

## Submission to the ACCC's public consultation on the Draft ACCC Guidelines to assist the Copyright Tribunal in the determination of copyright remuneration - October 2018

### Introduction

1. Isentia Group Limited (**Isentia**) welcomes the opportunity to provide this submission to the Australian Competition and Consumer Commission's (**ACCC**) public consultation on its *draft ACCC Guidelines to assist the Copyright Tribunal in the determination of copyright remuneration* October 2018 (**Draft Guidelines**).
2. Isentia is an ASX listed Australian media intelligence company providing media monitoring services to its customers.
3. Isentia requires licences from copyright owners including, in relation to more than 90% of the content published by newspaper mastheads in Australia, from Copyright Agency Limited (**CAL**), a collecting society under the *Copyright Act 1968* (Cth), which grants a licence as an agent for CopyCo Pty Ltd, an incorporated joint venture, the shareholders in which are News Limited, APN Newspapers Pty Ltd (a subsidiary of News), Fairfax Digital Pty Ltd and Rural Press Pty Ltd (a subsidiary of Fairfax), and Bauer Media Pty Ltd.
4. Isentia therefore has an interest in the guidance provided by the ACCC to the Copyright Tribunal of Australia (**Copyright Tribunal**) under section 157A of the Copyright Act, in connection with the determination of fair, reasonable and non-discriminatory remuneration for licensors of copyright material.

### Executive Summary

5. As a copyright licensee which is highly dependent on licensing of copyright material on fair, reasonable and non-discriminatory terms, Isentia recognises the value of guidelines on matters relevant to the determination of reasonable remuneration and urges the ACCC to finalise and to make guidelines for the purposes of s157A.
6. There are well accepted bodies of law and economics concerning the fair, reasonable and non-discriminatory licensing of monopoly intellectual property rights from which the Copyright Tribunal would benefit in the form of guidance issued for the purposes of s157A of the Copyright Act.
7. In this regard, for the purposes of this consultation process, Isentia has engaged the services of an independent expert economist, Dr Christopher Pleatsikas, who has prepared a report outlining areas for further consideration in the Draft Guidelines, which is attached at **Annexure A**.
8. Isentia's three main areas for consideration and proposals to address them are as follows:
  - (a) **Overarching principle of bargaining power** - The main focus of the Draft Guidelines is to provide a framework to counter any market power held by collecting societies and providing material to assist parties preparing economic evidence to support their claims in the Copyright Tribunal.

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Isentia submits that the Draft Guidelines should more directly address the potential lack of bargaining power by licensees in negotiations with licensors (which can differ from considerations of market power) and implications of this on achieving an economically efficient licensing fee. The Draft Guidelines should include guidance for the Tribunal to examine the effects of bargaining power disparities, as well as considerations of market power, in the determination of licence fee disputes.

(b) **ACCC's pricing principles** - Isentia submits that:

- (i) *previous bargains* - the Draft Guidelines should account for the proposition that frequently (if not predominantly) previous bargains between a licensee and licensor may not be indicative of an economically efficient price (for example because of disparities in bargaining power or an exercise of market power). The problem of "boot-strapping" - where a licensor in subsequent fee negotiations seeks to increase fees based on previous bargains - should also be recognised in the Draft Guidelines. The Draft Guidelines should provide the guidance that the Tribunal should be especially slow to accept previous bargains as indicative of an economically efficient price in circumstances where no objective empirical method was used to determine the market value of the licensed property.
- (ii) *Recognition of a licensee's contribution* - In determining an economically efficient licence fee, the Draft Guidelines should make provision for due consideration to be given to the contribution by the licensee to an increase in the utilisation of the licensed property which in turn must increase the revenue streams available to licensors;
- (iii) *No basis for calculating licence fees on 'across-the-board' revenues* - the Draft Guidelines should clarify that there is no sound economic basis on which licence fees may be based on "across the board" revenues without determining first whether the revenue is directly referable to the licensed property in question. Even in circumstances where a licence fee is set at a relatively small percentage of the licensee's revenues, there is no economically sound justifiable reason, even on efficiency grounds, for determining a licence fee on this basis. Where a licensee provides other services or adds value in the services it supplies in a downstream market, fees should not be levied with respect to revenues from those value add services where fees have been paid on copyright material. The Draft Guidelines should also provide guidance that the Tribunal should take into consideration the impact of "royalty stacking" (where licensees may be required to pay other licence fees in order to offer to the market their goods and services) and its effect on reducing incentives for innovation.
- (iv) *Non-discriminatory licence fees* - the Draft Guidelines should direct the Tribunal to consider the issue of non-discrimination among licensees in establishing licensing fees. Non-discriminatory fee structures within a particular market would encourage a fairer and more sound level playing field. Moreover, high fixed fee structures are likely to disadvantage smaller market participants or new

