



Inquiry into IT Pricing

*Submission to the House Standing Committee on Infrastructure and
Communications*

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The strategies of price discrimination engaged in by a number of international publishers, coupled with a lack of competition and restrictions on the ability of consumers to engage in arbitrage, is likely to undermine the legitimacy of copyright law in Australia. By increasing prices beyond a reasonable and fair level, these strategies also undermine the goal of copyright law to enhance access to cultural goods. Enhancing access – and therefore lowering prices – is crucial to enhancing Australia's innovative capacity and the ability of Australians to experience, learn, act, and grow through cultural works.

We recommend that the committee investigates the following options:

- Repeal parallel importation restrictions;
- Fundamentally reconsider the operation of anti-circumvention law in the context of digital distribution models;
- Prohibit and render unenforceable contractual restrictions on parallel importation;
- Introduce a right of digital resale in Australia.

Arbitrage enhances competition and increases access to culture

Copyright operates to provide an incentive for firms to invest in the production and distribution of creative expression. As a utilitarian statutory monopoly, it operates to balance the incentives provided to producers against the interests of the public in having rich access to expression. Seen this way, access is the goal of copyright – access to culture is a predicate for individuals to learn, grow, create, and contribute back to society.¹ The exclusive rights provided to copyright owners are designed to ensure that producers have the ability to invest in the production of new expression, but they are not ends in themselves.

When copyright is not balanced, and when the market for copyright products is not competitive, producers and distributors are able to extract monopoly rents. The supra-competitive prices, above and beyond the levels that are needed to incentivise investment, result in an inefficient social cost – deadweight loss – that represents the unmet demand for access to copyright works. Excessive prices exclude consumers who are willing to pay a fair price for access. To the extent that copyright should be concerned to maximise access, this loss is highly problematic.

Price discrimination is seen as unfair by Australian consumers

The CHOICE submission to this enquiry demonstrates the prevalence of massively inflated pricing digital downloads purchased in Australia.² The difference is particularly visible in the games industry, where some publishers on Steam offer digital downloads to Australians at up to three times the price of the same download is available to consumers in the US. Certainly, not all publishers inflate prices to such an extent in the Australian market, but the practice has become sufficiently widespread to cause problems for Australian consumers.

Price discrimination leads to a perception that Australian consumers are being 'ripped off' by copyright owners and intermediary distributors. No convincing argument has been put forward to explain why price differences are so great, particularly given that the Australian dollar has been relatively stronger against the US dollar in recent years. Digital distribution models drastically reduce publishers' costs and limit the rights of Australian consumers to make use of historically important secondary markets in used games, software, music, and films. The cost savings to publishers, however, have apparently not been passed on to consumers.

In a qualitative study of consumers' perceptions of deviant consumer behaviours, Paula Dootson has found that when presented with consumption constraints, consumers fixate on fairness. Semi-structured in-depth interviews were conducted on 29 Australian consumers aged 18 to 85, at which point data saturation was reached. The participants in the study believed restrictions on content and higher pricing was discriminatory to Australians, making them feel like "second-class citizens". There was consensus among participants for equal and timely access to any content available to other consumers – a valid demand in a global economy. The perceptions of unfairness reinforce the consumer's belief that he or she is a victim. This mindset makes it easier for the consumer to overlook any harm incurred by the organisation when the consumer illegally circumvents these constraints. Confusion over the reasoning for such constraints also makes it difficult for the consumer to accept that they cannot attain their desired product or service. Parallel importation restrictions and technological protection measures that restrict arbitrage are not seen as fair by consumers. For example, electronically accessing products and services overseas is often likened to

1 Nicolas Suzor, "Access, progress, and fairness: rethinking exclusivity in copyright" (2013) 15(2) *Vanderbilt Journal of Entertainment and Technology Law* 297.

2 Choice, "Submission #075 to the Australian House of Representatives Inquiry into IT Pricing" (2013).

importing in that consumers do not draw a distinction between purchasing a product when visiting the U.S. and virtually purchasing it while still in Australia. When a consumer wants a product or service that can only be attained using illegal methods, the consumer will use justification techniques to reduce any psychological discomfort they feel when knowingly performing the infringing act.

One of the behaviours considered in this study as a means of circumventing constraints was creating a fake US iTunes account to access and pay for content not available in Australia. While there was confusion over the legality of this behaviour, there was consensus among participants that the behaviour was questionable but justified since the organisation still received payment. From the consumer's perspective, this payment mimics a standard exchange of goods for money, thereby overriding any perceived harm incurred by the organisation. "Money is what they [organisations] want... if you're not going to provide service I'm going to go take a different route to get something I want".³ In fact, participants rarely perceived any harm towards the organisation when engaging in this behaviour. Even individuals who did not intend to create the fake U.S. iTunes account understood this denial of harm rationalisation. Another behavior used to circumvent constraints is illegally downloading TV shows from the Internet for free, for personal consumption. For illegal downloading, the participants' justifications shift from denial of harm to denial of responsibility. Instead of a consumer taking responsibility for their illegal actions, denial of responsibility involves placing blame on the organisation and the unfair policies that ultimately leave consumers with no perceived alternative to fulfil their consumption demands. Both of these methods of circumventing consumption constraints are perceived by consumers to be low risk, prevalent in society, and easy to execute, which all seem to influence perceptions of acceptability, thereby legitimising them as perceived behavioural alternatives for the consumer. Creating a fake U.S. iTunes account is considered the better alternative to illegal downloading as the organisation still receives payment and the unacceptable acts underlying these behaviours are likened to lying and stealing, and lying is perceived to be more tolerable.

