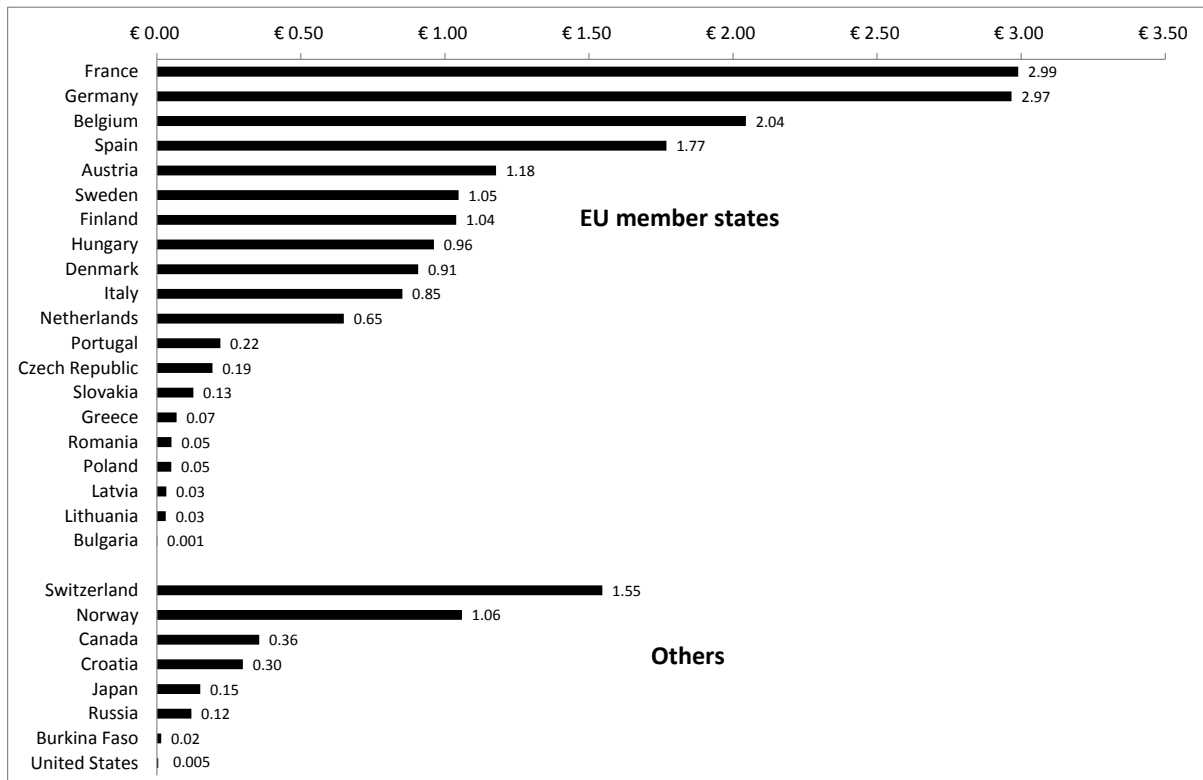
<sup>1</sup> Exceptions are: the UK and Ireland, that so far have not introduced a private copying exception other than for time shifting TV-content; and Malta, Cyprus and Luxembourg, who treated private copying as *de minimis* (Kretschmer, 2011, p. 10).

smartphones. Game consoles are generally exempted (WIPO, 2012), as the Copyright Directive does not apply to software.

There are also massive differences in the heights of levies. For a blank CD for instance, nominal levies range from € 0.009 in Czech Republic to € 0.35 in France. Alternatively, several countries have levies relative to the price of media, ranging from 1.25% in Bulgaria to 6% of in Greece. For devices such as MP3-players, nominal levies often depend on the storage capacity. For a 32 GB player, copyright levies range from € 1.42 in Latvia, to € 22.52 in Hungary. Levies for hard disk DVD-recorders range as high as € 50 in France (WIPO, 2012, p. 13-14).

Figure 1 gives the revenues collected per capita in 2010 in several countries. Revenues per capita range from less than € 0.01 in the United States and Bulgaria to nearly € 3 in France and Germany. For all EU Member States taken together, revenues totalled about € 648 million in 2010 (WIPO, 2012). As a result of rapidly changing technology used for storing and copying content, in combination with a tradition of litigation over the incorporation of new media and devices in levy schemes, revenues tend to vary over time. An upward driver is the rapidly increasing storage capacity of most devices, which implies that revenues based on a fixed amount per MB or GB increase rapidly in time. A downward driver is the dynamic nature of the consumer electronics market. For instance, the use of blank CDs and DVDs has plummeted as they are substituted by USB sticks and memory cards. Likewise, the market for MP3-players is cannibalized by smartphones.