- (v) entrants, whereas variable fee structures are more likely to give rise to a level playing field for market participants which will facilitate fairer markets and increase competition and market innovation.
  - (vi) *Other markets and jurisdictions* - rates in other jurisdictions for comparable schemes and rates for comparable bargains in other product markets can play an important role in benchmarking licensing rates, in particular where the licensor is a monopoly or near monopoly supplier of the licensed rights. Isentia recommends that the ACCC adopts a more positive approach to these as appropriate benchmarks in the Draft Guidelines.
- (c) Finally, set out in paragraph 27 below are some principles concerning transaction costs that are relevant when considering alternatives to blanket licence fees and the utility of survey evidence which Isentia considers are deserving of greater emphasis in the Draft Guidelines.

### ***Overarching Principles***

- 9. The ACCC's primary focus in the Draft Guidelines is on addressing disparities in market power between licensees and licensors.
- 10. Isentia does not disagree that this should be a key focus of the Draft Guidelines in seeking to determine a reasonable copyright remuneration.
- 11. However, Isentia considers that in addition to the focus on market power concerns, proper consideration should be given to a disparity in bargaining power between licensee and licensor. Failure to properly account for this disparity may potentially result in a remuneration structure that is at odds with the objective of an economically efficient remuneration for copyright material.
- 12. Isentia submits that the Draft Guidelines should more directly address the effects of a potential lack of bargaining power between licensee and licensor by giving guidance to the Tribunal to have explicit regard to the relative bargaining power of the parties and to take this factor into consideration in the determination of licence fee disputes.

### ***ACCC's Pricing Principles***

- 13. The ACCC notes in its Draft Guidelines that the Tribunal has considered a range of approaches in making pricing determinations, including benchmarking; construction of a hypothetical bargain and judicial estimation. Of these, the ACCC recommends benchmarking (by using appropriate rates as a source of information for determining remuneration) and construction of a hypothetical bargain (by applying an economic model to construct an appropriate licence fee level and structure).
- 14. Isentia does not disagree that these are the methods more likely to achieve an economically efficient remuneration fee for copyright materials. However, Isentia considers that in implementing these pricing approaches, the Draft Guidelines should give due regard to the following concerns.

#### *Previous bargains*

- 15. There may be circumstances where previous licence fees can be a good measure of economically efficient price. However, this is likely to be comparatively rare. Isentia

acknowledges that it would be prudent for the Draft Guidelines to properly account for the proposition that a previous licence fee between a licensee and licensor is not likely to be indicative of an economically efficient price. This may arise, in circumstances where there are disparities in bargaining position between the licensee and the licensor or indeed where the previous bargain between licensee and licensor was struck under conditions where the licensor was especially dependent on the licensee which was in a position to adopt a "take it or leave it" approach.

16. This problem is exacerbated in circumstances where there is no objective empirical method for estimating competitive market conditions for the purposes of determining competitive market value of the licensed property. Further, problems associated with benchmarking against previous licence fees may be amplified where collecting societies seek to continuously increase licence fees based on previous bargains struck where there is no objective, empirical basis for doing so.
17. As such, Isentia is of the view that the Draft Guidelines should provide guidance that the Tribunal should be especially slow to accept previous bargains as indicative of an economically efficient price in circumstances where no objective empirical method was used to determine the market value of the licensed property.