In a related subsequent quantitative study, 100 Australian consumers participated in a best-worst scale study using a balanced incomplete block design to assess degrees of deviant consumption behaviours. In this study, creating a fake U.S. iTunes account to access and pay for content not available in Australia was deemed the second 'most acceptable' behaviour out of the ten tested. The most acceptable behaviour was using a 4 cent fuel voucher from the grocery store to buy petrol. Illegally downloading TV shows from the Internet for free, for personal consumption was ranked fifth on the list, with very little variation between it and the behaviours ranking third (Returning merchandise to a store by claiming it was a gift when it was not) and fourth (Saying there are only 2 people staying in a holiday apartment when there are really 4). The legal behaviours considered more deviant than illegally downloading TV shows were: lying about a child's age in order to get a discount and not saying anything when the waitress miscalculates the bill in your favour. The outcome of this study demonstrates that these two illegal methods of overcoming consumption constraints are perceived by the consumer to be acceptable if not justified.

Unfairly high prices undermine the legitimacy of copyright law

There is a severe danger that parallel importation restrictions and technological protection measures that operate to prevent Australian consumers from accessing digital media at a fair price undermine the legitimacy of Australian copyright law. The more that Australian copyright law is seen as anachronistic and supportive of perceived unfair business practices, the less likely it is to be followed. The apparently unjustifiable difference between prices in Australia and comparable European and US markets is likely to lead consumers to infringement. A recent report from the Social Science Research Council on copyright infringement in developing societies shows that

³ Respondent 3, Male 18-25 age bracket, 2012.

consumers will turn to infringement where reasonably priced options are not available.⁴ Many representatives of copyright industries consistently call for stronger copyright law and greater investment of public funds in copyright enforcement. At the same time, it has become apparent that by failing to provide reasonably priced, effective, and convenient legal distribution channels, some copyright owners are contributing to infringement and the growing disregard for copyright law. In this context, recent attempts by copyright owners to shift the burden of enforcing copyright law to taxpayers (through criminal copyright regimes) and to internet intermediaries (through litigation against ISPs⁵ and lobbying for graduated response regimes⁶) should be treated with strong skepticism.

Parallel importation restrictions should be removed

Restrictions on parallel importation entrench distribution monopolies and drive up prices for consumers. Higher relative prices are not just a distributional problem – they lower the availability and circulation of knowledge and culture through our society. In an age where it is increasingly important for Australia to grow its innovative capacity in order to compete internationally,⁷ unnecessarily restricting the flow of information is harmful. Parallel importation restrictions appear to benefit local distribution chains, but the evidence that they directly support local content producers appears to be weak. We agree with the submission by A/Prof Matthew Rimmer that

Parallel importation restrictions are anachronistic. The Australian Parliament should repeal all remaining parallel importation restrictions under Australian copyright law, in order to promote consumer choice, competition, and innovation.⁸

TPM provisions should not protect market segmentation

Technological Protection Measures (TPMs) were designed to protect the interests of copyright owners by limiting the ability of users to circumvent digital locks on copyright content. The theory is that without a technical means of locking up copyright material, no trade in digital goods could be sustainable. Because the locks applied are often trivial to bypass, legal regulation was considered necessary to prevent the trade in circumvention tools and circumvention services and, eventually, actual acts of circumvention by end users.

The reality of TPMs has turned out much differently. TPMs now appear to impose significant costs on legitimate but technically unsophisticated users. They prevent users from making backups of their software as permitted by the copyright act.⁹ They prevent blind people from using software to read books aloud.¹⁰ They cause untold headaches for consumers who purchase content only to find that the copy protection software is faulty, rendering their purchase useless. If and when Australia introduces new copyright exceptions to allow commonplace activities like making backups of digital copies of films, books, games, and music; and making copies of each of these for viewing on portable devices or over cloud services, these activities will also be hampered by TPMs. They do not, however, prevent technically sophisticated individuals from breaking the locks and engaging in large-scale infringement.

4 See Joe Karaganis, *Media Piracy in Emerging Economies* (2011).

5 *Roadshow Films Pty Ltd v iiNet Limited* [2011] HCA 54 <<http://www.austlii.edu.au/au/cases/cth/FCA/2010/24.html>>.

6 Nicolas Suzor & Brian Fitzgerald, “The legitimacy of graduated response schemes in copyright law” (2011) 34(1) *University of New South Wales Law Journal* 1.

7 Cutler & Co, *Venturous Australia - building strength in innovation* (2008).

8 Matthew Rimmer, “Submission #092 to the Australian House of Representatives Inquiry into IT Pricing” (2013), 29.

9 *Copyright Act 1968* (Cth) s 47C.