Figure 1: Copyright levies collected in 2010 (€ per capita)



Source: based on WIPO (2012).

Notes: within the EU, no copyright levies exist in Cyprus, Ireland, Luxembourg, Malta and the UK; no data is available for Slovenia and Estonia.

## The economics of copyright levies

### *Types of private copying*

As discussed above, copyright levies are well-established in many jurisdictions, most prominently in the European Union. Nonetheless, the underlying economic rationale is not undisputed. In order to analyse the economics of copyright levies, it is useful first to distinguish various 'types' of private copying that may be different from an economic perspective:<sup>2</sup>

1. Making copies of broadcasted material for *time shifting*; for example storing radio- or TV-content on a recording device to watch it another time and if desired repeatedly.
2. Making '*clone copies*' of or '*format shifting*' CDs, DVDs and media files, or storing streaming audio and video for offline playback (also known as '*stream ripping*' or '*stream capture*').
3. Making clone copies or format shifting to *share* content with members of your *household, family and friends*.
4. Making clone copies or format shifting from media *rented or borrowed* from libraries or commercial renters.
5. Making *backup copies* of content.
6. *Downloading* and storing content from *unauthorised sources* on the Internet (and making ensuing copies thereof).

Typically, private copies of type 1-5 are allowed under the private copying exceptions. However, types 2-5 may be prohibited or restricted by DRM and licence or rental agreements. Downloading from unauthorised sources on the internet (6) is prohibited in most countries.

There are economically relevant differences between all these types of copies. Copies of type 1 and 2 enhance the utility that consumers derive from their legitimate purchase or subscription. It enables them to consume this content at a more convenient time or place, on a more practical device or without carrying discs and devices around. For instance, they can keep a copy of their favourite CDs in their car or vacation home or play them on their computer, smartphone or MP3-player. Time-shifting also enables them to skip advertisements in TV-programmes. Copies of type 3 and 4 are different from the former in that they extend the circle of consumers that derive utility from an original unit of content.<sup>3</sup> Unauthorised downloading (6) resembles the former types, with the notable difference that the extended circle of consumers is anonymous and potentially unlimited. Backup copies (5) do not provide utility directly but act as an insurance against mishaps.

### *Harm and indirect appropriability*

These differences are relevant in light of the *harm* that private copying may cause to copyright holders and the concept of *indirect appropriability*. If copyright levies should be understood as a compensation for harm caused by private copying, as is the case at least according to EU law, it is important to analyse the economics behind this harm more closely.

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<sup>2</sup> A somewhat different typology can be found in Kretschmer (2011, p. 9 & 70), which sums up activities that users may consider private. Kretschmer also mentions user generated content, uploading and online publication, performance and distribution within networks of friends as separate categories. These are ignored here as they are not considered to fall under the private copying exception.

<sup>3</sup> One could also argue that making copies of legally borrowed or rented content (4) is a form of time shifting (beyond the rental period) rather than an extension of the circle of consumers.

A seminal contribution to this issue is by Stan Liebowitz (1985), who studies the effect of photocopying on demand for journals. He finds that ‘publishers can indirectly appropriate revenues from users who do not directly purchase journals and that photocopying has not harmed journal publishers.’ (p. 945). The value consumers (or scholars) derive from copies contributes to the willingness to pay of libraries. Hence, publishers end up selling fewer originals at a higher price, which may even raise profits. If the number of copies per original differs substantially, such ‘indirect appropriability’ depends on the ability to price discriminate: charging a higher price for users that are likely to enable extensive copying while preventing arbitrage. In practice, this is done by a higher price for libraries and a lower price for individuals.

In general, selling fewer originals at a higher price introduces two opposing effects which may lead to both higher and lower profits. This issue was further studied by Besen and Kirby (1989), who model private copying while distinguishing: (1) the extent to which originals and copies are perfect substitutes; and (2) whether private copying has constant or increasing marginal costs. Increasing marginal costs may not only stem from the technology itself, but also from the ‘costs’ of organizing the copying process within sharing groups. Besen and Kirby conclude that the effect of private copying on consumer and producer surplus and total welfare depend strongly on the assumptions about substitutability and the costs of copying.<sup>4</sup> When the marginal costs of copying are *constant*, copies will be distributed at marginal costs and the value of copies cannot be appropriated. The introduction of (relatively cheap) copying technology will then lower the price of originals and profits will decline subsequently. Consumer surplus will increase, while the effect on total welfare is ambiguous. If the marginal costs of copies are *increasing*, copying leads to fewer originals sold at a higher price: indirect appropriability. Besen and Kirby (1989, p. 280) conclude that the effect on welfare will depend on whether or not copying is cheaper than producing originals: ‘in the case where the size of the sharing group is fixed, consumer and producer welfare generally increase when copying is efficient and decline when it is not. When the costs of both originals and copies are low, however, producers will generally lose and consumers will gain from the introduction of copying.’