*Recognition of a licensee's contribution*

18. Isentia further submits that the Draft Guidelines make provision for due consideration to be given to the contribution by the licensee to an increase in the utilisation of the licensed property which in turn must increase the revenue streams available to licensors.

*No basis for calculating licence fees on 'across-the-board' revenues*

19. Licence fees should only be calculated on revenue derived by the licensee which is directly referable to the licensed property. Many licensees may already hold worldwide licenses that reflect rights to use licensed property on that basis. Other licensees may offer goods and/or services that are not directly referable to or do not directly use licensed property or may add value over and above the use of the copyright material in a downstream market. It would not be economically efficient for licensees in those situations to be charged a licence fee based on revenue without determining first whether that revenue is directly referable to the use of the licensed property for which a fee is charged.
20. Isentia submits that the Draft Guidelines should clarify that there is no sound economic basis on which licence fees may be based on "across the board" revenues, even when it is set at a relatively small percentage, without first determining whether the revenue is directly referable to the licensed property in question through a detailed examination of that use, excluding other services offered by a licensee including value added services for which it may charge its customers in a downstream market.

*Non-discrimination in licensing fee structures*

21. Isentia also considers that the Draft Guidelines should address the impact of licence fee structure on market participants. Isentia submits that standard, non-discriminatory fee structures within a particular market would encourage a fairer and more sound level playing field.
22. For example, a licence fee structure which involves, say, a fixed lump sum component and a percentage cost or variable cost component, might benefit larger or incumbent market participants, because the lump sum component may represent a smaller percentage of

their overall revenues. Whereas fixed and variable cost fee structures might disadvantage smaller market participants and indeed may stifle new entry and innovation. Therefore, in Isentia's view, fee structures which are more likely to give rise to a level playing field for market participants will facilitate fairer markets and increase competition and market innovation.

*Royalty stacking*

23. Additionally, Isentia considers that due regard should be had to the issue of royalty stacking, the concern here being that licensees may be required to pay other licence fees in order to offer to the market their goods and services. Royalty stacking may have the effect of reducing incentives for innovation.

*Rates in other jurisdictions and rates in comparable, more competitive markets*

24. The Draft Guidelines appear to adopt an overly cautious approach to the consideration, as an appropriate benchmark, licensing arrangements for comparable schemes in other jurisdictions and rates determined for licensing of copyright material in comparable, more competitive markets.
25. In Isentia's view, rates in other jurisdictions for comparable schemes and rates for comparable bargains in other product markets can play an important role in benchmarking licensing rates in particular where the licensor is a monopoly or near monopoly supplier of the licensed rights.
26. Isentia submits that the ACCC should adopt a more positive guidance to the Tribunal to the consideration of licensing arrangements for appropriately comparable schemes in other jurisdictions and rates determined for licensing of copyright material in comparable, more competitive markets in benchmarking licensing arrangements where cogent evidence of the comparability can be adduced. This may be achieved by containing some guidance in the Draft Guidelines on examples of and circumstances where comparable bargains should be taken into consideration by the Tribunal where such evidence is available.

***Principles for further development***

27. In addition to developing more fully the economic concept of bargaining power and the disparity between licensee and licensor as outlined above, Isentia submits that the following economic principles should be considered for further development in the Draft Guidelines:
- (a) ***transaction costs when considering alternatives to a blanket licence*** - while there may be some circumstances, including the example given at footnote 30 of the Draft Guidelines, where it is possible to readily benchmark a licence fee against the sum of individual licences that would otherwise be required, Isentia considers that caution should be expressed here because the negotiation of licences on a case-by-case basis directly with copyright owners may also be a costly exercise which may mean that the comparison is not appropriately like-for-like.
- (b) ***the usefulness of experimental data*** - the Draft Guidelines deal with both choice experiments and survey data. As presently drafted the Draft Guidelines suggest that survey data is inferior to other types of experiments. Given that the presentation of survey data is dealt with by the Federal Court of Australia's practice note, Isentia suggests that the Draft Guidelines be amended so as to reflect that survey data may permissibly be used and that guidance on the standards necessary for this purpose may be derived from the Federal Court of Australia's practice note.

