

# The Levy Runs Dry

## A Legal and Economic Analysis of EU Private Copying Levies

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**Abstract:** This article provides a legal and economic analysis of private copying levies in the EU, against the background of the Copyright Directive (2001/29), a number of recent rulings by the European Court of Justice and the recommendations presented by mediator Vitorino earlier this year. It concludes that notwithstanding these rulings and recommendations, there remains a lack of concordance on the relevance of contractual stipulations and digital rights management technologies (DRM) for setting levies, and the concept of harm. While Mr Vitorino and AG Sharpston (in the Opinion preceding *VG Wort v. Kyocera*) use different lines of reasoning to argue that levies raised on authorised copies would lead to double payment, the Court of Justice's decision in *VG Wort v. Kyocera* seems to conclude that such copies should nonetheless be levied. If levies are to provide fair compensation for harm resulting from acts of private copying, economic analysis suggests one should distinguish between various

kinds of private copies and take account of the extent to which the value said copies have for consumers can be priced into the purchase. Given the availability of DRM (including technical protection measures), the possibility of such indirect appropriation leads to the conclusion that the harm from most kinds of private copies is *de minimis* and gives no cause for levies. The user value of copies from unauthorised sources (e.g. from torrent networks or cyber lockers), on the other hand, cannot be appropriated indirectly by rightholders. It is, however, an open question in references for preliminary rulings pending at the Court of Justice whether these copies are included in the scope of the private copying exception or limitation and can thus be levied for. If they are not, as currently happens in several EU Member States, legal and economic analysis leads to the conclusion that the scope of private copying acts giving rise to harm susceptible of justifying levies is gradually diminishing.

**Keywords:** Private Copying, Exception or Limitation, Levies, Fair Compensation, Harm, Technological Protection

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### A. Introduction<sup>1</sup>

<sup>1</sup> In 1965, Germany was the first country to introduce a private copying (PC) levy on sound and video recording equipment, following landmark decisions by the German Federal Supreme Court between 1955 and 1964, namely in the *Grundig Reporter*<sup>2</sup> and *Personalaus-*

*weise*<sup>3</sup> cases.<sup>4</sup> In the ensuing decades, many countries followed suit and levies were introduced on a variety of recording or copying devices and blank media. At the present day, most countries within the European Union (EU) have some form of copyright levies, as well as the United States, Canada, Russia and several

countries in Latin America and Africa. In Asia, Japan is the only country with copyright levies.<sup>5</sup>

- 2 PC levies have long been one of the most hotly debated topics in EU copyright law and policy. It is a common area for discussion between rightholders, collective rights management organizations (CMOs), the consumer electronics and ICT industries and even consumer representative associations. At the EU level, PC levies have been on the harmonization agenda since the 1988 Green Paper on Copyright and the Challenge of Technology<sup>6</sup> and, following stakeholder consultations (in 2006 and 2008)<sup>7</sup> and the 2011 IPR Strategy,<sup>8</sup> remain an “on-going initiative” of D.G. MARKT.<sup>9</sup>
- 3 Notwithstanding the perennial attention for levies, in 2013 a number of developments came together which could lead to a leap forward in this debate. In January of this year, Mr António Vitorino, appointed in late 2011 by Internal Market Commissioner Michael Barnier as mediator to lead a stakeholder dialogue in this field, delivered his recommendations on the matter (hereinafter, the “**Recommendations**”).<sup>10</sup> The Commission has made clear that reform in this field is necessary from the single market perspective and presented the Recommendations as “non-binding provisions”.<sup>11</sup> However, despite these having merited discussion in the latest “competitiveness” meeting of the Council of the EU, there is no indication of legislative action in the field for 2013, as previously promised for 2012 in the IPR Strategy.<sup>12</sup>
- 4 This institutional backdrop is complemented by a confusing extant legal regime at the European level – namely, in what concerns the rules of the Copyright Directive on fair compensation for the private use exception or limitation<sup>13</sup> – which has spawned not only a number of divergent national implementations, but also a considerable number of European Court of Justice (ECJ) judgements and (a multitude of) pending preliminary references from national courts on the interpretation of said provisions.<sup>14</sup>
- 5 This article explores the current EU secondary law landscape on PC levies, with a special emphasis on the economic analysis of some of its most disputed issues, such as the correct definition of the concept of harm, the effect of authorisation acts by rightholders and the application of digital rights management (DRM) technology – in particular, technological protection measures (TPMs) – on the condition of fair compensation and its calculation, as well as its relationship with unauthorised file sharing on the Internet.
- 6 In order to do so, following this introduction, **Part B** provides a detailed and updated legal background on the framework of rules applicable to PC under the *acquis communautaire*.<sup>15</sup> It examines the relevant legal provisions in the Copyright Directive, as well

