AN ECONOMIC ANALYSIS OF THE DIVISION OF COPYRIGHT BETWEEN NEWSPAPER PUBLISHERS AND JOURNALISTS

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ABSTRACT

The *De Garis* case found that a press-clipping service had infringed the copyright owned by newspaper journalists when it reproduced without a licence the articles of those journalists. The facts of the case are merely instances of a problem that is becoming widespread: technical change has facilitated the reproduction of newspaper copy and the ownership of copyright has therefore become a policy issue of increasing importance. This paper presents an economic analysis of the allocation of intellectual property by the *Copyright Act* 1968 (Cth) between newspaper journalists and publishers. It argues that, because of the costs of allocating licence fees to contributing journalists, and because of costs of risk-bearing, copyright should be owned not by journalists but by newspapers.

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I. INTRODUCTION

The *Copyright Act* 1968 (Cth) (*Copyright Act*) is the copyright law in Australia. Section 32(1) together with s 32(4), provides that, subject to the Act, an Australian journalist who writes a newspaper article ("an original literary work") owns the copyright of the article. The main limitation on journalists' ownership of copyright is s 35(4) which provides that if the article was written for the purpose of publication in the newspaper and was made in pursuance of an employment contract the proprietor is the owner of the copyright in so far as the copyright relates to the publication of the work in a newspaper.

The case of *De Garis and Another v Neville Jeffress Pidler Pty Ltd*[1] (*De Garis*) has clarified the rights and obligations of press-clipping services. In that case, before the Federal Court, Beaumont J found that a press-clipping service had infringed the copyright owned by two journalists. His Honour stated that an employed journalist retained copyright for the purposes of photocopy and clipping services even though s 35(4) grants copyright to the proprietor for the purpose of publication of the newspaper.[2] His Honour proceeded to state:

> In my view, the distribution of photocopies of selected newspaper articles does not constitute the publication of a newspaper, magazine or similar periodical for the purposes of s 35(4). The activity of providing press clippings on a commercial basis is different in character from the activity of publishing a newspaper. Nor can it be said that the monitoring service is an integral part of the publication of the newspaper in the sense explained in *John Fairfax*. They are distinct activities.[3]

Since the *De Garis* case, the press has contained reports of continued attrition between The Copyright Agency Ltd (CAL) and the Australian Journalists Association (AJA) on the one hand and the press-clipping services on the other. On 16 July 1992, *The Australian Financial Review* reported, p 9, that CAL had just completed the signing of an agency agreement with a news-clipping firm, *The Information Factory*. The same article reported that neither Neville Jeffress Pidler Ltd (the respondent in *De Garis*) nor the Commonwealth Government had yet entered into licence agreements with CAL.

The negotiations between CAL and the AJA and the press-clipping services are symptoms of a wider problem. Recent developments in the technology for photographic reproduction and electronic storage and transfer of printed works have increased the difficulties that are faced by journalists in enforcing copyright: it is becoming increasingly difficult for them (or their agents) to discover persons who may be infringing their copyright. Furthermore, if the press-clipping service

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1 (1990) 95 *ALR* at 625.

2 *Ibid* at 638.

3 *Ibid* at 639.

wishes to obtain a licence from the journalist who wrote an article, it is often difficult to discover the author because many articles are not signed. Still further difficulties arise when journalists (or their agents) try to negotiate a price at which they will grant a licence to those who wish to use the work.

In the language of economics, the problem is that technological developments have raised the transactions costs of licence agreements between journalists and the users of newspaper articles - where transactions costs include the costs of discovering the parties to the negotiation, the costs of conducting the negotiations, and the costs of enforcing the contract.

Given these technological developments it seems necessary to reassess whether the allocation of copyright under existing legislation is appropriate. In the next section of the paper the distinctive features of an "economic analysis" of copyright are described, and an associated rationale is provided for the existence of copyright protection for goods such as books, newspapers, sound recordings and computer software, which are produced from "intellectual labour". In section 3 the economic approach outlined in the previous section is applied to the issue of the appropriate division of the ownership of copyright between a newspaper publisher and journalists. Concluding remarks are contained in section 4.