The scenario of *constant* (near-zero) marginal costs of copying resembles the situation of unauthorised file sharing over the internet (type 6 above), even though such file sharing did not occur when Besen and Kirby wrote their paper. Their analysis implies that indirect appropriability is not feasible in the face of online file sharing. This also follows from the fact that the number of copies generated per original copy sold may differ immensely. Some CDs will not be copied at all, while others will be ripped and uploaded to torrent sites to be seeded to millions of users (Liebowitz and Watt, 2006). This complicates price discrimination.

The scenario of *increasing* marginal costs will apply to offline private copying and may or may not cause harm, depending on the costs and value of copies in comparison to that of originals and the size of sharing groups. Copying may cause no harm at all to copyright holders, but copies may also become competitors to the originals, constraining the price the copyright holder can charge and reducing profits substantially (Varian, 2005).

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<sup>4</sup> Like other models discussed in this section, the models Besen and Kirby develop ignore possible positive dynamic effects of the consumption of copies on future sales (the so-called ‘sampling effect’) and negative effects of lost sales on the future production of content.

Empirical testing of the net effect of private copying on profits is lacking. Surveys carried out in the context of the levy setting process in various countries typically focus on the number of private copies and the self-reported substitution rate (for example Verhue and Hilhorst, 2012; PwC, 2012) and ignore the effect of private copying on the demand for the first original and the complex dynamics of indirect appropriability. It is likely that the net effect will differ for the various types of private copying discussed in the former subsection. As mentioned there, private copies of type 1, 2 and 5 do not extend the circle of consumers that derive utility from an original unit of content. No ‘copying groups’ are formed in which copies become competitors to the original. Some additional sales could be foregone as a result of such copying, for instance when a person would have bought his favourite CD twice to play it at home and in her car, but to the extent that consumers can roughly anticipate their copying behaviour, the option to copy can be priced into the initial purchase. Put differently, the demand curve for originals will reflect the expected utility derived from such private copies. This is an important notion, as it means that in such a case a copyright levy that charges ‘the value that consumers attach to the additional copies’, as Vitorino (2013, p. 19-20) suggests, would lead to double payment.<sup>5</sup>

However, the demand curve will not reflect the utility of *unforeseen* copying possibilities: in the first decade after the introduction of the CD, consumers will not have expected the possibility to make perfect copies of CDs within their home, let alone to rip 500 CDs unto a portable device. Hence, the utility they derive from copying and ripping these CDs will not have been reflected in their initial purchase at the time.

Turning to copies shared within one’s household, and with family and friends (type 3), the models of Besen and Kirby (1989) and Varian (2005) are more likely to apply, and private copying might be harmful to copyright holders even though some of the additional utility can be appropriated indirectly. This is partly due to the fact that the size of such copying groups is variable and price discrimination according to group size is not possible. The utility of copies of type 4 could in theory be appropriated indirectly by setting the appropriate rental prices, unless restrictions put on the rental price from a public service perspective prohibit doing so.

To summarize, the utility downloaders derive from unauthorised file sharing cannot be priced into the initial purchase. For other types of private copying, these benefits can to some extent be appropriated by using smart pricing, depending on the cost structures. For time shifting, format shifting and clone copying for personal use, this is likely to be the case. However, for copies passed on to family and friends (type 3) this may not be sufficiently possible and harm from such private copies may well occur.

### *The application of DRM*

Koelman (2005) points out that DRM technology increases the opportunities copyright holders have to appropriate the additional utility derived from private copying. This is in line with remarks in the Copyright Directive on the ‘application or non-application of technological measures’ and Vitorino’s (2013) recommendation that licenced copies do not require additional remuneration by a levy.

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<sup>5</sup> Time shifting of TV-content is a somewhat different issue: advertisers will be aware that some of their ads will be skipped when consumer watch programmes they recorded. This will lower advertising revenues for channels, while increasing the willingness to pay consumers have for receiving TV-channels and for recorders.