as the recitals commonly used to interpret them. It goes on to examine the multiple ECJ judgements that have attempted to fill gaps in the legal regime and interpret the provisions in question. This is complemented by a succinct overview of forthcoming ECJ cases that will address some of the remaining and still controversial aspects. **Part C** critically examines the Vitorino Recommendations against the extant legal regime and interpretation thereof by the ECJ, as well as economic arguments, thus highlighting its virtues and shortcomings. **Part D** facilitates the transition to economic analysis by establishing the baseline of the application of PC levies in Europe. **Part E** conducts the economic analysis proper. It provides a typology of PC acts, examines the concept of harm against that of indirect appropriability, and discusses the effect of DRM in the PC exception or limitation as well as in the calculation of levies. **Part F** concludes that the case for levies to compensate for harm caused by “classical” private copies is gradually diminishing as the utility consumers derive from offline private copies can to a large extent be appropriated indirectly. The choice *not* to apply TPMs is nowadays a rational choice that, from an economic perspective, should not be treated differently from the choice to apply TPMs or any other sort of DRM.

## B. Mapping the legal background

### I. The legal framework

- 7 The purpose of this part is to provide an updated overview of the legal framework applicable to PC at the secondary law level in the EU. As such, this part does not attempt an in-depth analysis of all the dimensions and nuances of the legal regime of this exception or limitation. This mapping exercise intends to shed light on some of the most relevant problems with extant legal rules, so as to subsequently introduce economic arguments that can assist in its elucidation. With that objective, this part looks first at the legal context of the exception, followed by an examination of its requirements.<sup>16</sup>

#### 1. The context of the private copying exception or limitation

- 8 Secondary European copyright law is constituted by a body of directives aimed at harmonizing the field, the so-called *acquis communautaire*. Under the *acquis*, it is possible to identify economic substantive rights that are either exclusive or non-exclusive, in the sense that they do not entitle rightholders to prohibit a specific use but merely to a claim for remuneration or compensation.

- 9 The Copyright Directive, which implemented the WIPO Internet Treaties,<sup>17</sup> horizontally harmonized several economic rights – reproduction, communication/making available to the public and distribution – and adjusted them to the digital age.<sup>18</sup> The reproduction right is granted both to authors and related rights owners. Performers and broadcasters have a specific right of first fixation,<sup>19</sup> meaning that the general reproduction right applies only to the reproductions of those fixations.<sup>20</sup> The relevant international treaty provisions referring to this exclusive right<sup>21</sup> clarify that it applies without restriction in the digital environment – arguably including all forms of incidental, transient or technical copies.<sup>22</sup> Similarly, the Copyright Directive’s reproduction right increasingly applies to online dissemination of content, of which reproduction is an essential constituent. Such a broad interpretation is clear not only from the letter of Article 2 but also from ECJ decisions dealing with its scope, which seem to apply an expansive reading of the concept of reproduction,<sup>23</sup> coupled with a likewise ample concept of protectable subject matter (the “work”, understood horizontally as the “author’s own intellectual creation”).<sup>24</sup>
- 10 Notwithstanding, (primary) exclusive rights in the *acquis* are in certain instances limited in their scope by the application of non-exclusive (secondary) rights and, where relevant, accompanying exceptions or limitations. Non-exclusive rights can be conceptually divided into myriad dispersed harmonized rights of remuneration or fair compensation.<sup>25</sup>
- 11 Because PC involves acts of reproduction, it calls into application Article 2 of the Copyright Directive. This provision contemplates a broad exclusive right,<sup>26</sup> covering all digital reproduction acts made over the Internet, except transient copies; the latter are exempted by the sole mandatory exception/limitation in the Directive – Article 5(1)<sup>27</sup> – the main purpose of which is to enable transmission by Internet service providers or lawful use by end-users.<sup>28</sup> All remaining twenty exceptions or limitations in the Directive – which are listed *exhaustively* in Article 5(2)-(4) – are optional, including that for PC.<sup>29</sup> These optional exceptions apply to the reproduction right,<sup>30</sup> the distribution right<sup>31</sup> and the rights of communication/making available to the public.<sup>32</sup> Where Member States chose to implement such optional exceptions, certain provisions are conditional upon the grant of fair compensation – Article 5(2) (a), (b) and (e) – while others do not come with such conditions, though it is possible that national law provides for such compensation.<sup>33</sup> Furthermore, all exceptions are subject to the Directive’s version of the three-step test in Article 5(5).<sup>34</sup>

## 2. The requirements of the private copying exception or limitation

- 12 This Article focuses on the right to fair compensation for reproductions covered by the PC exception or limitation. This right is prescribed for in Article 5(2)(b) of the Copyright Directive, which states that:

*[... M]ember States may provide for exceptions or limitations to the reproduction right [...] in respect of reproductions on any medium made by a natural person for private use and for ends that are neither directly nor indirectly commercial, on condition that the rightholders receive fair compensation which takes account of the application or non-application of technological measures referred to in Article 6 to the work or subject-matter concerned.*

