

THE MARKET FOR BOOKS AND THE IMPORTATION PROVISIONS OF THE COPYRIGHT ACT 1968

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1. Introduction

A case study of the interconnection between law and economics has been played out in the arena of Australian public policy-making over the past three years. It concerns the market for books and the importation provisions of the Copyright Act 1968 (Cth). The Copyright Law Review Committee examined the moral and legal issues of copyright owners' private property rights versus public rights of access, but did not address the economics of the market for books.¹ The Prices Surveillance Authority took an economic view of the issue and argued that the economics of the situation rather than unresolvable moral issues should underpin the law.² The Authority's report was followed by a vast amount of public debate, mostly carried out in the pages of the daily press, where economic arguments were confronted with moral outrage. Cabinet's final decision, incorporated in a Bill recently introduced into Parliament, was a compromise between the two approaches.³

2. The Importation Provisions

The Copyright Act (Cth) ss. 37, 38, 102 and 103 makes it illegal to import and distribute copyright articles, including books, into Australia for purposes of trade without the licence of the Australian copyright owner, where their manufacture in Australia by the importer would have constituted an infringement of copyright. Direct imports by individuals and libraries are not illegal as they are not for purposes of trade. Pirate and parallel imports are treated identically. Parallel imports are here defined as those manufactured under copyright protection overseas but imported by persons other than the Australian copyright holder.⁴ This means, in short, that booksellers cannot directly import books from overseas even though the books have been produced with the authors' consent and may be on sale there more cheaply and earlier, including in paperback form,

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¹ Copyright Law Review Committee, *The Importation Provisions of the Copyright Act 1968* (1988).

² Prices Surveillance Authority, *Inquiry into Book Prices Interim Report* (1989) and *Inquiry into Book Prices Final Report* (1989).

³ News Release by Lionel Bowen, Attorney General, 21 December 1989; A Bill for An Act to amend the Copyright Act 1968 (Cth) in the House of Representatives 17 October 1990.

⁴ Other definitions of parallel imports may include goods manufactured in countries without copyright protection, which although not illegal in the country of manufacture are not produced with the permission of the author (or maker in the case of subject matter other than works).

than in Australia. The Act applies equally to all types of copyright products: books, records, films and videos and computer software.

Copyright legislation did not always provide protection against parallel imports. Early legislation only provided protection for works published domestically and importation provisions provided protection against pirate editions published overseas. The British Copyright Act, 1842, 5 & 6 Vict., allowed the free importation of books into Australia. Under this nineteenth century 'open market' Australian booksellers and wholesalers imported directly from overseas, principally from London but also from America.⁵ They established buying offices in London which obtained books at source with the highest possible discounts; such that Australian retailers were able to sell books at the published British price.

The Berne Convention 1886 committed each signatory country to providing copyright protection for works published in all other signatory countries. With the internationalization of copyright protection, the notion of the territorial divisibility of copyright developed. The 'British Publishers' Traditional Market Agreement' was first established in 1899, under which British and American publishers agreed to split the world's markets for English language books, whereby British publishers acquired the copyright for the countries of the British empire and former empire and American publishers acquired the copyright for the United States and its dependencies. Territorially specific reproduction rights were made more valuable by restrictions on the importation of parallel imports as well as pirate imports. Territorial copyright was embodied in the British Copyright Act, 1911, 1 & 2 Geo. 5, adopted in Australia by virtue of the Copyright Act 1912 (Cth).

The combination of the Traditional Market Agreement and the 1911 Act provided the basis for the demise of the Australian entrepreneurial booksellers and importers who were replaced by the Australian agents and offices of British publishers, who came to dominate the supply of books to Australia.⁶ In 1974 the traditional market agreement was the subject of anti-trust action in the United States, settled by a consent decree prohibiting American publishers from engaging in such market allocations.⁷ However, despite the formal ending of the agreement, British publishers continue to dominate the supply of books to the Australian market. Those with major interests have set up Australian subsidiaries while others appoint an exclusive distributor.

The Copyright Act 1968 (Cth) provides stronger protection against parallel importation than did the 1911 Act. The latter did not specify the hypothetical manufacturer of the imported goods. Section 2(2) of the 1911 Act provided that copyright was infringed if a work was imported for sale or hire where it 'would infringe copyright if it had been made within the part of His Majesty's dominions in or into which . . . importation took place.' Hence, if the imported product was

⁵ Kirsop, W., 'Bookselling and publishing in the nineteenth century' in Borchardt, D. H. and Kirsop, W. (eds) *The Book in Australia* (1986) 16.