**Isentia Submission**  
**Annexure A**

## **Expert Economic Comments on the Draft ACCC Guidelines**

**By Dr Christopher Pleatsikas**

### **I. Background and Qualifications**

1. I, Christopher Jon Pleatsikas, am an economist, living in Berkeley, California. I am a Vice President at Charles River Associates, an international economic, litigation support services and business strategy consulting firm, headquartered in Boston, Massachusetts. In the past I was co-Director of the firm's Asia-Pacific Competition Practice, based in Sydney.
2. I have been a Managing Director at the Berkeley Research Group and at LECG, LLC, both global economics and business strategy consulting firms. I have also been a Principal at Putnam, Hayes & Bartlett (now part of PA Consulting) and a Manager of the Economic Analysis Unit at Price Waterhouse (now part of PricewaterhouseCoopers). I have also been a Distinguished Lecturer/Lecturer in the Economics Department of the University of California, Santa Cruz.
3. I received a B.A. from the University of Pennsylvania, as well as an M.S. in Natural Resources from the University of Vermont and a Ph.D. in Regional Economic Analysis from the University of Pennsylvania. In addition to teaching industrial organization (competition economics) at the University of California, I have taught economics and quantitative methods at both the University of Pennsylvania and the University of Maryland.
4. My particular areas of expertise are industrial organisation, competition policy, intellectual property analysis, regulation, and microeconomics. I have extensive experience in Australia, as well as in New Zealand, the United States and Europe.
5. I have testified before and submitted testimony to the Australian Federal Court and the Australian Competition Tribunal, as well as the Australian Copyright Tribunal, state and federal courts in the United States and courts in New Zealand and the Republic of Singapore. I have also testified under Australian Federal Court rules in several private

arbitrations in Australia. I have been engaged by private clients and by antitrust regulators, including the Australian Competition and Consumer Commission.

6. I have authored and co-authored a number of papers. For example, I have authored and/or co-authored articles on market definition, on the competitive effects of long-term contracts, on piracy of intellectual property, on predatory pricing and on the problems encountered in competition analysis. I am also editor of the “Report from North America,” a column on antitrust developments published regularly in the *Australian Journal of Competition and Consumer Law*.
7. I have been asked to review the “Draft ACCC Guidelines to assist the Copyright Tribunal in the determination of copyright remuneration,”<sup>1</sup> for the purpose of providing my comments from an economist's perspective on the Draft Guidelines. All of the opinions expressed in this report are my own. I have particularly focused on “Part B: Pricing Principles”<sup>2</sup> because that part of the Draft Guidelines discusses economic principles.<sup>3</sup>
8. My report is organized as follows:
  - (a) Section II discusses my opinion concerning the importance of due consideration of relative bargaining power of the parties as an overarching principle that should be addressed in the Draft Guidelines (in addition to considerations of market power);
  - (b) Section III contains my opinion on additional principles that are not, in my view, adequately addressed in the Draft Guidelines. Those principles include:
    - i. problems with using previous license fees as an economically efficient price benchmark;
    - ii. lack of consideration of the contribution by licensees to the utilization of licensed property in determining license fees;
    - iii. problems associated with license fee structures including problems that arise when applying license fees to "across the board" revenues;
    - iv. problems of “associative dissonance/associative bias” in setting license fees;
    - v. the practice of "royalty stacking" and its impact on incentives for innovation;

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<sup>1</sup> Hereinafter referred to as the “Draft Guidelines”.

<sup>2</sup> I.e., Sections 4 through 6 of the Draft Guidelines.

<sup>3</sup> The stated objective of Draft Guidelines is the determination of an economically efficient remuneration policy for Copyright materials. See Section 4, pp. 19-20, of the Draft Guidelines.

- vi. the objective of non-discrimination in establishing license fee structures; and
  - vii. the utility of the Tribunal's consideration of evidence of comparable schemes in other jurisdictions and rates in comparable, more competitive markets.
- (c) Section IV contains my specific comments on areas that in my opinion could benefit from further development in the Draft Guidelines; and
- (d) Section V contains my recommendations which, if implemented, would address the concerns I have raised in my report.