- 13 It is fundamental to understand the basics of the meaning and scope of this exception, so as to highlight the problems that underlie PC levy systems.<sup>35</sup> For that purpose, the following paragraphs will look at the legal requirements for PC, as they result from the text of the Directive and its Recitals.
- 14 First, its scope encompasses reproductions made on all technologies and media – whether analogue or digital.<sup>36</sup> Second, it applies to acts of reproduction of all subject matter (despite Recital 38 mentioning solely audio, visual and audio-visual material), with the exclusion of computer programs and databases.<sup>37</sup>
- 15 Third, the exception is purpose-bound in the sense that it applies only for *private use* and for *non-commercial ends*. Although there is no definition of what “private” is in the Copyright Directive, there is rough consensus that the beneficiaries of this provision must be *natural persons* making reproductions for their *personal purposes* and within the *private sphere* which, depending on the national implementation, may include a broader or narrower circle of (close) family and friends.<sup>38</sup> This would mean, in principle, that other related but potentially broader concepts in national law – such as “personal use” and “own use” (which may include professional and commercial use) – fall outside the scope of the provision.<sup>39</sup> Also, given that only reproductions by a natural person are allowed, acts carried out by the latter on behalf of a legal person are not exempted.<sup>40</sup> However, this does not mean that reproductions made by natural persons on behalf of another individual and/or for her private use are not allowed (as long as with non-commercial purpose), as these might fall in the private use category.<sup>41</sup> More problematic is the case of third-party copying by a legal person acting as a commercial provider that facilitates PC by a natural person for private purposes; here, it seems that Member States must regulate the effect of the intervention of intermediaries and service providers in the reproduction act.<sup>42</sup> To be sure, such leeway has led to divergent national implementations on the issue of third-party copying.<sup>43</sup> This brief sketch

is enough to highlight the potential legal certainty challenges facing national courts in defining what “private” means in this context, especially in light of its potential expansion in the digital environment (e.g. within social networking platforms) and in opposition to a dynamic concept of *public* in the *acquis*.<sup>44</sup>

- 16 Closely related to the private nature of the use is another *cumulative* requirement as to the purpose of the reproduction: it cannot be for *directly or indirectly commercial* ends.<sup>45</sup> Again, the scope of this requirement is not made clear by the wording of the Directive and is further confused by the fact that – whilst private acts are by definition non-commercial – non-commercial acts can fail the qualification as private.<sup>46</sup> Put differently: in mathematical terms, private acts are a subset of the set of non-commercial acts. The definition of commercial can encompass a wide range of meanings – from “commercial”, “economic”, “for profit”, “business” and the like – while the scope of non-commerciality is complex to define, especially in connection to online uses.<sup>47</sup> At the very least, it seems that the term *commercial* cannot be a synonym for *economic*, let alone welfare economic. This is because a PC exception excluding all welfare economic significant uses would be devoid of meaning and scope, as every PC act bears such a significance or consumers would not engage in them. Beyond that, it seems difficult to clearly define the scope of commerciality here. National legislators and courts have attempted to do so by setting forth subjective and objective criteria: the *infringing intent* of the copier (actual or constructive knowledge, linked to the profit-making aim) and the definition of a specific number of copies beyond which PC is not acceptable.<sup>48</sup> It is, however, difficult to transpose these criteria to define indirect commerciality in digital PC.<sup>49</sup>
- 17 Fourth, where the national legislator implements a PC exception or limitation, such an implementation must be accompanied by the provision of fair compensation, aimed at compensating authors for the harm caused by unauthorised reproductions. The meaning and scope of this requirement, as interpreted by the ECJ, are discussed in greater detail below.<sup>50</sup>
- 18 However, it bears mentioning from the outset **Recital 35**, which states that fair compensation is aimed at compensating rightholders “adequately for the use made of their protected works”. It adds that the determination of the “form, detailed arrangements and possible level of such fair compensation” must take into consideration the “particular circumstances of each case”. These should be evaluated according to several criteria, with a valuable one being the “possible harm to the rightholders resulting from the act in question”. The recital goes on to address cases where rightholders have already received payment in a form other than the fair compensation (e.g. via a license fee), raising the possibility that such cases might not give rise to separate (and hence double) payment. Regarding the *level* of fair compensation, “full account” must be taken of the “degree” of TPM usage; furthermore, in “certain situations where the prejudice to the rightholder would be minimal” (*de minimis*), no obligation to pay fair compensation may arise.<sup>51</sup> This recital, by linking fair compensation to a notion of harm, distinguishes it from the concept of equitable remuneration,<sup>52</sup> which is based on the value of the use in trade.<sup>53</sup>
- 19 Pursuant to Article 5(2)(b), the method for calculation of the amount of fair compensation must take into account whether the rightholder of the work or subject matter susceptible of reproduction has applied to the same any TPMs referred to in Article 6 of the Directive. This article instructs Member States to provide adequate legal protection against the circumvention of any effective TPMs, i.e. “any technology, device or component that, in the normal course of its operation, is designed to prevent or restrict acts, in respect of works or other subject-matter, which are not authorized by the rightholder”.<sup>54</sup> TPMs are *effective* when they provide rightholders control over the *access* to the work or to a *use* thereof.<sup>55</sup> *Access controls* are measures for protection of the work, such as encryption, scrambling or other transformation. *Use controls* refer to mechanisms that prevent, e.g., copies of the work from being made. The legal protection of TPMs is afforded both against circumvention and preparatory acts.<sup>56</sup>
- 20 Member States may limit the legal protection of TPMs by implementing *mandatory* measures regarding acts of circumvention in case rightholders do not implement such measures voluntarily. This is to ensure that rightholders make available to the PC beneficiary the means of benefiting from the exception (to the extent necessary for that purpose), *where that beneficiary has legal access to the work concerned*.<sup>57</sup> If legal access is a necessary requirement, it seems that the limitative measures in question can only target *copy control* TPMs. However, such measures cannot be triggered (i) if rightholders have already made PC acts possible, or (ii) vis-à-vis *copy control* TPMs that limit the number of reproductions made by users in accordance with such provisions.<sup>58</sup> Both voluntary and mandatory TPMs are afforded legal protection.<sup>59</sup>
- 21 **Recital 52** clarifies the Directive’s preference for the adoption of voluntary measures by rightholders, which Member States should promote; where no voluntary measures are taken, these should be imposed on rightholders, under the terms described above. Any measures (voluntary or imposed) must not only respect rightholders’ entitlement to use TPMs, but also “the condition of fair compensation under that provision and the possible differentiation between various conditions of use in accordance with Article 5(5)”.<sup>60</sup>