⁶ *Ibid.*

⁷ *U.S. v. Addison-Wesley Publishing Co. & Ors.* Decree issued 24 November 1976, (1977) Trade Regulation Reports 70640.

made overseas by the owner of the Australian copyright, such imports could be interpreted as legal.⁸ In the case of books, the Australian copyright holder was usually a British publisher, who generally imported the British edition for sale in Australia. The wording of the 1911 Act was interpreted as allowing booksellers in Australia to directly import this same edition but not to import the alternative American edition. Hence 'buying around' by Australian booksellers continued despite the establishment of British publishers in Australia. Following the recommendations of the Spicer Committee,⁹ the 1968 Act specified the hypothetical manufacturer as the importer, making such imports by booksellers illegal and completing the establishment of a 'closed market' in Australia.

3. *Copyright: Moral and Economic Issues*

Copyright has long been characterized by two alternative rationales; moral rights *versus* economic rights. The two positions are most sharply distinguished in the approach and legislation of continental countries such as France, Switzerland and Germany which emphasize the moral rights of authors and the approach of the United States which concentrates exclusively on economic rights. Although the moral rights of authors, their just rewards and their contribution to society are often invoked as the reasons behind copyright legislation in Australia, its origins in British legislation clearly lie in the protection of the publishing industry.¹⁰

Copyright legislation creates a property right in the product of intellectual labour by providing its owner with a series of rights over the use of that work. From a moral perspective this is viewed as the author's right to do as they wish with the product of their labour and to control its use by others. These *rights* may be counter-balanced from a moral perspective by *obligations*. For example, protection from importation may involve a responsibility to make the work available to the public in that country. Resolving the moral question of where to draw the legal lines on rights and obligations, however, is a very difficult one; authors proclaim their 'absolute and inalienable' right to control the use of their intellectual product, while consumers proclaim their right to access the latest developments in cultural and scientific thought. Similar issues of rights and obligations occur with other forms of property rights, *e.g.* the rights of land owners to use their land as they wish *versus* their obligation not to visually or chemically pollute their neighbours and the rights of patent owners to the exclusive use of their invention *versus* the right of society to benefit from that invention.

One of the most useful contributions of the economic approach to the study of law is that it provides a framework which helps to enable the resolution of conflicts in moral rights and obligations. Thus, the economic analysis of

⁸ Similar provisions in United Kingdom and New Zealand legislation have been the subject of different judicial interpretation, see Copyright Law Review Committee, *The Importation Provisions of the Copyright Act 1968* (1988), Appendix D.

⁹ *Report of the Copyright Law Review Committee* (1959).

¹⁰ Copyright Law Review Committee, *The Importation Provisions of the Copyright Act 1968* (1988), Appendix D.

copyright cuts across the moral dilemmas above and examines the costs and benefits of various degrees and forms of copyright protection.¹¹ This is a specific application of the economic theory of property rights. The optimal nature and extent of any particular property right will be that which in a utilitarian sense maximizes the economic welfare of society as a whole. While a legal approach to property rights based on moral issues might suggest an identical balance of rights and obligations for all types of property, this does not follow from an economic approach. Thus the optimal balance of rights for land owners differs from those for patent owners or copyright owners. To some extent these differences are reflected in Australian legislation. However, all forms of copyright work (books, records, films and videos, computer software *etc.*) currently enjoy very similar property rights, which may not be economically optimal.

A free competitive market tends to equate the cost of producing a good with the price an individual consumer is prepared to pay, which also tends to maximize the utility derived from society's resources. Intellectual products are an example of what economists term 'market failure', where a free competitive market does not produce this optimal allocation of resources. These products have several distinguishing (and distinct) characteristics: they suffer from problems of 'non-exclusivity'; they are 'public goods'; they may give rise to 'cultural externalities and/or they may be characterized as 'merit goods'.

'Non-exclusivity' occurs where producers or consumers cannot be excluded from enjoying the benefits of someone else's labours without payment; this is known as the 'free-rider' effect. Free riding may occur in a wide variety of circumstances, *e.g.* firms may free ride on other firms investment in after sales service or advertising; consumers may free ride on the provision of television or radio broadcasts or their neighbour's provision of an attractive garden. In the case of books, copiers can reproduce books without paying for their origination costs, free riding on someone else's investment. Their lack of payment means that the private returns from investment in writing books would not fully reflect the actual benefits received by society, and hence there is a tendency to under-investment.

