Forum

The PSA enquiry into musical recording prices

Professor Alan Fels and Dr Jill Walker of the Price Surveillance Authority defend its findings

The Prices Surveillance Authority's 1990 inquiry into the Prices of Sound Recordings was initiated following complaints regarding the high prices of records in Australia compared with overseas.

The terms of reference were wide, including consideration of competition, efficiency, new technology, profitability, employment, the development of Australian music, copyright and piracy.

Why prices are high

After examining a large volume of price information provided by the industry and covering many countries, the Authority concluded that the price of records in Australia was too high and that they had been maintained at consistently and significantly higher levels than in most overseas countries for at least a decade. Examples of the discrepancies observed were CD prices 42 per cent higher than in the USA, cassette prices 64 per cent higher than in Canada and LP prices 21 per cent higher than in the UK. The extent of the discrepancies are much greater once figures are adjusted for differences in the sales tax component.

The Authority concluded that the source of the high prices lay in a combination of the importation provisions attached to the *Copyright Act 1968*, relatively price inelastic demand compared to other countries and an absence of price competition between record companies. The importation provisions provide copyright holders, effectively record companies, with the exclusive right to import records into Australia, preventing competition from 'parallel importers' reducing prices to internationally competitive levels.

Costs of manufacturing and distribution in Australia are not excessive. Record companies choose to manufacture here because it is competitive, both in terms of cost and timeliness.

The Authority recommended the repeal of the importation provisions of the *Copyright Act*, sections 37, 38, 102 and 103, as they relate to parallel imports from countries which enforce adequate copyright protection over record reproduction. The Authority does not consider the provisions to be a part of copyright protection, but rather an attachment to the *Copyright Act* which has nothing to do with correcting the market failures addressed by copyright protection.

Copyright protection is designed to prevent free-riding on intellectual property, thereby increasing the returns to copyright owners and increasing investment in intellectual property. If people can copy records, perform songs and so on without remuneration being paid to the owner of the asset which they are utilising, there may be insufficient investment in those assets relative to the true level of demand. Import protection against pirate records is a necessary adjunct to this protection, since free importation of pirate records would undermine the reproduction right. No such argument, however, applies to protection against parallel importation. There is no market failure in the distribution of records, it is simply a restriction on free trade and competition. It does not even protect domestic manufacturing, it simply gives exclusive rights over importation. Opening the market to competition will force local record companies to reduce their prices or lose market share to parallel importers.

Piracy

Piracy will not get any worse as a consequence of opening the market. There are currently no provisions to stop pirate imports passing through customs and there is no reason to believe piracy would be more prevalent once the market was open to parallel imports.

The Authority did agree that piracy is a problem facing the industry now and in the past. It therefore recommended a number of measures to help combat piracy: to allow customs intervention, to increase the chances of conviction and to increase fines for convicted pirates.

It was claimed that the high returns from overseas artists provided the funds to invest in unprofitable and/or high risk Australian artists. The Authority did not accept these claims. It is true that many recordings will not cover their costs from domestic market returns. The aim is to recover costs from international sales, if not on the first record then later as the artist's career builds. Since international sales are the key to profitability, domestic prices will have little effect on returns.

Record companies will continue to invest in Australian artists because consumers want to buy their records, not only consumers in Australia, but consumers around the world. The only question is whether Australian consumers should have to pay more to buy a Peter Garrett record than consumers overseas.

The Inquiry also found that artists were at a disadvantage when dealing with record companies. Most Australian artists do not actually earn any royalties from their recordings. The cost of the recording is recouped by the record company from those royalty earnings. Unlike composers and the 'maker' of the recording (generally the record company), artists do not own a copyright in their performance which has been recorded.

The Authority took the view that the logic for granting performers a copyright was as compelling as the provision of copyright to authors and composers and urged the Government to reconsider the case for such a copyright. It would give artists an important bargaining tool and/or statutory rights of remuneration in relation to the use of the recording; for example, a share of the blank tape levy.

Most Australian artists do not currently earn a living from their work. They would benefit from lower prices, increasing record sales, an interest in live music and from the protection of their performers' copyright.