- 22 Furthermore, the Copyright Directive introduces a special rule for licensed interactive on-demand services.<sup>61</sup> According to the same, Member States are not allowed to implement measures limiting the effect of TPMs for purposes of enabling PC if the work in question is *made available online for interactive on demand transmission on agreed contractual terms*.<sup>62</sup> This allows for the elimination of the possibility to engage in PC by end-users where (i) the work is made available online, (ii) subject to specific licensing terms prohibiting those acts and (iii) accompanied by TPMs preventing them.
- 23 The principle at work here is that TPMs can theoretically be used to prevent or control acts of digital reproduction and subject them to additional payment by users (even where such acts would otherwise be lawful), a fact that would make indirect payment through a levy system unwarranted, insofar as there would be no unauthorised reproduction act and no harm to compensate.<sup>63</sup> To be sure, these considerations have raised an important discussion on the possibility of the “phasing-out” of PC levies in the digital environment.<sup>64</sup>

## II. ECJ case law

- 24 The ECJ has ruled on the definition of fair compensation for PC in Article 5(2)(b) of the Copyright Directive in *Padawan*,<sup>65</sup> *Stichting de Thuiskopie*<sup>66</sup> and, more recently, in joined Cases *VG Wort v. Kyocera*<sup>67</sup> (preceded by an Opinion by A.G. Sharpston<sup>68</sup>) and *Amazon.com v. Austro-Mechana*.<sup>69</sup> The combination of these four rulings provides a blueprint of fundamental aspects of the PC legal regime and fills some of its gaps, namely those relating to the meaning and scope of the concept of fair compensation, the criterion of harm, the effect of rightholders’ authorisation and TPM application in the right to fair compensation. This section looks in sequence at these topics.
- 25 Conversely, because it is outside of the questions examined herein, this article will not look at the parts of these judgements dealing with the *liability and effective burden of compensation*. Regarding this topic, it is sufficient to point out the general rule that, since the relevant harm is (likely) caused by the natural person engaging in PC acts, it is in principle this person that should be liable for financing the applicable fair compensation.<sup>70</sup> In practice, however, the identification of these end-users, the enforcement of this obligation and the minimal nature of each use are too complex and cumbersome.<sup>71</sup> The Copyright Directive recognizes as much, by allowing exceptions to the principle, such as the exemption from payment in cases of *de minimis* uses (cf. Recital 35, *in fine*) and, with the objective of financing fair compensation, the adoption of systems of PC levies (cf. Recital 38), imposed not on end-users but on intermediar-
- ies who either make digital reproduction equipment, devices and media available to the first or provide them with copying services.<sup>72</sup> Following this logic, *Padawan* has elucidated that PC levies cannot be applied indiscriminately to digital reproduction equipment/devices/media which are (i) not made available to private users, and (ii) reserved to uses with a different purpose than PC.<sup>73</sup>