## **II. Lack of Consideration of Bargaining Power Disparities**

9. In my opinion, the Draft Guidelines do not adequately consider the implications of disparities in bargaining power between licensors and licensees. Instead, the primary focus of the Draft Guidelines is on disparities in market power between licensor and licensee. While the existence of a monopoly licensor is clearly problematic for the establishment of an economic efficient licensing fee for the copyright material of interest, it is not the only important bargaining problem that occurs. In many or even most cases, there is also a bargaining power disparity that would make it difficult to achieve an economically efficient outcome. Bargaining power disparities may be as or even more important than market power disparities in making it difficult or impossible to agree on an economically efficient license fee.

### ***Bargaining Power and Market Power***

10. To some extent the apparent greater emphasis on market power and not bargaining power in the Draft Guidelines may derive from the somewhat subtle distinction between the two concepts. While these two concepts may be related in many circumstances, market power applies across a relevant market, while bargaining power refers to a disparity in leverage in a negotiation between two specific parties, often parties that operate in separate markets.<sup>4</sup> It is likely that bargaining power disparities will be substantial in favor of the licensor in at least many copyright licensing negotiations.
11. For example, the likelihood of equality of bargaining power is low in situations where the licensor is a monopolist and the licensed property itself is not the main source of

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<sup>4</sup> There may be some ambiguity in the Draft Guidelines in the distinction between market power and bargaining power. See p. 20 of the Draft Guidelines.



income for the licensee but the licensed property is an inherent input into the products marketed by the licensee.<sup>5</sup> The fact that the stream of income at risk to the licensee is much larger than for the licensor if no license is agreed significantly exacerbates the potential for a disparity in bargaining power between the parties (in favor of the licensor). In addition, bargaining power disparities may arise when a licensor is not necessarily compelled to license to a particular party or a particular set of parties, but the licensee(s) must license the copyrighted materials in order to conduct its (their) business. Finally, there may be significant disparities in bargaining power where the licensee faces competition from other licensees and the licensor is a monopolist. In fact, multiple sources of bargaining power disparities (in favor of the licensor) may characterize copyright licensing negotiations in many circumstances.

12. The existence of bargaining power disparities would, all else equal, make it unlikely that negotiated licensing fees would reflect economically efficient prices. Failure to acknowledge the impact of bargaining power disparities could make it more difficult for litigated licensing fees to reflect economically efficient prices.
13. Furthermore, even in situations where bargaining power may be reasonable equal, this does not guarantee that a competitive market price will be established, as when the negotiation involves two firms with significant market power in their respective markets. For example, market failure is likely the norm in situations in which there is a monopoly licensor. Even in situations where the licensee is a monopsonist purchaser, it is a well-accepted tenet in economics that bilateral monopoly does not generally result in an economically efficient price.
14. For these reasons, a primary emphasis on market power disparities without due consideration of bargaining disparities is not appropriate for determining an economically efficient remuneration scheme for copyright materials. By the same token, the more competitive the market in licensed property (i.e., the more competitive the market on the supply side of the copyright material), the more likely, all else equal, that comparative bargains will be an appropriate guide to economically efficient license fees.

### **III. Other Overarching Principles That Are Not Sufficiently Addressed**

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<sup>5</sup> See also p. 20 of Draft Guidelines

### *Use of Previous Licensing Fees*

15. As noted above, merely because a previous license fee was negotiated between a licensor and a licensee does not necessarily imply that it is equivalent to an economical efficient price, particularly when it was negotiated under the threat of litigation and particularly when there were bargaining power disparities that characterized the previous negotiation. The problems with utilizing previous negotiated rates is especially acute in situations where no objective empirical<sup>6</sup> methods for estimating competitive market license fees were utilized to determine the market value of the licensed property.
16. The problems in using previous established rates more generally can be magnified when so-called “bootstrapping” is the basis for collecting society licensing strategies. Bootstrapping occurs when collecting societies in subsequent negotiations seek to continuously increase license fees based on previous bargains they struck or bargains struck by other collecting societies and where no objective, empirically-derived (i.e., based on empirical data on value to users) standards for license fees exist.