A 'public good' is not necessarily produced by the public sector (although that is often a solution) but is rather a product or service which is characterized by a lack of 'opportunity costs' in consumption; that is one person's consumption does not detract from another person's consumption of the same product or service. Examples of public goods are lighthouses, television and radio broadcasts. The intellectual (as opposed to physical) content of books also shares these characteristics. In the case of public goods, utility is maximized when the cost of production is equated with the *sum* of the various prices consumers are prepared to pay; thus a competitive market tends to result in too few public goods being produced.

Apart from the technical externalities associated with the free-rider problem, it

¹¹ Landes, W.M. and Posner, R.A., 'An Economic Analysis of Copyright Law' (1989) 18 *Journal of Legal Studies* 325.

may be argued that individual welfare is raised through 'cultural externalities' generated by the production and consumption of some books. Alternatively, books may be characterized as 'merit goods'¹² which have a value to the community over and above any value to individuals. Hence Donald Horne has referred to a 'market of ideas'.¹³ A free market may fail to mediate these benefits and hence result in a sub-optimal level of output.

This combination of characteristics means that every additional consumer who copies a book adds to their utility and that of society without there being any additional cost to society. However, if everyone was allowed to copy freely, maximizing society's utility from existing books, there would most probably be very few books ever produced, since authors and publishers would have no financial incentive to invest. Two alternative solutions to these problems suggest themselves.

The first solution is for the state to fund directly the production of literary and artistic works and for consumers to pay only the marginal costs of physical reproduction (the cost of copying). This has largely been the solution adopted by Eastern Bloc countries in the past. The obvious problems here are how to determine the optimal level and pattern of public funding. The state may not be very responsive to either individual or community preferences for one particular product such as books; furthermore it may deliberately distort those preferences.

The second solution, adopted by Western countries, is copyright legislation. This addresses the free-rider problem by granting the copyright owner the exclusive right to control the reproduction of their product, it prevents copying; all demand for the product results in financial reward to the copyright owner. However, this solution does little to address the public good problem or problems associated with cultural externalities and merit goods, and will therefore tend to overly limit access to literature and scientific texts. This problem is addressed in part by public subsidies to the arts and the funding of public libraries for which authors are compensated through public lending rights legislation.

A further problem created by the granting of copyright protection is that it provides the owner with a monopoly over the production (and distribution) of that good. This is not necessarily inconsistent with competitive markets, but it creates that possibility, which in turn tends to produce inefficiencies in the allocation of resources and the cost of production (and distribution).

If copyright legislation is the preferred solution, the question then arises as to where the limits of copyright protection should lie. Should copyright protection extend to ideas or only to the expression of ideas? Should it cover derivative works or only the original work? Should it include rights to control the public performance and broadcasting of works? What is the appropriate period of protection? At what point are rights 'exhausted'? Moral theories are not very helpful in resolving these issues. Economic theory can be useful in helping to

¹² Musgrave, R. A., *The Theory of Public Finance* (1958).

¹³ *Australian*, 8 December 1989.

provide answers and in practice the law often resolves issues in ways consistent with economic theory.¹⁴

The question of the exhaustion of rights is the one which underlies the issue of parallel imports; having sanctioned the reproduction of a book in one country, should the author's rights over the further distribution of that book be exhausted or should they be able to prevent those reproductions from being imported into another country? As this section of the paper has shown, there is a clear problem of market failure associated with the production of books in an unregulated market; they will be copied and the rewards to the original author and publisher will be appropriated by the copier, giving rise to underproduction. However, once a book has been validly reproduced, is there any need for legal restrictions to be imposed on its distribution, in particular on international competition in its distribution (by restricting sales of a book which has been legitimately reproduced in one country in another country)? To justify restrictions on the distribution of books of this kind, one would have to identify some area of market failure in the area of book distribution; that is an area other than one associated with copying, a failure overcome by copyright protection in the original country of production of the book.

4. *The Economics of the Importation Provisions*

The importation provisions clearly benefit the owners of the Australian copyrights in books, who are guaranteed the returns from all sales of those books in Australia, but do they also maximize the total welfare of society? As Adam Smith pointed out, the pursuit of self-interest results in the maximization of society's economic welfare provided it is tempered by a competitive market. Smith was highly critical of 'mercantilist' economic policies which sought to restrict free international trade and protect domestic suppliers from import competition. The importation provisions (as they relate to parallel imports), restrict import competition and are not necessary to address the free-rider problem of copying books.

Although copyright protection provides the owner or assignee of the copyright with exclusive rights over the production and reproduction of an individual book, this is not necessarily inconsistent with a competitive market outcome. This will depend on the availability of books which are close substitutes for each other. In this context, it is significant that copyright does not protect ideas but only the expression of ideas. Hence there may be competitive texts expounding the same economic theories or legal doctrines. If one publisher charges a monopoly price, others can enter the market with a competitive text and offer it at a lower price.