### 1. Fair compensation as an autonomous concept of EU law and an unwaivable right

- 26 No provision in the Copyright Directive makes reference to national laws in connection with the meaning and scope of the concept of “fair compensation”.<sup>74</sup> As such, both the need for uniform application of EU law and the principle of equality demand that the secondary law provision be given an EU-wide independent and uniform interpretation, taking into consideration both its context and the objective of the specific legislative instrument.<sup>75</sup>
- 27 In that light, as with equitable remuneration, the concept of fair compensation must be deemed an autonomous EU law concept, subject to uniform interpretation in countries that have implemented the exception.<sup>76</sup> This assessment is in line with the Copyright Directive’s objective of facilitating a harmonized framework on copyright and related rights (by establishing a high level of protection) and safeguarding competition in the internal market, for which a uniform interpretation of EU law is required. This much is noted in Recital 32, which mentions the need for the coherent application of exceptions or limitations with the objective of ensuring a functioning internal market.<sup>77</sup> Such coherent application, however, must be made against another of the Directive’s objectives, notably that of striking a “fair balance of rights and interests between the different categories of rightholders”, as well as between these and users.<sup>78</sup>
- 28 Furthermore, in light of the objectives of the Copyright Directive and the context of Article 5(2)(b), which impose an obligation of result on Member States, the Court has noted that the EU legislator did “not wish to allow the persons concerned to be able to waive payment of that compensation to them”.<sup>79</sup> In supporting this view, the Court relies on systematic interpretation of the *acquis*, drawing comparisons between the right of fair compensation and that of unwaivable equitable remuneration for rental.<sup>80</sup> In the Court’s view, for the right to be interpreted as waivable, there would have to be an express reference in the Directive’s text; as there is not, the right of fair compensation is unwaivable.<sup>81</sup> In other words, if the Directive imposes on Member States an obligation of result regarding the actual recovery of a fair

compensation,<sup>82</sup> this obligation “proves conceptually irreconcilable with the possibility for a rightholder to waive that fair compensation”.<sup>83</sup>

## 2. The criterion of harm

29 The autonomy and uniformity of this concept are to be understood without prejudice to the power of Member States to determine, in light of applicable EU law, “the form, detailed arrangements for financing and collection, and the level of that fair compensation”.<sup>84</sup> Recitals 35 and 38 of the Copyright Directive are indicative of the EU legislator’s intent to create a system designed at adequately compensating rightholders for the likely harm resulting from unauthorised acts of reproduction.<sup>85</sup>

30 As per the Court of Justice, both the notion and level of “fair compensation” have a connection to the criterion of harm suffered by the rightholders resulting from the introduction of the private use exception or limitation, meaning that this concept must be perceived “as recompense for the harm suffered by the author”,<sup>86</sup> and that its calculation should be based on said criterion.<sup>87</sup>

31 It should be noted that, while the Copyright Directive qualifies this harm as resulting from the act in question, i.e. the unauthorised reproduction (cf. Recital 35), the Court of Justice qualifies this harm (also) as that resulting from the introduction of the exception or limitation, a distinction with relevant economic consequences.<sup>88</sup> This point is addressed in greater detail below.<sup>89</sup>

## 3. The effect of (explicit or implicit) authorisation in the right to fair compensation

32 On the topic of the effect of explicit or implicit authorisation in the right to fair compensation, *VG Wort v. Kyocera* basically states that, where end-user acts fall within the scope of an exception or limitation, any authorisation of the same by rightholders is irrelevant for application or calculation of fair compensation.<sup>90</sup>

33 The Court’s reasoning can be summarized as follows. First, Member States can implement Article 5(2) and (3) either via the legal mechanisms of exceptions (a broader exclusion of exclusive rights) or limitations (a more restricted casuistic exclusion of certain acts from the scope of exclusive rights).<sup>91</sup> In both instances, either the Directive requires that some exceptions or limitations are accompanied by fair compensation or Member States opt to do so.<sup>92</sup> Where fair compensation is provided for, it must be based on the harm caused to rightholders by unau-

thorised reproductions. When particular reproduction acts fall within the scope of a compensated exception or limitation, such uses are possible despite authorisation by rightholders. Consequently, any authorisation by rightholders of the same “is devoid of legal effects under the law of that State” and cannot impact the harm caused by the reproduction.<sup>93</sup> This in turn means that these authorisations cannot be taken into consideration when calculating the level of fair compensation.<sup>94</sup> This understanding, it should be emphasized, represents a significant departure from the status quo in many Member States’ levy systems, which take into consideration such authorisation to either eliminate levies in certain cases or substantially limit their amount.

34 On this point, the Court strays from A.G. Sharpston’s Opinion. Although the Opinion shares the same basic understanding, the A.G. qualifies her position in light of the interpretation that “the legislature clearly intended there to be some possibility for contractual arrangements to coexist with such exceptions and limitations”.<sup>95</sup> The Directive not being clear, Member States should enjoy a level of discretion, which includes the possibility of rightholders either renouncing the claim for fair compensation or making their works available through contractual arrangements that price such fair compensation for future copying into the transaction; in either case, no fair compensation from PC levies is due for these acts (as the same would, quite curiously, be “exhausted”).<sup>96</sup> A similar outcome (although following a different logic) results from the Vitorino Recommendations, analysed below.<sup>97</sup>

35 The Court’s ruling on this point raises concerns that, in many instances of digital PC, end-users will now be subject to double payment: the amount paid for a licensed use (which already prices into the purchase subsequent acts of digital copying by the user); and a levy, which must be calculated as if no digital copying is priced into the purchase of a work. At least two arguments can be raised to potentially limit this negative consequence of the Court’s judgement.