Some high profile artists fear that an open market will undermine that income by letting in overseas versions of their records on which royalties may not yet be recouped and/or allowing deletions from failed overseas releases to enter Australia. While recognising these fears, the Authority believes only a minority of successful artists are affected, that the fears are exaggerated and that contractual changes could overcome the problems. As long as local record companies reduce their prices to meet the competition provided by parallel importers, the first problem will not arise. Deletions only occur where a record has failed and in most cases a failure overseas will also be a failure in Australia. However, in some cases local artists may be a success here but fail overseas. A number of contractual proposals have been suggested which would protect artists from the impact of deletions; buy-back clauses or up-front royalty payments would both be feasible to negotiate with overseas record companies.

Carlos Suarez, of Regular Records, discusses the Australian Independent record companies' view of the PSA report

The PSA's recommendation to allow parallel importing is premised on the assumption that control over distribution conflicts with the operation of a competitive market by cutting out import competition. The effects of such proposals would be deleterious for independents, who by their very nature specialise in developing local artists.

Competition v Incentive

The PSA stated that sections 102 and 103 have adverse competitive effects "with no obvious benefits". Given Professor Fels' recent chairmanship of the Trade Practices Commission, it is indeed surprising that he omitted to bring to the media's attention a recent TPC Background Paper which states that "the grant of exclusive rights under the various intellectual property regimes generally has only a limited effect on competition" and that "whilst some conflict arises in the short term because competitive conduct is restricted by the exclusive rights granted, the objective of granting the exclusive rights is to foster innovation and therefore competition in the longer term." Further, and perhaps more importantly, Professor Fels has pushed for parallel importing without a balanced analysis of the competing interests of copyright law and competition policy which informs this debate. While copyright grants exclusive rights to its owners, which is prima facie anti-competitive, it also has its economic rationale to protect and encourage the investment of capital. Clearly, the task is to balance the scope of the copyright protection as against competition policy so as to provide maximum benefits to the community. Not only has Professor Fels examined the competition side of the equation from the limited perspective of prices, he totally ignored the other side of the equation, namely the benefits to the industry and the community that flow from the present arrangements under the *Copyright Act*.

The level of copyright protection, as presently embodied in the Act, is in proportion to the risk taken by the investor. Because of the very high risks involved in picking commercial 'winners', exclusivity of rights is necessary to reflect the commercial risks taken – conside that only about one out of every seven albums will ever return a profit. Exclusivity is the economic rationale upon which independents will invest in raw and untried talent. Any attempts to fiddle with the Act will inevitably increase the risk ratios and thereby decrease the confidence to invest.

Why would an independent company want to spend on average $100,000.00 recording an unknown band with two supporting videos totalling at least $50,000.00, if the risk ratio is further increased by having to compete with imports in the territory for which that company has promoted and marketed the recording? Either investment in local bands will drop off, with adverse long term cultural effects, or only those bands that fit into an extremely tight set of 'Top 40' requirements, will have money invested in them. Australia's niche in the world music market lies with its ability to foster a peculiarly Australian sound that is recognised by record executives all over the world. The independent company Powderworks, which invested in Midnight Oil as an unknown band, might not today commit the same funds if they knew that the law would fail to respect their intellectual property rights – especially when it took that band until its sixth album to break even. Such a scenario would mean that we could lose that specialised niche in the long term, and with it, a cultural tradition.

Deletions

While Professor Fels has dismissed the incidence of cut-outs and deletions coming into the country, it is a fact that 95 per cent of Australian acts are unsuccessful overseas. When an artist is popular in Australia, yet the album fails in the USA, the excess production of stock is 'deleted' and sold to discount wholesalers in the USA. These wholesalers are then able to sell the product back into Australia. However, Australian artists and their record companies do not receive any royalties on the sale of such deleted albums. The benefits go to the US wholesaler and the Australian importer.

The PSA believes that protection against piracy is totally distinct from protection against parallel imports. This is nonsense as it is impossible to detect at the dockyards whether a shipment of CDs contains pirated or non-pirated copies – they both look the same. By the PSA's own admission, "the chances of border detection of pirate records is zero, since section 135 (of the *Copyright Act*) only applies to printed copies of works."

The PSA's option to retain the importation right over imports from non-Berne convention countries with sub-standard copyright protection, ignores the reality that some signatory countries such as Thailand and The Philippines, while having normal copyright protection, are major pirate markets.