The importation provisions extend copyright protection from control in the sphere of *production* into control over the sphere of *distribution*. Economic analysis clearly identifies a market failure associated with copyright products,

¹⁴ Landes, W. M., and Posner, R. A. *op. cit.*

namely piracy, but it is a market failure associated with production not distribution.¹⁵ In other words, at the stage of book production there is a problem of market failure associated with the problem of copying, since copying leads to underproduction. The problem is fully overcome by copyright laws which prohibit piracy. Once the book has been produced validly, questions arise about its distribution. The presumption is that the market should be allowed to distribute books without legal restrictions on trade or competition, unless a specific failure in that sphere can be identified. There is no reason why copyright restrictions should extend beyond the sphere of production.

It has been a well-established economic principle since Adam Smith that free international trade maximizes society's economic welfare; through competition it directs resources to their most productive use, encourages the search for the most cost efficient means of production and distribution and results in the specialization by individuals and countries in the production of those goods and services where they are most efficient. Why should books be different from other goods and services in this respect? To support an economic argument for the existence of the importation provisions, they must give rise to some other benefit which outweighs the negative impact on competition. The Prices Surveillance Authority's Inquiry produced considerable evidence that the lack of international competition in the book trade has resulted in significant disadvantages for Australia: price discrimination; poor availability; and high costs.

In the first place, British publishers, who generally control the copyright for books outside the U.S.A., are able to engage in 'price discrimination' between markets, *i.e.* charge different prices for the same books in different countries, with Australia (and New Zealand) paying much higher prices than other English speaking countries. These higher prices are not related to cost differences to any significant extent. Due to the import restrictions, publishers can set prices on the basis of what each market can bear rather than on the basis of the relative cost of supplying that market as would happen under competitive conditions.

Persistent price discrimination between different geographic markets can only occur, in general, if three pre-conditions are satisfied. The first is that there is a lack of competition in the higher priced markets. With respect to the Australian book market, this is brought about by the legal inability of booksellers to import lower priced copies of the same, or substantially the same, book. The lack of competition is reinforced, if evidence to the Inquiry by a former managing director of a major British book publisher is accepted, by the collusion of British publishers in determining the pricing of Australian books.¹⁶

The second pre-condition for price discrimination is that demand conditions must differ in the various markets. If they do, then it is profitable to charge a higher price in the market with greater willingness to pay than in the market with

¹⁵ The provisions currently apply equally to both pirate and parallel imports. Protection from pirate imports is a necessary adjunct to the prevention of copying; all participants in the books debate agreed that protection from pirate imports should be maintained. The issue is whether the owner of the Australian copyright should also enjoy protection from parallel imports.

¹⁶ Prices Surveillance Authority, *op. cit.* 33.

less willingness to pay. Higher prices can be, and are, charged in Australia and New Zealand than in most other English speaking countries. British books sent to Canada (at very similar freight costs) have to be sold at much lower prices than in Australia (and even at prices a little lower than in the U.K.). This is because, despite the similar import restrictions in that country,¹⁷ Canadian bookbuyers can purchase lower priced books from across the United States border. Information on the pricing policies of Australian and Canadian subsidiaries of British publishers suggested that they set a price which the market in that country would bear and this in turn determined the transfer price from the U.K. parent company.¹⁸ In the United States, prices of books are relatively low compared to Australia because the larger market, with its longer print runs, keeps costs down; and because there tends to be more competition in the larger market, keeping prices closer to costs. Much the same applies in the U.K., although on a lesser scale than in the U.S.A. In India, British publishers cannot extract high prices because there is competition from pirate books and because of lower average incomes. In Australia and New Zealand several factors allow publishers to charge higher prices: the small Australian market with its small print runs means that price competition from local books is slight and that Australian bookbuyers do not therefore have low priced local alternatives to turn to; there also tends to be limited price competition in the smaller Australian market; unlike in Canada, buyers cannot so readily purchase from nearby markets with low prices; Australian incomes are higher than in Asia and so there is greater willingness to pay on this account as well.

The third precondition for price discrimination is that suppliers must be able to keep the markets in which higher prices are charged separate from the lower priced ones. In Australia this is achieved by the importation provisions of the Copyright Act. If this separation did not occur, then 'arbitrage' would occur: lower priced books from overseas would be imported, ultimately reducing the price of books in Australia. Providing that the retail sector was competitive (or even if it set prices on a cost-plus basis), bookbuyers would pay lower prices.