36 The first is that the Court recognizes the relevance of the application of TPMs on the calculation of the levy, such as to allow an indirect adjustment of the levy rate which reduces the impact of the double payment problem. Second, many instances where levies are not being collected on the basis that subsequent digital copying is priced into the license or purchase (e.g. Apple’s iTunes) will likely fall squarely under the provision of Article 6(4), fourth subparagraph of the Copyright Directive. This provision, noted above, can be interpreted as allowing the contractual overridability of the PC exception or limitation for works made available online, with copy control TPMs and subject to a licensing agreement. In such cases, it can be argued that there is effectively

no PC act and therefore no levy to be paid. Consequently, no risk of double payment arises.

#### 4. The effect of TPM application in the condition of fair compensation

- 37 As noted above, Article 5(2)(b) of the Copyright Directive demands that fair compensation take account of the application or non-application of TPMs to the copied works. Recital 35 further provides that “full account” must be taken of the “degree” of TPM usage vis-à-vis determining the level of fair compensation.
- 38 When interpreting these provisions, the Court notes that TPMs are meant to allow rightholders to restrict the practice of unauthorised acts by end-users, whilst the PC exception or limitation is designed as a legislative permission for unauthorised reproduction acts.<sup>98</sup> As such, it is for the Member States to define the proper scope of PC, which should be done also by the encouragement and regulation of the voluntary application of TPMs by rightholders. In other words, the application of TPMs helps delimit the scope of PC. It is that delimited scope that forms the basis for the calculation of fair compensation. In this light and due to the voluntary nature of TPMs, even where these are *available* but not *applied*, the condition of fair compensation must remain applicable.<sup>99</sup> Member States may nonetheless adjust the level of fair compensation in light of the application of TPMs, thus encouraging its voluntary adoption and better application of the exception or limitation.<sup>100</sup>
- 39 Again, the Court’s judgement seems to stray away from A.G. Sharpston’s Opinion, which believes this to be a matter of policy not clarified by the Directive, thus being up to Member States to decide *whether* and to *what extent* fair compensation should be provided for where TPMs are available to but not applied by rightholders.<sup>101</sup> It now seems that Member States can only decide the *extent* of fair compensation.
- 41 At the time of writing, rulings are awaited in *UPC Telekabel v. Constantin Film*,<sup>102</sup> *Copydan Båndkopi v. Nokia*<sup>103</sup> and *ACI Adam and Others v. Stichting de Thuis-kopie*.<sup>104</sup> These cases address some of the issues still unresolved by the above legal framework and case law.
- 42 *Copydan Båndkopi v. Nokia* examines the concept of “fair compensation” in relation to levies on memory cards for mobile phones; it further addresses a multitude of related questions that read like a “treatise” on PC.<sup>105</sup> The latter relate to topics such as the subsistence of the right to fair compensation for reproductions made from various sources (e.g. paid and gratis licensed content, DRM-ed and non-DRM-ed content, subsequent copies from third-party copies, lawful and unlawful Internet copies), the adequate consideration of the application of TPMs, the scope of the *de minimis* exemption, and the correct articulation of concepts of “fair balance” (cf. Recital 31 of the Copyright Directive) and “fair compensation” in the selection of levy targets.<sup>106</sup>
- 43 The issue of the (un)lawful nature of the source of the copies from which the relevant reproductions are made features prominently in *ACI Adam and Others v. Stichting de Thuis-kopie*, which furthermore inquires as to the effect of the application of the three-step test (Art. 5(5)) on the scope of PC and its articulation with the Enforcement Directive.<sup>107</sup>
- 44 For its part, *UPC Telekabel v. Constantin Film* tackles the issue of the nature of the source of the copy through the lens of the interpretation of Article 8(3) of the Copyright Directive, on the application of injunctions against intermediaries (here: Internet Service Providers) whose services are used by users of infringing content made available online.<sup>108</sup>
- 45 The quantity and depth of the above requests for preliminary rulings will quite likely yield rulings that clarify most of the (many) questionable issues surrounding PC in the EU. Maybe for that reason, the Vitorino Recommendations analysed below shy away from some of the important issues raised in such requests, such as the nature of the source of the copy<sup>109</sup> or even the full impact of TPM application in the assessment of fair compensation, which has in the meantime been addressed in *VG Wort v. Kyocera*.<sup>110</sup>

### III. Colouring the remaining legal landscape: forthcoming ECJ case law (brief reference)

- 40 However clarifying the above-mentioned ECJ case law was, it has nonetheless left in its wake a patchwork harmonization of the PC exception/limitation. In fact, not only has there been an institutional effort to further harmonize this field – as noted by the mediation process leading to the Vitorino Recommendations – but it has also caused the ECJ to be flooded with multiple references for preliminary rulings.