II. AN ECONOMIC APPROACH TO COPYRIGHT LEGISLATION

Copyright legislation has the primary purpose of providing the owner of a product of intellectual labour with a series of rights over the use of that work. The circumstances in which copyright protection should be provided, and the extent to which property rights should be assigned to the producer of an intellectual good under copyright legislation, are important questions for policy-makers. This paper presents an economic approach to these problems as raised by the judgment in *De Garis*.

The distinctive feature of an economic approach is the attempt to provide a framework within which it is possible to ascertain the level and form of copyright which maximises the welfare of society. In such a framework, an optimal level and form of copyright are determined by a trade-off between the benefits of providing incentives to create work and the sum of the losses from limiting access to that work and the costs of administering copyright protection. For example, Landes and Posner argue that:

> For copyright law to promote economic efficiency, its principal legal doctrines must, at least approximately, maximise the benefits from creating additional works

minus both the losses from limiting access and the costs of administering copyright protection.[4]

The effect of copyright on incentives for the creation of new works derives from the allocation of property rights in those works under copyright legislation. The seminal paper by Ronald Coase on "The Problem of Social Cost"[5] showed that the efficient functioning of the economy was contingent upon the ability of persons to enforce property rights. The property rights referred to by Coase were construed very broadly. In essence, every economic asset should be owned by someone; and that person should be able to use the resource (and, indeed, to trade the resource) so as to secure maximum advantage from ownership. These property rights imply that the owner of any resource must be able to exclude from the use of the resource any person with whom the owner has not agreed to trade.

Property rights, and the associated ability to exclude, are vital for economic efficiency. Market economies rely on private individuals to make resource-allocation decisions. Private individuals generally make decisions that further their own self interest. A system of enforceable property rights ensures that the person who makes the decision will bear all the costs and gain all the benefits of that decision. Accordingly, the benefits and costs to the decision maker ("the private benefits and costs") will coincide with the benefits and costs to the whole of society ("the social benefits and costs"). In such a world, the individual decision makers may continue to make decisions that are self-motivated; but in choosing to allocate resources in accordance with their self-interest, they will (coincidentally) be allocating resources so as to maximise the welfare of society as a whole.

Copyright protection can readily be justified within this framework of property rights. The literary work is an economic asset and its ownership should be specified clearly. Furthermore, the owner should be able to exclude from use of the asset any person with whom the owner has not signed a licence.[6] This ability to exclude will ensure that persons only use the literary work if they pay for that use. So the social benefits of the work will accrue to the owner of copyright as a private benefit. For example, where the exclusive right to reproduce a literary work is vested with the original producer, then any demand for copies of that work should result in a payment to the producer. This increase in private returns will provide greater incentives for the production of literary works with a resulting increase in the range of literary works and an increase in the quantity produced of each literary work.

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4 W Landes and R Posner "An Economic Analysis of Copyright Law" (1989) 18 *Journal of Legal Studies* 326.

5 R Coase "The Problem of Social Cost" (1960) 3 *Journal of Law and Economics* 1.

6 For an analysis of the effects of copying on production of intellectual products in a market economy, see S Besen and S Kirby, "Private Copying, Appropriability and Optimal Copying Royalties" (1989) 32 *Journal of Law and Economics* 255.