The Prices Surveillance Authority's report clearly and authoritatively documented the existence of substantial and persistent price differences between Australia and other English speaking countries, differences which can only be sustained by the importation provisions of the Copyright Act. A typical paperback bestseller would retail for \$A11.95 in Australia, \$A7.05 in Canada and \$A5.45 in the U.S.A. (in a different edition). Examination of data on the comparative prices of identical books supplied to the Australian and Canadian markets by British publishers found that books are marketed in Canada at prices generally below or close to the U.K. price, despite the additional freight costs; on average they were \$0.35 or 2.58 per cent below the U.K. price. By contrast, the same books marketed in Australia were sold at prices well above those in the U.K.; on average they were \$2.99 or 31.3 per cent higher.¹⁹ The Authority

¹⁷ Copyright Act 1921 (Can.).

¹⁸ Prices Surveillance Authority, *op. cit.* s. 4.3.

¹⁹ *Ibid.* 51.

estimated that removal of the import restrictions on books would on average lower the price of books in Australia by some 30 per cent, with variations between some categories.

In addition to excessive prices, considerable evidence was presented to both the Copyright Law Review Committee and the Prices Surveillance Authority regarding the poor availability of books in Australia. This had three aspects: the late release of titles onto the Australian market, months and sometimes years after their release overseas; only being able to obtain the hardback edition of a book in Australia when the paperback is available overseas; frequent out of stocks and long delays in filling orders for back titles. Without the spur of a competitive distribution system, the incentive to improve efficiency is limited.

Furthermore, the importation provisions have resulted in a certain set of arrangements for the distribution of books in Australia.²⁰ A large number of publishers supply directly to a large number of retailers. Mass handling by wholesalers which existed in the nineteenth century has been suppressed by the closed market. The multiple orders and deliveries which the current system produces does not suggest cost efficiency; a freely competitive market would allow this hypothesis to be tested. This distribution system has also produced a high level of stock holding by Australian publishers; stock to sales ratios were found to be two to three times higher than the average for the manufacturing industry.²¹ Such stockholding has a high cost in terms of the alternative uses of resources invested in them. Whether publishers have chosen the level and pattern of stockholding which represents an optimal allocation of resources against competing demands is not currently tested by a competitive market.

The market failure which copyright protection over reproduction addresses is the free-rider problem of piracy. The importation provisions extend copyright controls into distribution, creating a legislative vertical restraint on trade. These provisions are not required to address the problem of copying and clearly they have undesirable costs in terms of excessive prices and inefficiency. Are there any free-rider problems in distribution which could justify such constraints?

The issues of vertical integration between production and distribution and vertical restraints commercially imposed by producers over distributors has been the subject of much economic and legal literature in the field of industrial organization and trade practices. Producers who seek to exercise control over the distribution of their product, either by directly taking over the distribution function or by requiring distributors to supply their products under certain conditions may have the purpose or effect of creating barriers to the entry of new producers into the market. However, it is accepted widely now that certain forms of vertical restraint which might otherwise be seen as anti-competitive are efficient means of overcoming problems of free-riding. This particularly arises in the case of products which are characterized by high levels of after-sales service. The exercise of control over distribution may be necessary for producers to

²⁰ *Ibid.* s. 4.4.

²¹ *Ibid.* 41.

ensure quality control and that other producers do not free ride on their after-sales service. Hence the High Court of New Zealand recently ruled in favour of the exclusive dealing arrangements imposed on retailers of its whitegoods by Fisher & Paykel Limited.²²

However, there is a crucial difference between the debate in the trade practices arena about the costs and benefits of not outlawing vertical restraints such as exclusive dealing, and the debate about the importation provisions of the Copyright Act. In the latter case, there is a legislative enforcement of vertical ties. In the former, the debate is about whether the law should be used to prohibit such ties. Whether particular vertical restraints are pro- or anti-competitive depends on the specific characteristics of the market and the structure of the industry; which suggests it is inappropriate to have blanket legal enforcement without regard to those specific (and changing) characteristics.

After-sales service such as that provided in the whitegoods or motor vehicle industries is not a characteristic of the book industry and free-riding by parallel importers would therefore not pose a problem in this area. Free-riding may also occur in relation to advertising and promotion; parallel importers may benefit from the demand created by the Australian copyright holder's investment in advertising and promotion. This issue is relevant to the book industry. However, the costs of this free-riding must be balanced against the costs of import protection outlined above. Advertising costs are less significant for the book industry than they are for example in the record industry; and it is far from certain whether the level of advertising produced with import protection is the optimal one.