### *Contribution by the licensee to licensor's revenue streams should be recognized*

17. Due consideration should be given in establishing economically efficient license fees to the contribution by the licensee to an increase in the utilization of licensed property and the revenue streams available to the licensors. In many cases the efforts of the licensee to utilize the copyright material will directly benefit the licensor through an increase in other income streams available to the licensor (e.g., the licensee’s promotion of a particular song may increase the popularity of both the song and the artist that performs it, thereby contributing to the success of the artist’s concert tours; alternatively, the promotion of licensed written materials by the licensee may contribute to greater traffic on the licensor’s website, which, in turn, may increase advertising revenues derived from the licensor’s website).

### *“Across-the-board” license fees may not be appropriate*

18. License fee rates should only be applied to those activities for which the licensee utilizes the licensed property. Many licensees either (1) have licenses that may already reflect rights to use licensed property (e.g., worldwide licenses) and/or (2) may offer goods

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<sup>6</sup> Empirical in this context implies that data-driven analyses to establish the value to users have been conducted, not just that comparisons with previous license rates have been performed.

and/or services that do not utilize the licensed property in question at all or may offer goods and services that may use the licensed property but also supply other goods or services (i.e., ancillary and/or value-added services). Applying a license fee on an across-the-board basis to all of the licensee's products and/or revenues in either or both situations is not likely to be economically efficient (e.g., because it may artificially inflate the marginal cost of goods or services that should not incur a license fee) and therefore not appropriate. License fees should only be applied to goods and services that use the licensed property directly. In cases where license fees are warranted where some licensed property may be used but other value-added or ancillary services are supplied in addition, either no license fee or reduced license fee rates may be appropriate.

19. Applying full license fees across-the board and/or to ancillary or value-added services would increase marginal costs above the efficient level. If marginal costs are set above the efficient level (e.g., when a license fee is charged for inputs that are either already licensed through another source or for inputs do not require a license at all or should only be charged a license fee at a reduced rate), it is likely, all else equal, that some economically efficient sales will not be made. That is, some buyers who place a marginal value on the product at least equal to the efficient level of marginal costs will be precluded from buying the product (because marginal costs will be set too high). A reduction in economic efficiency would inevitably result from such a policy.

***Problems stemming from “associative dissonance/associative bias”***

20. In the absence of empirical methods for establishing value, it is likely that license rates may suffer from a phenomenon that could be termed “associative dissonance” or “associative bias”. This problem is particularly acute in situations where the licensee's products incorporate the licensed property as an incidental element in its products or even as just one element in a multi-faceted good or service that incorporates many elements that are not licensable by the specific collecting society of interest (e.g., video entertainment that also includes some music elements). The problem of associative dissonance or associative bias manifests itself in a view that, as long as the license fee is a relatively small percentage of licensee revenues, it should be presumptively viewed as “reasonable” (because it will not have a large impact on costs). However, there is no necessary relationship between a license fee that is a relatively small percentage of licensee's revenues and the value that the licensed property actually contributes to the

licensee's revenues. That is, just because a license fee is set at a relatively (in absolute terms) small percentage of the licensee's revenues, there is no reason to believe it is economically efficient.

***Problems with Royalty stacking***

21. A related problem that should be considered in setting license fees is known as “royalty stacking” (or in the context of patents, “patent thickets”). Due consideration should be given to the other royalties that the licensee may be required to pay for and access to other licensed property that may be required in order to offer relevant goods or services. Royalty stacking can result in excessive royalties that can reduce incentives for innovation and increases in quality and even make it unprofitable for the licensee to offer goods or services.