#### C. The Vitorino Recommendations

- 46 The Recommendations, published on 31 January 2013, are relevant not only for their institutional weight, but mostly because they provide an adequate mapping of significant points of contention within the levies debate. They have furthermore been qualified as “non-binding provisions” on PC levies by the Commission.<sup>111</sup>



47 In order to be properly understood, the Recommendations must be read in light of both the then-pending requests for preliminary rulings by the ECJ (mentioned above) and the mediator's baseline understanding of key issues of the PC legal framework and debate. The latter can be inferred from his introductory remarks in the document.<sup>112</sup> First, Mr Vitorino believes that none of the currently proposed alternatives justify the "phasing out" of hardware-based levies.<sup>113</sup> Second, the link between the PC beneficiaries causing the "harm" and those liable for financing fair compensation "should not be severed".<sup>114</sup> Third, online business models are shifting from ownership to access-based models, leading to a future decrease in the level of levies collected.<sup>115</sup> In fact, where rightholders are remunerated via licensing agreements for uses through (typically DRM-ed) "online services" covering reproduction of their works, imposition of levies would configure a double payment. (This assumption, however, seems to have been challenged in the meantime by *VG Wort v. Kyocera*.) As such, the focus of the Recommendations is squarely placed on the "consistency, effectiveness and legitimacy" of current levy systems.<sup>116</sup>

48 The Recommendations are divided into two clusters: the first addresses new business models, licensed services and the PC exception or limitation;<sup>117</sup> the second is directed at levy systems in the internal market.<sup>118</sup> The following sections look at both clusters in sequence, focusing on those recommendations that are aimed at PC and the issues raised by the previous analysis of its legal framework.

## I. On new business models, licensed services and private copying

49 In this context, Mr Vitorino basically offers one recommendation regarding the clarification that end-user copies made for private purposes in the context of licensed services (by rightholders) cannot be considered to cause any harm giving rise to additional remuneration in the form PC levies.<sup>119</sup>

50 Although the current business market for online services is dynamic and evolving, Mr Vitorino identifies a tendency for comprehensive offers to consumers, comprising multiple features (device portability, synchronization, cloud "storage and matching", playlist sharing, etc.), for the most part falling outside the scope of the PC exception; as such, the argument goes, the lawful operation of these complex access-based services requires licensing agreements.<sup>120</sup>

51 If that assessment is true, the question then becomes how to qualify end-user copies made for private purposes under licensed services. Such a qualification depends on whether the rightholder's consent for PC acts is valid. If invalid, the use falls under the excep-

tion or limitation and (unless *de minimis*) should give rise to payment of fair compensation. Mr Vitorino considers the consent to be valid without explicitly laying out his legal arguments, instead echoing different stakeholders' opinions.<sup>121</sup> Such opinions can be structured as follows: a rightholder's authorisation for private use does not equate to the contractual overridability of the exception or limitation; it is instead a contractual disposition of an already exempted act; therefore, the rightholder is entitled to grant such authorisation against whichever counter performance is deemed adequate. The logical conclusion of this argument, and one which Vitorino endorses, is that PC acts so authorised (i.e. made in the context of a licensed service) will cause no "harm" and therefore give rise to no claim for fair compensation.<sup>122</sup>

52 It is noteworthy that A.G. Sharpston's Opinion, preceding the Court's judgement in *VG Wort v. Kyocera*, reaches a similar conclusion on this precise issue, albeit following a different reasoning.<sup>123</sup> A.G. Sharpston argues for the validity of national laws allowing rightholders to either "renounce any claim to fair compensation or make their works available for copying subject to contractual arrangements", thus enabling them to receive fair compensation in advance for future acts of PC; in either case, such rightholders would have no claim for fair compensation, which should be deemed "exhausted".<sup>124</sup> As noted above, the Court in *VG Wort v. Kyocera* took a different view, clearly stating that any authorisation of an act encompassed in the scope of a PC exception or limitation is void of legal effects and thus has no bearing on the fair compensation owed.<sup>125</sup>

53 Mr Vitorino's interpretation rests on a belief in online service providers' ability to cater to market needs via direct licensing. In this context, the mediator recognizes that a CMO-enabled private ordering regime may hinder authors and performers, due to their lack of bargaining power in negotiations with corporate rightholders, a fact often leading to the latter acquiring all economic rights on works and benefiting from direct licensing practices. Notwithstanding, he argues that these issues are not the province of the PC levies framework, and should instead be addressed in the forum of contract and labour law, as well as collective rights management.<sup>126</sup>

54 In sum, Mr Vitorino argues that licensed copies should not give rise to PC levies, as that would lead to double payment. This solution is supported by Recitals 35 and 45 of the Copyright Directive (opening the door for contractual stipulation in this field) and by the ECJ rulings in *Padawan* and *Stichting de Thuiskopie*, which link fair compensation to "harm" caused by *unauthorised* reproduction. Put differently, authorised uses cause no harm requiring (fair) compensation. Although the conclusion is legally sound, Mr Vitorino's road to reach it is criticisable, insofar as it



rests on an assumption of a universal licensing requirement for modern multi-feature service offers to end-users. This pro-licensing approach, increasingly advocated by the Commission for the online use of copyrighted works (as transpires from its “Licenses for Europe” initiative<sup>127</sup>), represents a policy trend whose effect is to endorse a restriction to the scope of the PC exception or limitation. A restriction of this magnitude may be legally questionable, on the grounds that it goes beyond ECJ interpretation of the PC exception’s scope, especially post-*VG Wort v. Kyocera*, thus raising questions of legal uncertainty. It also opens the door to some normative discussion on the justification of this exception in light of current contractual and technological possibilities in the digital realm.