5. The Copyright Act and the Trade Practices Act

It has been suggested that any anti-competitive consequences arising from the importation provisions could be dealt with by the Trade Practices Act 1974 (Cth). By creating a legal monopoly to overcome certain problems of market failure, copyright creates problems for the interface with competition law. Section 51(3)(a) of the Trade Practices Act deals with this problem by providing a *limited* exception to Part IV of the Act for copyright products.

(3) A contravention of a provision of this Part other than section 46 or 48 shall not be taken to have been committed by reason of —

(a) the imposing of, or giving effect to, a condition of —

(i) a licence granted by the proprietor, licensee or owner of a patent, of a registered design or of a copyright . . . ; or

(ii) an assignment of a patent, of a registered design or of a copyright . . . to the extent that the condition related to —

. . . (v) the work or other subject matter in which the copyright subsists;²³

The key phrase 'relate to' is open to judicial interpretation and has yet to receive much attention.²⁴ In exercising their exclusive rights under the Copyright Act, copyright owners should not impose conditions on licensees which do not 'relate

²² *Fisher & Paykel Limited v. Commerce Commission & Ors.* (1990) 3 N.Z.B.L.C.

²³ Trade Practices Act 1974 (Cth).

²⁴ 'Intellectual Property Exceptions' (1983) *Australian Trade Practices Reporter* 8633.

to' the copyright. The interpretation of this phrase is critical in determining how limited is the exception.

The exception does not extend to s. 46 (abuse of market power). The use of this section in relation to the importation provisions has never been tested by the courts. However, it would seem in the case of books that the use of s. 46 would require a very narrow definition of the market.²⁵ The famous 'Time-Life' case concerning the importation provisions did not test their relationship to s. 46. Parallel imports were found to be illegal, but Murphy J., in his minority judgment, commented:

Neither Angus & Robertson Bookshops nor the respondent chose to expose the full facts. The evidence is scanty, but suggests that the Australian public will suffer if the respondents succeed, that the copyright is being used to manipulate the Australian market, and that the respondents will control the outlets, and the price to the public will be almost doubled, and the Australian public will have delayed access to publications freely available in the United States.²⁶

Excessive prices to consumers, unreasonable delays in supply and cost inefficiency in the distribution of books are not issues directly covered by s. 46. It seems unlikely that the Trade Practices Act provides the opportunity to deal effectively with the anti-competitive consequences of the importation provisions.

6. *International Conventions and Agreements*

Australia is a signatory to several international treaties relating to copyright administered by the World Intellectual Property Organization (WIPO) and the United Nations. It has been suggested that the importation provisions derive from Australia's obligations under those treaties, particularly the Berne Convention. The Berne Convention requires signatory countries to provide certain specific minimum rights for works first published in any member country. These rights relate to the production and reproduction of copyright works. Additional rights may be provided at the discretion of member countries, but Article 5 provides that these additional rights should be provided on the basis of equal national treatment. The Berne Convention does not explicitly provide any general rights over distribution. It has been argued that this omission reflects a belief by member countries that no such explicit rights are required because they are implicit in the reproduction rights granted by the Convention. In fact, the history of the Berne Convention would suggest otherwise.²⁷ Attempts to introduce a general right of distribution into the Convention have been explicitly rejected because of fears concerning the potential anti-competitive consequences of such a right. Australia voted against the last attempt to introduce one at the Stockholm Convention in 1968.

²⁵ Copyright Law Review Committee, *The Importation Provisions of the Copyright Act 1968* (1988) 44; Cornish, W. R. and McGonigal, P. G., 'Copyright and Anti-trust Aspects of Parallel Imports Under Australian Law' (1980) 6 *International Review of Industrial Property and Copyright Law* 731.

²⁶ *Interstate Parcel Express Co. Pty Limited v. Time Life International (Nederlands) B. V.* (1977) 138 C.L.R. 534.

²⁷ Ricketson, S., *The Berne Convention for the Protection of Literary and Artistic Works: 1886-1986* (1989).

Under the current round of negotiations of the General Agreement on Tariffs and Trade (GATT), trade related aspects of intellectual property rights are a significant item on the agenda. This reflects a desire, initially by the United States, to get effective enforcement of intellectual property rights, a function which was not being performed by WIPO. The United States has proposed that a GATT agreement on copyright should include a requirement for member countries to adopt importation provisions in their copyright legislation.²⁸ This reflects the interests of the United States as a net exporter of copyright products. The proposal has not received support from any other parties. In particular, developing countries, who are usually net importers of copyright material want to have maximum access to copyright products at competitive prices. However, other countries, including Australia (also a net importer), have also not been supportive of the move. This reflects a desire for flexibility in domestic legislation, including the ability to deal with any anti-competitive consequences of import controls.