Against the creation of incentives to expand production, it should also be noted that since copyright protection provides the owner of a literary work with the exclusive right to distribute that work it may allow the producer to restrict output in order to achieve a higher price and level of profits. However, as it can never be a profitable strategy for a firm with exclusive distribution rights to restrict output of any work to zero, the incentive to restrict output that is introduced through copyright protection will not affect the range of works produced.[7]

The impact of copyright protection should therefore be to cause an unambiguous expansion in the range of literary works produced; the effect on the quantity of each work will be determined by the relative impact of the incentives for increased production which are created due to higher private returns and for lower production due to the existence of exclusive distribution rights. An economic analysis therefore suggests that optimal copyright provisions which maximise social welfare will be designed to achieve a balance between the increase in social welfare from greater incentives for production of literary works and the decrease in social welfare from the granting of exclusive distribution rights.

Interestingly, it is this economic perspective which appears to have been the dominant influence on the evolution of copyright legislation in Australia. For example, the Copyright Law Review Committee, whose recommended revisions to the *Copyright Act* were implemented in 1968, stated that:

> In arriving at our recommendations our task has essentially been one of balancing the interests of the copyright owner with those of the copyright users and the general public. The primary end of the law on this subject is to give to the author of a creative work his just reward for the benefit he has bestowed on the community and also to encourage the making of further creative works. On the other hand, as copyright is in the nature of a monopoly, the law should ensure, as far as possible, that the rights conferred are not abused and that study, research and education are not unduly hampered.[8]

III. THE DIVISION OF COPYRIGHT BETWEEN NEWSPAPER PUBLISHERS AND JOURNALISTS

Private returns to newspaper production will be below the social benefits from production due to the absence of effective restraints on the consumption of a

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7 Landes and Posner, note 4 *supra* at 335, argue that a further cost of copyright provisions is that "... too much protection can raise the costs of creation for subsequent authors to the point where those authors cannot cover them even though they have complete protection for their own originality".

8 Copyright Law Review Committee *Report of the Committee Appointed by the Attorney-General of the Commonwealth to Consider What Alterations are Desirable in the Copyright Law of the Commonwealth*, Canberra, AGPS (1959) pp 8-9.

newspaper or periodical by consumers other than those who paid the original producer. This disparity between private and social returns and consequent sub-optimal level of production provides the rationale for the introduction of copyright protection for newspapers. However, having recognised that a role may exist for copyright protection a further issue must then be resolved: to which of the parties involved in production of a newspaper should copyright be assigned? In particular, should ownership of copyright for individual articles in a published newspaper be vested with the newspaper publisher or with journalists? An economic analysis of this issue involves establishing the optimal division of copyright; that is, the division of copyright between newspaper publishers and journalists which maximises social welfare.

In this section both transaction cost and risk-sharing arguments relating to the optimal division of copyright are considered.

A THE TRANSACTIONS COST ARGUMENT

Consider the example of a firm which produces a single good and hires labour as an input. Where a competitive market for labour exists, a worker's choice of employment will depend on a comparison of the net utility across available jobs (where net utility represents wages plus other pecuniary and non-pecuniary benefits of work minus the disutility of effort and the opportunity cost of training). Hence, in order to attract employees the wage paid by a firm for a given type or skill category of labour must be such that the net utility from working at that firm is at least as great as can be obtained in alternative employment.

Suppose that the firm can produce either a good over which it can enforce its property right or a good over which its property right cannot be enforced. Call these goods 'enforceable' and 'unenforceable' respectively, and suppose that each requires the same labour input and disutility of work. If the good which is produced is enforceable then the returns received by the firm will equal the social benefits of production; and a socially optimal quantity of the good will be supplied. On the other hand, if the good which is produced is unenforceable then the private returns to production will be below the social benefits and there will be underproduction of this good.

What are the consequences for wages of workers employed by the firm of this difference in output between enforceable and unenforceable goods? Since disutility of work and skill requirements are the same for production of each type of good, where labour is hired in a competitive labour market, the type of good which is produced will not affect the wage which must be paid to hire each unit of labour. Regardless of differences in the returns to the firm for production of each type of good, it is necessary to pay workers a wage which provides a net utility sufficient to attract them to the firm, and this net utility is invariant to the level of private returns to the firm.