10 N. Suzor, P. Harpur & D. Thampapillai, “Digital copyright and disability discrimination: From braille books to bookshare” (2008) 13(1) *Media and Arts Law Review* 1.

Most relevantly for this enquiry, digital locks enable publishers to segment the market, eliminate competition, and extract monopoly rents from Australian consumers. In *Stevens v Sony*, the Australian High Court vigorously rejected the proposition that protecting market segmentation was a legitimate purpose of Australian anti-circumvention law.¹¹ To the extent that the massive new powers granted to copyright owners through anti-circumvention law are justifiable, the High Court held that they must 'prevent or inhibit' copyright infringement. Using TPMs to segment the market and drive up prices was not a legitimate purpose which Australian civil and criminal law would protect. In that case, a digital lock that went too far – a lock that restricted legitimate parallel importation, rather than copyright infringement – was not protected as a TPM under Australian law.

After the introduction of AUSFTA, the Australian TPM provisions were strengthened to include devices that 'control access' to copyright works. In the course of introducing the new provisions, an exception was made to recognise the concerns of the High Court in *Stevens v Sony*. The new definitions of a 'technological protection measure' and the new 'access control technological protection measure' are limited to exclude region coding:

if the work or other subject-matter is a cinematograph film or computer program (including a computer game)--controls geographic market segmentation by preventing the playback in Australia of a non-infringing copy of the work or other subject-matter acquired outside Australia¹²

Unfortunately, the exception is based on old technology – the physical copy of a digital good. In the new digital distribution ecosystem, the publisher is in continual control of downloading and ongoing use of digital products. When consumers use sites like Steam, iTunes, or Amazon's Kindle store, they are locked in to whatever pricing and arbitrary control regimes the publishers and distribution intermediaries decide to implement. In this context, the operation of the TPM scheme needs to be fundamentally reconsidered.

Potential solutions

Competition is vital to keeping prices low enough to allow Australians to have access to digital cultural goods on fair terms. The recent trend has been towards the creation of locked digital ecosystems: phones locked to app stores, book readers locked to single retailers, music and films only playable on the retailing company's devices, computer games only available through a single digital distributor. One of the unfortunate results of this trend is to drive up prices for consumers and to enable publishers to exercise unprecedented control over how and where cultural goods are enjoyed. This is bad for three reasons: increased control over how media is used limits legitimate acts of consumption, expression, learning, sharing, and cultural play; increased prices and closed ecosystems limit consumer access to cultural goods; and perceived unfairness challenges the legitimacy of copyright law.

Increasing competition in digital markets is complex, but not impossible. There is an important role for the ACCC to play in ensuring that there is sufficient competition in distribution channels for digital goods. The strategy of giant digital distribution systems like iTunes and the Kindle store has been to vertically integrate their devices with their stores, such that consumers become relatively locked-in to their ecosystems. Effective competition requires that digital goods must be somewhat portable, and limiting the monopolies of distributors is critical for both consumers and the creators of digital content. Ensuring that distributors do not engage in anti-competitive behaviour is an important first step to increasing competition in the market for digital goods.

In order to increase competition, it is necessary to ensure some mobility in digital markets. Consumers should be able to access digital content from a range of suppliers, and creators should have a range of distribution channels available to them. Only through effective competition can the

¹¹ *Stevens v Kabushiki Kaisha Sony Computer Entertainment* (2005) 221 ALR 448 .

¹² *Copyright Act 1968* (Cth) s 10.

difficult balancing goal of copyright – to encourage investment at a level that maximises the flow of information – be achieved. This problem needs to be addressed holistically. Some options that should be investigated include:

- Ensuring that TPM law does not prohibit removing digital content from locked ecosystems. For example, books purchased on Amazon's Kindle store should be readable on any e-reader, and music purchased on iTunes should be playable on any capable device.
- Ensuring that contractual restrictions do not prevent competition or consumer rights through the terms of service. Steam, for example, allows users to purchase games to 'gift' to other users, but attempts to prohibit users from bypass regional pricing by transferring money to a person in another jurisdiction in exchange for a game. These contractual provisions – and termination of accounts and confiscation of legally purchased items that flow on from their breach – serve to limit competition. In some cases, they may be unfair terms under the Australian Consumer Law, but more investigation is required as to whether they ought to be enforceable.
- Repealing parallel importation laws.
- Introducing a legally protected right of digital resale. Resale is important to allow arbitrage in copyright markets. In a physical distribution model, competition is enhanced by people who purchase legitimate copies in one market for sale in another – subject to parallel importation laws. In a digital market, resale is generally an infringement of copyright. The lack of a robust secondary market entrenches the monopoly power of distributors. The lack of a market for used goods also greatly limits access in the digital economy – second hand retail stores provide a vital function in enhancing access to culture. A recent decision of the European Court of Justice has upheld the right of legitimate purchasers of digital content to resell it.¹³ The possibility of introducing a right of digital resale in Australia should be investigated.

13 *UsedSoft GmbH v Oracle International Corp*, Case C-128/11, Court of Justice of the European Union (3 July 2012) <http://curia.europa.eu/juris/documents.jsf?num=C-128/11>.