One argument which has been put forward against opening the market to parallel imports is that it will be very difficult to distinguish a legal (parallel) import from an illegal (pirate) import. Thus the cost of effective enforcement could be high or reproduction rights could be undermined. To the extent that the GATT negotiations are successful in raising levels of effective protection against piracy in member countries, this argument would become redundant.

7. Policy Options

Before the Prices Surveillance Authority examined the market for books, the Copyright Law Review Committee had examined the importation provisions in general, as they relate to all copyright material not just books. The Committee's review was essentially a legal one; although economic issues were examined, the Committee felt itself unable to assess the conflicting evidence presented to it and to make an informed judgment on the critical issue of price. Without any conclusive economic analysis, they felt unable to recommend the repeal of the provisions.²⁹ However, they did not regard copyright as a set of 'absolute rights' and proposed to shift the boundaries of these rights. They focused on possible amendments which might achieve a better balance between the moral rights and obligations of copyright holders, and in particular the obligation of copyright holders to make their work available to the public in return for the protection which it receives. Their proposed reforms were designed to deal with the problems of poor availability which had arisen under the existing regime of import protection. The importation of a non-pirated copyright article by a person engaged in trade or commerce without the licence of the copyright owner should be permitted where:

²⁸ Negotiation Group on Trade-Related Aspects of Intellectual Property Rights, Communication from the United States, Draft Agreement On the Trade-Related Aspects of Intellectual Property Rights, 11 May 1990.

²⁹ Copyright Law Review Committee, *op. cit.* 234-47.

- (i) the article, or an article substantially similar to it, is not available within a reasonable time; or
- (ii) the importer has received a specific written order for the article.

All copyright material was to be treated in the same way except that 'reasonable time' was to be determined separately by regulation for each industry according to the time required for manufacturing and/or importing the articles; the same moral issues of rights and obligations apply to all goods and services receiving copyright protection. An economic analysis would not necessarily produce the same answers for all markets. As discussed previously the free-rider issue is critical to the analysis of controls over distribution and their effect on competition; the nature and extent of free-rider problems are critically dependent on specific features of different markets.

The Prices Surveillance Authority examined the specific characteristics of the market for books and the effect of the importation provisions on competition, prices and efficiency. This economic analysis was able to provide much clearer answers than an examination of moral issues; the Authority concluded that the provisions had undesirable consequences on all these fronts in the market for books. The reforms proposed by the Copyright Law Review Committee would go only half way to addressing these problems. While they would improve the availability of books and probably reduce the price of specialist books and backlist titles, they would maintain import protection for the majority of books sold in Australia, with all the attendant consequences of high prices and inefficiency. Without an open market there would be little competitive pressure to bring down the price of these books to Australian consumers; and the development of book wholesaling, bringing cost efficiencies from mass handling would be unlikely. In addition, the reforms proposed by the Copyright Law Review Committee would themselves involve economic costs; the definition of 'substantially similar'³⁰ was to be left to the courts, with all the associated costs of litigation; and there would be considerable administrative costs for potential importers associated with establishing the copyright status of individual titles and the paperwork required for individual written orders.

The Authority therefore recommended the repeal of the importation provisions with two exceptions:

- (i) pirated books; and
- (ii) books by Australian resident authors with a separate Australian publishing contract.

The latter recommendation was to be limited to ten years to promote the development of the 'infant industry' of Australian literature and publishing.³¹

The release of the Authority's report was met with moral outrage by prominent authors and publishers. They claimed that copyright was an inalienable property

³⁰ This definition is particularly important because of the effect on the availability of paperback books; is a paperback book substantially similar to the same book in hardback form?

³¹ This recommendation may have come into conflict with Article 5 of the Berne Convention regarding national treatment and legal drafting problems may have arisen in relation to defining an Australian publishing contract.

right of authors which should not (indeed could not) be tampered with by governments. Morris West, for example, made the following remarks:

copyright and the rights arising out of copyright are the inalienable property of the author. To expropriate this property under any pretext is a fundamental invasion of human rights.³²

It was argued that Australian authors, rather than British publishers, benefited from the importation provisions and that the Prices Surveillance Authority's proposals to open the market would result in the demise of Australian culture and literature. The Authority had commented on the growth of Australian originated books during the past decade, but their analysis was firmly grounded in economics. Publishers had invested in these books not out of altruism and a concern to promote Australian culture for its own sake, but from economic self-interest. The market for books with an Australian identity is a growing one; publishers had correctly identified this and were making investment decisions based on expectations of profits, in the long run if not in the short run. Australian literature should not be promoted simply because it is Australian, but because people want to read it and are prepared to pay for it. It is no coincidence that the authors leading the campaign against the Authority were those with established international reputations who were able to exploit the importation provisions to enable the charging of higher prices for their books in Australia than overseas, thereby reducing the access of Australians to their books.