***Non-discriminatory licensing fee structures***

22. In addition, the Guidelines should consider the issue of non-discrimination in establishing license fees. Non-discrimination has become an accepted principle in the establishment of standards-essential patents and is a useful concept for application in the licensing of copyright materials. For example, discriminatory licensing fee structures in the form of high fixed fees may disadvantage smaller competitors and entrants and favor larger incumbents. Discrimination in licensing fees may also, in some circumstances, discourage innovative products or innovative service providers.

***Utility of comparable schemes in other jurisdictions and rates in comparable, more competitive markets***

23. Sections 5.4 and 5.5 of the Draft Guidelines briefly discuss benchmarking in other jurisdictions and in more competitive licensing circumstances. While I recognize that there may be some circumstances in which such benchmarks may not be useful for setting economically efficient licensing fees in Australia, these benchmarks may provide useful guidance in many circumstances. In my opinion, the discussion of these topics in the Draft Guidelines is too brief and too vague to provide useful guidance to the Copyright Tribunal. It would be more useful to cite examples where such benchmarks have provided useful guidance. More useful still would be the development of criteria that

would assist the Tribunal in evaluating when and to what extent such benchmarks may be useful guides in establishing license fees.

#### **IV. Specific Comments on Information in the Draft Guidelines**

24. Despite inadequate or no consideration of the preceding overarching principles, the Draft Guidelines do contain many useful insights some of which may benefit from even greater emphasis. These include:

- (a) The observation that “Market power may affect rates even if those rates are determined by arms-length negotiation between the collecting society and licensee(s)”.<sup>7</sup> Of course, as stated above, bargaining power disparities may be even more important in distinguishing between rates that are likely to be economically efficient and those that are not.
- (b) The Draft Guidelines note that stated preference and contingent valuation methods do tend to be problematic in their application.<sup>8</sup> There is a vast body of literature on the subject that is relevant to determining whether and to what extent the problems inherent in many of the applications of these methods may have been substantially ameliorated or even cured in any particular circumstance. Where such methods are well-designed they may well be useful tools for analyzing value.
- (c) Non-user WTP (willingness-to-pay) probably is not useful for the determination in calculating license fees, at least in most instances.<sup>9</sup> There should be a presumption that an unwillingness to take up a license is an indication that the license rates exceed the perceived value of the copyright material to the non-user. Of course, there is a different question as to whether the reason for an unwillingness to license is that the license fee has been set higher than an economically efficient level. If so, it could be economically efficient to set a lower license fee (as users who might be willing to pay a price equivalent to or greater than the economically efficient price may be excluded from use).
- (d) A key issue in WTP estimation is the correct specification of the next best alternative.<sup>10</sup> Proper specification of the next best alternative may be straightforward in some cases or very difficult in others. However, just because the alternative specified may not be quite as good as the next best alternative is not necessarily an appropriate reason to exclude information provided. A decision of the usefulness of the information provided should be determined on a case-by-case basis.

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<sup>7</sup> P. 20 of the Draft Guidelines.

<sup>8</sup> Pp. 24-25 of the Draft Guidelines.

<sup>9</sup> P. 27 of the Draft Guidelines.

<sup>10</sup> P. 27 of the Draft Guidelines.

- (e) Consumption of licensed copyright material is generally non-rivalrous and marginal supply costs are generally low or essentially zero.<sup>11</sup> These facts should inform the decision to set license fees, particularly for innovative uses, as they imply that economically efficient fees (possibly excluding incentive effects for creating the copyright material<sup>12</sup>) are low.

25. In addition to the many useful observations included in the Draft Guidelines, there are some observations where the Draft Guidelines appear to deviate from economically sound argument. Specifically:

- (a) The Guidelines tend to understate the potential magnitude of transaction costs when discussing alternatives to a blanket license.<sup>13</sup> For example, the negotiation of individual licenses on a case-by-case basis directly with copyright material developers and/or their representatives may be relatively costly.
- (b) There may be insufficient consideration of the usefulness of experimental data, which may often be obtained at relatively modest cost, in determining the value of licensed property. Properly constructed experiments may be an innovative and cost-efficient way to empirically estimate the value of licensed property to the licensee.<sup>14</sup>
- (c) Calculating economic surplus associated with copyright material can be an extremely difficult proposition.<sup>15</sup> It may be particularly difficult when alternatives to use of the licensed property are difficult to conceive or are relatively poor substitutes. Likewise, option values may be difficult to calculate.<sup>16</sup>
- (d) One could imply a perfection bias in some of the comments about the utility of surveys.<sup>17</sup> One must not let the perfect be the enemy of the good when trying to utilize empirical data to infer value. Merely because a more perfect survey and/or experimental design is possible (or conceivable), one should not discard the results of a less perfect (but perhaps more practically feasible) option.
- (e) As stated in the Section dealing with overarching principles that are not well-addressed (or addressed at all) in the Draft Guidelines, there is no reason to presume that bargaining power is more or less equal between licensor and licensee.<sup>18</sup> Any conclusion on this factor would have to be situation-specific. In

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<sup>11</sup> P. 27 of the Draft Guidelines.

<sup>12</sup> There is no well-established benchmark that has determined the economically efficient license fees required to incentivize copyright material developers to create copyright material. However, some observers believe that the economically efficient monetary fees required are low, given the other creative benefits derived by copyright material developers.

<sup>13</sup> P. 21 of the Draft Guidelines.

<sup>14</sup> See Section 6 of the Draft Guidelines., but the ACCC does mention choice models, which can be the subject of economic experiments. P. 25 of the Draft Guidelines.

<sup>15</sup> P. 23 of the Draft Guidelines.

<sup>16</sup> P. 27 of the Draft Guidelines.

<sup>17</sup> P. 25 of the Draft Guidelines.

<sup>18</sup> P. 28 of the Draft Guidelines.

my opinion, it is unlikely that bargaining power equality will prevail in most copyright licensing situations.

## V. Recommendations

26. Having regard to the matters I have set out above, and based on my experience as an economist, I consider that it would be appropriate for the ACCC to adopt the following recommended changes and/or additions to the Draft Guidelines.
- (a) In my opinion, the Guidelines should include an analysis of the implications of bargaining power disparities for achieving economically efficient licensing fees and the need to evaluate how these disparities may affect both current negotiations and license fees agreed/established in the past. Furthermore, the Guidelines should direct that an analysis of bargaining power disparities be undertaken as part of the adjudication process for determining license fees.
  - (b) The Guidelines should make it clear that, even in situations where there is a monopolist licensor and a monopsonist licensee, bargaining power disparities may still exist and, even if they do not, prices negotiated under bilateral monopoly are not generally economically efficient.
  - (c) The Guidelines should explicitly recognize that negotiated rates that do not rely on objective measures of value are not necessarily economically efficient and that “bootstrapping” strategies may be problematic from the perspective of establishing economically efficient licensing fees.
  - (d) The contribution by the licensee to the licensor’s revenue streams should be explicitly recognized as a factor to consider in setting economically efficient licensing fees.
  - (e) The potential problems in utilizing “across-the-board” licensing fees should be discussed in the Guidelines. These include charging license fees on ancillary or value-added services that do not use the relevant license property at all or charging full rates for license fees where some licensed property may be used but other ancillary or value-added services are also supplied.
  - (f) Potential problems stemming from “associative dissonance/associative bias” and royalty stacking should be discussed in the Guidelines.
  - (g) The Guidelines should recognize the establishment of non-discriminatory licensing fee structures as an appropriate objective.
  - (h) Sections 5.4 and 5.5 of the Draft Guidelines, which discuss the use of benchmarks from other jurisdictions and/or more competitive licensing circumstances should be considerably bolstered by examples or, even more relevantly, the development of criteria that could be utilized by the Tribunal to determine under what circumstances and to what extent these benchmarks would be useful. As these Sections currently stand, they provide virtually no guidance.

- (i) The Draft Guidelines should be revised to provide additional guidance on the use of alternatives to a blanket license and on the use of experimental data for valuation of copyright materials. In addition, I would suggest that comments regarding economic surplus and option values be expanded so that the Tribunal has better guidance on when and how such methods might be useful. Finally, in my opinion, the problem of perfection bias in empirical methods should be explicitly addressed.