The proposed decrease in copyright protection would place Australian independents at a disadvantage to most of our trading partners who all have prohibitions against parallel imports. Why destroy a healthy export producing industry ($90 million per year) that has succeeded without government assistance?

The PSA's position would also be at odds with the GATT's Uruguay Round negotiations which has sought to bolster intellectual property rights. Professor Fels has stated in the media that importation provisions are essentially non tariff barriers to trade which run counter to the spirit of the GATT. Import provisions are however a normal part of intellectual property rights used by the most of our trading partners. While such rights give rise to a 'monopoly' due to their legal nature, they are not a form of import protection per se.

Professor Fels

Phil Dwyer reviews the PSA recommendations from the Musicians Union perspective

The Prices Surveillance Authority inquiry into the price of records is principally concerned about prices. However, the scope of the inquiry was broad and the real contention involved the parallel import provisions of the *Copyright Act*. These provisions restrict the importation into Australia of legally sourced records without the approval of the copyright owners.

Throughout the inquiry the 'industry' seemed to speak with one voice. The major and independent Australian companies were represented by The Australian Record Industry Association (ARIA). The collecting societies including The Australian Performing Rights Association (APRA), The Australian Mechanical Copyright Owners' Society (AMCOS) and The Phonographic Performance Company of Australia (PPCA) supported the ARIA position. The 'industry bodies' such as AUSMUSIC and, surprisingly, Export Music Australia all supported the ARIA position. That position was that, if the parallel import provisions were removed, the industry would collapse.

The opposing view was put by consumer organisations. They argued that the provisions were used to insulate the Australian market from competition and to sustain artificial prices of records.

The ACTU became involved in the inquiry and made a joint submission with the Musicians Union and Actors Equity. That submission recognised an obligation to consumers and, at the same time, detailed a package for the reform of the industry to redress the imbalance between the record companies, publishers/composers on the one hand and artists and performers on the other. The principal recommendation was that a performer's copyright should be created.

ARIA argued that if the provisions were removed Australia would be flooded by pirate tapes and CDs. However, the provisions relate to legally sourced product and have no relevance to illegally sourced pirate records. Submissions were made by the ACTU to strengthen the piracy provisions by increasing penalties and by placing the onus on the retailer to establish that the product sold was legally sourced. These submissions were not supported by ARIA.

Finally, there was an attempt to draw artists into the debate by the suggestion that there would be insufficient capital left in the industry to fund the recording of local artists if the provisions were removed. The ACTU argued that investment in the industry was commercial and not charitable in nature. Record companies take risks when they invest money. This is done for commercial reasons. Likewise artists take risks when they contract their exclusive services to record companies. There is not, and never has been, any concept of subsidy in the contemporary music industry. For every $50.00 spent by the Australian consumer, 10 cents finds its way to an Australian artist. This is hardly an effective method of subsidy.

Artists' income

There was a suggestion that artists, given that their contractual entitlements are often calculated as a percentage of the recommended retail sales price of records, would suffer a decrease in income if the retail price was reduced. This argument ignored that fact that if the price of records is reduced, then the volume of sales may well increase. Further, only about 5 per cent of artists are contracted and of that 5 per cent only one in ten is 'recouped'. It is customary to recoup all recording and video production costs against the artist's entitlement to royalties. Very few artists sell enough records to recoup.

Throughout 1991 there has been an attempt by those opposing the PSA's recommendations to win the support of artists by suggesting that if an Australian artist is successful in Australia but fails overseas, then the copyright owners will take steps to facilitate the dumping of that product into Australia. It may be solved by giving Australian performers the right to veto the importation of their works into Australia.

The argument that is now being put by ARIA is that they require existing profit margins to enable them to continue to invest in the local industry. If those margins are not maintained they will withdraw and treat Australia simply as a market for product. This is precisely the situation that existed in Australia fifteen to twenty years ago. Even today 75 per cent of product sold is foreign. However, Australia has developed as a significant *source* of product. Men At Work are said to have generated in excess of $100 million from a total investment of less than $100,000. Local content rules guarantee airplay for local product. If the major record companies do not invest in local product then their parent companies and/or someone else will.

This inquiry was not about copyright. It was about money. It was about the redistribution of income from record companies to consumers, artists and performers. Unless and until ARIA addresses the price issue in a structural way their position both publicly and privately will continue to be untenable.