In order to achieve an improvement in social welfare, a scheme which provides ownership of copyright to producers of otherwise unenforceable goods is then introduced. Will the effect of this copyright scheme depend on whether it is assigned to the firm or to the workers who produce the intellectual public good? Suppose that the reason why the private returns to production of the unenforceable good are below the social benefits is that the enforceable good is a literary work; and it is possible for copies to be made and sold at a price below the cost of production of the original good. The introduction of copyright allows the owner of that copyright to either prohibit copying, which should increase demand for the original good, or to charge a royalty payment for each copy of the original good.

Where copyright is assigned to the firm, each of these possible mechanisms will increase the private returns to production; to the extent that copyright can raise the private returns toward the level of social benefits there will be an expansion in the range of literary works produced and (where the effect of copyright on production incentives dominates the incentives for restricting distribution) an increase in the production of each literary work. Each of these changes will generate an improvement in social welfare.

Alternatively, if copyright is assigned to workers, there will be no direct transfer of revenue to the firm as a result of the introduction of copyright. Workers will have an incentive to charge royalty payments for copies of the original work; but since these payments are received exclusively by workers there will be no change in private returns to the firm and hence, it might be expected, no change in supply of the literary work. However, this argument fails to take account of the effect of the royalty payments on the net utility of workers. Where a firm was previously offering a wage which was just sufficient to attract labour, with the introduction of copyright and royalty payments, net utility to those who work at the firm which produces the literary work will be strictly greater than for those who work at any alternative firm. Therefore, for workers who are only concerned with the expected value of monetary payments, the firm which produces the literary work could lower wage payments by an amount equal to the expected value of royalty payments and still attract the same quantity of labour. This reduction in the cost of supplying the literary work will raise the incentives for production of that good. Since the reduction in production costs when copyright is assigned to workers should be equivalent to the increase in private returns achieved if copyright is allocated to the firm, an identical outcome with respect to the range and quantity of literary works, and employment of workers, can be achieved in both cases. Note however that if the firm is unable to reduce wage payments to workers then the benefits from copyright protection cannot be transferred to the firm and there will be no improvement in production of the literary work.

That the production outcome in the market for intellectual goods could be invariant to the division of copyright between a firm and its workers is an application of the "Coase Theorem" which is derived from the article by Coase mentioned previously in section 2.[9] The theorem states that in any market with zero transactions costs and no restrictions on monetary transfers, a socially efficient outcome should be achieved for *any* initial distribution of property rights.

The Coase Theorem might be taken to mean that the decision by policy-makers on how to assign ownership of copyright will not affect the production of literary works and hence social welfare. However, it must be emphasised that both the Coase Theorem and the argument in the previous paragraph on the welfare effects of the division of copyright depend critically on the assumption of zero transactions costs.

With positive transactions costs each allocation of property rights may cause a different production outcome and hence a different level of social welfare. For example, suppose that significant transactions costs are incurred in administering any copyright scheme which involves payment of royalties to workers. Since transactions costs decrease the size of royalty payments received by workers, such costs will also reduce the size of the wage decrease which it will be possible for the firm to implement. With a smaller reduction in the cost of production the firm's incentives to expand production will be limited. In this case the social welfare outcome which is effected by assigning copyright to workers is inferior to that from assigning copyright to the firm; employment is also reduced by assigning copyright to the workers. Hence where there is a significant differential in the transactions costs which are incurred depending on which party is assigned copyright, the greater increase in welfare will be achieved by assigning ownership of copyright to that party which is associated with the lowest incidence of transactions costs.

With regard to the issue of the division of copyright between a newspaper publisher and journalists, it seems that significant transactions costs may be incurred where copyright is assigned to journalists. Indeed it has been argued that it would be such an expensive procedure to decide upon an appropriate division of royalty payments between journalists (for example, measuring the relative frequency of copyright of each journalist's articles, and separating the relative contribution of the author or authors of an article and a sub-editor) that royalty payments should instead be directed to a trade union representing journalists.[10]

9 Note 5 *supra*.

10 The Secretary of the Australian Journalists' Association has stated that "... it would be almost impossible to identify individuals whose work has been copied without onerous administrative costs that would wipe out most of the gains made." "Copyright Victory Backs Vital Principle" (August 1990) *The Journalist* 2.