However, the distinction between the 'application or non-application of technological measures' is not as binary as it may seem at first glance. DRM exists in many forms, ranging from fingerprinting or watermarking (also known as social DRM) to advanced encryption. DRM can also be used to limit the distribution of private copies among family and friends. Yet, the experience so far suggests that DRM will not eradicate all unlicensed copying. The technical and privacy issues that make strict enforcement problematic and give rise to copyright levies in the first place, have not disappeared with the introduction of DRM.

At the same time, now that various kinds of DRM are available to give copyright holders at least a firmer grip on copying and more opportunities for price discrimination and indirect appropriation, the decision *not* to apply DRM should also be considered. When consumers started copying and sharing CDs on a large scale, for instance, record labels introduced DRM on CDs, and until 2007, all digital music files bought from Apple's iTunes store also contained DRM technology. However, consumers did not appreciate the way in which DRM got in the way of supposedly legitimate uses. For instance, DRM sometimes caused computers to crash, which was a nuisance to people trying to play an audio CD with their computer, even without trying to copy it. Also, the use of DRM prevented consumers from format shifting, such as ripping their own CD collection onto their MP3-player.

Thus, the use of DRM may create a disutility for consumers and have a negative effect on demand for originals. For example, consumers who only play music from a hard drive or on their phone may stop buying CDs if DRM prohibits them to rip these. DRM may even cause consumers to revert to DRM-free content from illegal sources (Sinha et al., 2010; Vernik et al., 2011). Over the last few years, the music industry moved away from using DRM. From an economic point of view, this should be a rational choice. Indeed, Sinha et al. (2010) find that 'the music industry can benefit from removing DRM' and that 'a DRM-free environment enhances both consumer and producer welfare by increasing the demand for legitimate products as well as consumers' willingness to pay for these products.' (2010, p. 40). Therefore, the choice *not* to use DRM should be perceived as a rational choice in the spectrum ranging from more to less restrictive DRM technologies that are currently available. Now that right holders have these options, it makes no longer sense for copyright levies to draw a sharp line between the application and non-application of DRM as the Copyright Directive seems to suggest. The choice not to use DRM should not entitle copyright holders any more to compensation than the choice to use restrictive DRM. Hugenholtz *et al.* (2003, p.4) seem to find legal basis for this argument, proposing that 'levies are to be phased out not in function of actual use, but of availability of technical measures on the market place.'

Finally, harm from private copying cannot be equated to harm caused by the possible introduction of a private copying exception to copyright. As pointed out in the preceding paragraphs, consumers' private copying behaviour is to a large extent independent of its legal status, since enforcement is problematic. Private copying occurs without a private copying exception. Much of any harm from private copying would thus not be the *result* of such an exception. This implies that the suggestion, both in the Padawan-ruling and by Vitorino, to base compensation on the harm caused by the introduction of the private copying exception, could leave copyright holders empty-handed.

### *Other grounds for a levy than the compensation of harm*

Although the concept of 'harm' is central to the legal foundations of copyright levies, harm is by itself no sufficient economic argument to introduce a levy. Kretschmer (2011, p. 59-66) reviews several alternative arguments.

The *transactions costs* of individual licensing are often mentioned as an economic rationale for a private copying exception. However, DRM technology has made it easier to control individual copying behaviour than was conceivable twenty years ago. More importantly, transactions costs may be an argument for an exception, but not necessarily for compensation. As Kretschmer (2011, p. 60) points out: 'If the current parameters of copyright law ignore "economic efficiency" (i.e. if copyright law under-protects or over-protects), the transaction cost approach does not fly, as we are minimizing transaction costs towards a sub-optimal outcome.'

Another argument could lie in the extra value that devices derive from copying content. Considering that the costs of filling a 32 GB MP3-player with digitally bought MP3 files are to the tune of a few thousands of euros, it is unlikely that many people would buy one if private copying were not possible. If copyright holders are not rewarded for this, they do not receive efficient incentives to create content. However, such arguments could in theory be applied to all sorts of complementary goods and generally are no cause for intervention. Effects are often bi-directional: an MP3-player enhances the utility of CDs and vice versa and it is debatable if any compensation would enhance welfare.

A third argument understands levies as a 'tax' used to support the supply of content, which has characteristics of a public good. Like any tax, however, levies reduce demand for copies and related goods and services by increasing their price (Lunney, 2001; Fisher III, 2004; Koelman, 2005; Towse, 2008). It may even reduce the incentives to introduce new copying technologies somewhat (Lunney, 2001). On the other hand, any tax system suffers from the fact that it will reduce demand for taxed product and services or reduce production. In fact, this effect may be smaller for a copyright levy than for a general tax such as VAT (Netanel, 2003).