More generally it was argued that literature is too important to be subjected to economic analysis, that its benefits cannot be expressed in financial terms and that economists are unqualified to comment on these issues. We would argue that on the contrary economists are singularly well qualified to comment on these issues. Without the rigour of economic analysis, how are we to determine on the basis of moral argument the 'social value' of investment in this area and the legislative framework which enables Australia to make the most productive use of its limited resources from the whole range of potential economic activity, of which books are but one area? If it is the case that the production of books gives rise to cultural benefits which are not reflected in the market value placed on them, then they should be explicitly and transparently funded through public subsidies; for whatever the cultural benefits, they also have an economic cost to taxpayers. Creating a monopoly over distribution and raising their prices only serves to limit access to these cultural benefits. After much lobbying from authors and publishers defending the importation provisions on moral grounds and from booksellers seeking to open the market to competitive imports, Cabinet's decision represented a political compromise between the two:

- (i) if a book is first published in Australia or within 30 days of overseas publication, import protection will be retained, otherwise it can be freely imported;
- (ii) if a protected book ceases to be available from the local supplier for 90 days, it can be freely imported until local supply is resumed; and
- (iii) documented individual orders can be imported at any time.

³² *Australian*, 13 October 1989.

While this solution should improve the availability of books to Australian readers, its effect on prices will be muted; for books which meet the thirty day requirement there will be little competitive pressure to bring down prices and indeed the costs of air freighting books to meet this requirement may in some cases be passed on to consumers in *higher* prices. The proposals involve considerable administrative complexity and costs for any potential importers having to establish the copyright status of hundreds of books. This would be unlikely to spur the development of wholesaling activities which might bring back the benefits of cheap books enjoyed by nineteenth century Australians. Furthermore, the Bill appears to somewhat water down Cabinet's decision in respect of the 90 day 'revolving door' and individual orders. Free importation under the former is only available to a person who has placed an order with the local licence holder which has remained unfilled for 90 days; others must place their own orders before being able to import. The provisions for individual orders contained in the Bill only apply to *written* orders for *single* copies.

8. Conclusions

Authors claim that copyright is a set of 'absolute rights'. However, like other property rights, the law both grants these rights and places limits on them. All rights are limited because they cannot be exercised without affecting others. The question is how far should copyright extend? Moral arguments of rights versus obligations are inherently difficult to resolve. Economic analysis provides a useful set of tools for determining these boundaries. In general a freely competitive market maximizes society's total economic welfare. Why is competition not appropriate in the market for books?

The *production* of copyright products is characterized by market failures associated with 'public goods' and 'non-exclusivity'. Copyright protection is a means of dealing with the latter. However, it is not a justification for extending copyright controls into the sphere of *distribution*. Controls over free trade in goods and services, such as those contained in the importation provisions, tend to limit the 'Wealth of Nations'.

Production of books is an area in which, unless there are copyright laws, there will be market failure. Copiers of books will appropriate the rewards of the author and publisher, giving rise to underproduction of books. Copyright law in the country of original production protects against this source of failure. Moreover, other countries should prohibit the imports of pirate editions; this can be achieved without a blanket restriction on importation. Once a book has been legitimately reproduced in one country, there are no comparable problems of market failure in the area of distribution.

In recent years there has been a growing recognition that trade practices law may go too far in prohibiting various kinds of commercially determined vertical restrictions on trade (such as exclusive dealing). However, this debate has never endorsed statutory enforcement of vertical ties such as those embodied in the Copyright Act.

Are books different from other goods and services? Yes, they are different. They have a non-economic value which contributes to the 'Culture of Nations'. However, far from contradicting the general principles of economics, these benefits are achieved by their application to the market for books. The 'public good' and 'merit good' characteristics associated with books tend to result in their underproduction, supporting a case for public funding. Creating a legislative monopoly over the distribution of books, by contrast, has the effect of limiting access to books and the ideas contained in them, through poor availability and high prices.

More broadly, this examination of the importation provisions of the Copyright Act raises the issue of the difficult interface between intellectual property rights and competition policy, which has received scant attention in the past. The current age of information technology and biotechnology makes this area all the more important to study.