However if those royalty payments are not transferred from the union to individual journalists it will not be possible to reduce wages and there will be no adjustment in the cost of production for a firm. With significant transactions costs, assigning copyright to journalists will therefore not bring any improvement in social welfare.

It also seems that a high level of transactions costs would be incurred if copyright were to be allocated to publishers but with journalists being given the right to veto reproduction of any article. This right of veto provides scope for 'hold-up behaviour' by journalists who could demand some monetary payment in return for allowing reproduction of the article. Transactions costs which arise due to such bargaining between the publisher and journalists over the division of returns from copyright must also reduce the benefits of copyright which accrue to the firm, and hence will also limit the extent of improvements in social welfare. To avoid incurring significant transactions costs which may prevent copyright protection from affecting output of intellectual goods and social welfare, it therefore seems that copyright should be assigned to newspaper publishers.[11]

It has been suggested that a potential problem with assigning ownership of copyright is that it may allow a publisher to use a journalist's output in some form which adversely affects the reputation or future earnings of the journalist (for example, reproduction of individual articles of a journalist as a collected work). However, it seems that the appropriate response to this concern would be to allow a publisher's ownership of copyright to be modified through a contract prohibiting the reproduction or use of the article in specified forms which would be negotiated at the time of hiring of a journalist. The advantage of restricting any changes to a publisher's ownership of copyright to occur through negotiation between the publisher and journalist is that it ensures only those changes to the assignment of copyright which are socially optimal will be implemented. That is, only if the costs to the journalist from reproduction of the good in the specified form outweigh the benefits from reproduction received by the publisher will it be possible for the journalist to induce the publisher to renegotiate the division of copyright.

B. A NUMERICAL EXAMPLE OF THE TRANSACTIONS-COST ARGUMENT

A numerical example may assist in understanding why the optimal division of copyright would seem to involve assigning ownership to the newspaper publisher.

11 The argument that transactions costs will be greater if copyright is assigned to journalists rather than publishers does not seem to extend to the publication of a collection of newspaper articles by an individual journalist - in this case the distribution of returns from copyright to the journalist would not seem likely to incur significant transactions costs. Hence the criterion of maximising social welfare does not provide a basis for distinguishing between different assignments of copyright for books composed of articles originally published in a newspaper or periodical.

Suppose that a newspaper is produced using a single input - the labour of journalists - and that the cost of production consists of wage payments to journalists of $4500. Assume that the price per copy of the newspaper is $5 and that, in the absence of any possibility of copying, 1000 copies would be sold. Since the social benefit of production, which equals quantity purchased multiplied by selling price, is at least as great as the cost of production, it is in society's interest for the newspaper to be produced. However, if there is scope for copying which reduces to 800 the number of copies of the newspaper sold, then the newspaper will not be produced because the revenue received by the publisher ($4000) will be less than the total cost of production ($4500).

Now consider the effect on production of introducing copyright in the newspaper and assigning ownership to the publisher. Since the publisher can then charge $5 from each individual who receives a copy of the newspaper, either as a royalty or as a purchase price, total revenue will be increased by $1000 and the publisher can earn a positive return by producing the newspaper.