### *Other economic concerns with levies*

Apart from the debate about the harm caused by private copying, most other concerns with levies expressed in the literature have to do with the bluntness of the levy instrument. 'Rough justice' is a term often used in the context of levy systems, which means that a levy system will never be able to make exactly the right people pay levies and the right creators receive them. The last subsection already mentioned the losses resulting from the fact that levies will be fairly uniform, which implies consumers who make many private copies will be cross-subsidized by consumers who make very few copies or no copies at all. On the other hand, it should be noted that the Padawan-decision exempts professional use from levy systems, which is a step into the right direction.

Likewise, the distribution of levy revenues to creators will be 'rough', which implies creators receive imperfect price signals about the market valuation of works (Towse, 2008). In addition, the administrative costs of levy systems are stressed by some (Koelman, 2005).

## Levies 2.0

As mentioned above, downloading and storing content from unauthorised sources (private copies of type 6) is generally not allowed under private copying exceptions. However, since the rise of peer-to-peer file sharing, several academic authors have proposed to introduce some 'statutory licensing scheme' with a levy system to compensate for this practice (Ku, 2002; Netanel, 2003; Fisher III, 2004; Litman, 2004; Gratz, 2004; Oksanen and Valimaki, 2005).<sup>6</sup> Such proposals are also known as for instance 'content flat rate' or 'alternative compensation scheme'.

The logic behind the introduction of a levy on such behaviour is similar to that of 'classical' levies. In return for a levy of 2 to 5 per cent on broadband access and/or computer equipment, consumers could be allowed to engage in non-commercial file sharing and creative re-use while copyright holders are compensated for the harm done. Proposals differ in what the levy should cover (music, audiovisual material, books), whether it should be mandatory for consumers and for copyright holders, and in the way the revenues should be redistributed among right holders. Monitoring P2P-traffic for that purpose (Ku, 2002; Netanel, 2003) would seem a reasonable option. However, such a system has privacy issues and could be manipulated. Besides, it would favour less popular content as it would only count downloads and multiple playback would not be rewarded (Fisher III, 2004). Fisher III (2004) suggests sampling content consumption by consumers, while Gratz (2004) proposes to use the number of peers making content available for download, and Oksanen and Valimaki (2005) argue for voting systems to democratize remuneration and involve consumers.

So far, organizations of copyright holders have not been very enthusiastic about any of these proposals. A general drawback is that such a scheme would promote file sharing, destroying what is left of the current business based on physical formats, and wiping out promising new digital models, such as iTunes, Spotify, Deezer, Netflix and the like. Indeed, as the content industry often stresses, it is hard to compete with free, but it would be even harder to compete with free when it is legalised and consumers have paid for it in advance.

## Concluding remarks

Historically, copyright levies have been introduced to compensate right holders for the harm caused by private copying. However, economic analysis has shown that the utility consumers derive from offline private copies can to a large extent be appropriated indirectly. Hence, the harm caused by private copying will be substantially smaller than the utility consumers derive from private copies or even the sales forgone by such copying. For private copies that do not lead to a proliferation of content – for example time shifting, format shifting and backup copies – there may be no harm at all, provided consumers are aware of these copying possibilities at the time of their initial purchase.

DRM and innovative pricing schemes have improved the possibilities for copyright holders to appropriate the value of private copies. Therefore, charging levies for copies that are licenced by right holders would lead to double payment. Moreover, the choice *not* to apply DRM is nowadays a rational choice that from an economic perspective should not be treated differently from the choice to apply DRM. Altogether, the case for levies to compensate for harm caused by 'classical' private copies is gradually diminishing.

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<sup>6</sup> For an extensive analysis of this literature, see also Quintais (2013).

The argument of indirect appropriability does not apply to unauthorised online file sharing, as there is no relation between the uploader and the downloader and the number of copies made from an original will vary dramatically. It is an open question pending at the EU Court of Justice whether EU legislation allows levies to account for the harm caused by these copies, even if they are deemed illegal. If so, copyright levies will continue to have a sound legal basis within the EU. If not, they might still have a future as 'levies 2.0' in combination with a statutory licensing scheme.

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### Further reading

Hugenholtz et al. (2003) provides a good overview and analysis of the legal and policy background of copyright levies focusing on the EU up until that time. A more recent and factual overview is provided by WIPO (2012). For a thorough analysis of the various proposals for alternative compensation schemes, see Quintais (2013).