Alternatively, what will be the outcome of assigning copyright to journalists? In this case, the same royalty payments of $1000 will be available to be claimed by journalists. Where these payments are received directly by individual journalists two scenarios are possible. If journalists' wages are flexible then it will be possible for the publisher to reduce wage payments to $3500. Since net payments to journalists remain equal to $4500 it will still be possible to hire journalists; and with the reduction in production costs to $3500 the publisher can again earn a positive return by producing the newspaper. Alternatively, if journalists' wages cannot be adjusted downwards then production costs remain equal to $4500 and the newspaper will not be produced. If it is not possible to distribute the royalty payments from copying to individual journalists, then in order to hire journalists wage payments must remain at $4500 and hence the costs of production will continue to exceed total revenue. More generally, when transactions costs reduce the value of royalty payments received by journalists to less than $500, production costs will be at a level such that the newspaper will not be produced.

C. THE RISK SHARING ARGUMENT

A further argument which suggests that assigning copyright to publishers will be optimal is that this may achieve an efficient risk-sharing outcome between publishers and journalists. Where the publisher is assigned copyright the journalist's monetary income consists of a fixed wage payment; by contrast when a journalist is assigned copyright and receives royalty payments, that individual's income consists of a fixed wage payment plus royalty payments - the value of this latter component is uncertain and will vary with the amount of copying.

In a competitive labour market, utility from the fixed and variable wage payment schemes would have to be equal for a firm to be able to hire labour under either wage scheme. Where a worker is risk-neutral and cares only about the expected value of monetary income, that worker will obtain the same utility from fixed and variable wages which have the same expected value. However, if as is often assumed, the worker is risk-averse, then the worker will strictly prefer to receive a fixed wage payment rather than an uncertain wage which has the same expected value. In this case, in order to attract labour under the variable wage scheme, a firm would have to pay a variable wage with a higher expected value than the fixed wage. Hence where a firm is risk-neutral and employs a risk-averse worker, optimal risk-sharing entails paying a worker a fixed wage as this is the minimum cost method for the firm to provide a given level of net utility to a workers.[12] Optimal risk-sharing is therefore consistent with assigning copyright to the newspaper publisher as this arrangement will provide the worker with a fixed income. A fixed wage payment should also provide greater incentives for a worker to invest in training than a variable wage scheme.[13]

IV. CONCLUSION

Technical change over the last decade suggests that a review of the *Copyright Act* is timely. In particular, the allocation of copyright between newspaper journalists and newspaper proprietors must be reconsidered. Economic efficiency provides a standard for assessing the optimal allocation of copyright.

An economic analysis of the distribution of property rights seeks to provide a framework for determining the allocation of rights which maximises social welfare. In this framework the rationale for allocating ownership of copyright to the producer of an original copy of a literary work is that in the absence of copyright protection, private returns to the production of literary works will be below the social benefits. In a market economy a quantity of these goods will therefore be produced which is below the social optimum. Applied to the question of what is the optimal division of copyright between newspaper publishers and journalists, an economic analysis suggests that the allocation of copyright should be that allocation which achieves the maximum social welfare.

Where no transactions costs are incurred in distributing the returns from ownership of copyright then the outcome in the market for newspapers and periodicals will be independent of the assignment of copyright. However the

12 See S Rosen "Implicit Contracts: A Survey" (1985) 23 *Journal of Economic Literature* 1144.

13 See D Levhari and Y Weiss "The Effect of Risk on the Investment in Human Capital (1974) 64 *American Economic Review* 950.

assumption of zero transactions costs does not seem appropriate where journalists own the copyright or are assigned a veto power over the reproduction of the original good. In particular, the administrative costs of distributing royalty payments to individual journalists would seem likely to significantly reduce the size of monetary transfers received by those journalists and hence to limit the extent of reductions in production costs and incentives for increased production by newspaper publishers.

Furthermore, optimal risk-sharing between a publisher and an individual journalist, where the former is less averse to fluctuations in income then the latter, would involve the assignment of copyright to the publisher in order that the journalist should receive a fixed income, independent of the size of royalty payments. Both transactions costs and the risk-sharing arguments therefore suggest that an assignment of copyright to the newspaper publisher will yield the greatest improvements in social welfare relative to the case of a market for newspapers where copyright protection does not exist.