## II. On levy systems in the Internal Market and in particular the concept of harm

- 55 In what concerns levy systems in the internal market, Mr Vitorino’s departure point is that, pursuant to *Padawan*, the sole condition for the “*leviability*” of products is their technical capability to make (or store) copies.<sup>128</sup> Beyond this condition, Member States (and not the EU legislator) should decide which products to levy, according to their specificities.<sup>129</sup> Notwithstanding, and with respect for the principles of subsidiarity and proportionality, levy systems should be reconciled with Internal Market objectives.<sup>130</sup> Several recommendations are advanced in this context, aimed at providing specific solutions to existing “cross-border issues” connected with the divergent application of the PC regimes. For the purposes of this article, these can be divided into recommendations that do not focus on the concept of harm, and those that do focus on that concept.<sup>131</sup>
- 56 The first group of recommendations is of reduced interest to our inquiry, as it relates to levy systems in the Internal Market in general. First, it is recommended that levies are collected “in cross-border transactions in the Member State in which the final customer resides”.<sup>132</sup> Second, the mediator addresses concerns with double payments in cross-border sales and payment liability, by presenting an alternative proposition: either **(i)** “*liability for paying levies should be shifted...to the retailer’s level while simplifying the levy tariff system and obliging manufacturers and importers to inform collecting societies about their transactions concerning goods subject to a levy*”, or **(ii)** “*clear and predictable ex ante exemption schemes should be established.*”<sup>133</sup> Third, it is recommended that levies “be made visible for the final customer”.<sup>134</sup> In the context of the adoption of ex-ante exemptions from payment by manufacturers/importers, a parallel solution would be imposing this transparency obligation throughout the sales chain.<sup>135</sup> Finally, Mr Vitorino recommends that the tariff-setting process be improved and made transparent, that equal representation of all stakeholders be implemented, and that the process be subject to supervision by national authorities (at interim and/or final level).<sup>136</sup> Furthermore, it is suggested that levy-setting decisions should be subject to judicial review, preferably under specific procedural rules, ensuring fast decisions and clearly defining the effective date of application of the rate.<sup>137</sup>
- 57 Turning to the concept of harm, Mr Vitorino believes that, in order to achieve coherence in the levy-setting process, it is necessary to define “‘harm’ uniformly across the EU as the value consumers attach to the additional copies in question (lost profit)”, and provide a “procedural framework that would reduce complexity, guarantee objectiveness and ensure the observance of strict time-limits”.<sup>138</sup>
- 58 In this respect, it is rightly noted that the notion of “harm” caused to authors for PC purposes is subject to different interpretations. Harm is both a *valuable* (cf. Recital 35 of the Copyright Directive) and *necessary* (cf. *Padawan*) criterion for calculating fair compensation.<sup>139</sup> What is not mentioned in the Recommendations is that, while Recital 35 discusses the harm *resulting from the act of PC*, *Padawan* shifts that interpretation to the harm *resulting from the introduction of the exception or limitation*. In any event, Mr Vitorino believes this concept requires uniform interpretation (similarly to the related concept of fair compensation), providing a clear link to the amounts levied.<sup>140</sup>
- 59 To that avail, he proposes to “look at the situation which would have occurred had the exception not been in place” and concretely “assess the value that consumers attach to the additional copies of lawfully acquired content that they make for their personal use.”<sup>141</sup> This “would allow the estimate of losses incurred by rightholders due to lost licensing opportunities (‘economic harm’), i.e. the additional payment they would have received for these additional copies if there were no exception”; in most cases, “this amount would neither reach the level comparable to the value of the initial copy nor would it be so negligible that it could be completely ignored”.<sup>142</sup> To make this definition workable, “it would be necessary to assess not the *actual* number of copies made but rather the *hypothetical* (lower) number of copies that could have been licensed in the absence of the exception”.<sup>143</sup> It is thus “fair and reasonable”, Mr Vitorino continues, to “compensate rightholders precisely for lost income opportunities, e.g. via the licence agreements they would have concluded if there were no exception”, and “for the level of compensation to reflect the actual value attached by consumers to such additional ‘private’ copies”.<sup>144</sup>

- 60 There are several possible criticisms to Mr Vitorino's proposed interpretation of the concept of harm, both from the economic and legal standpoints. The first relates to the identification of "the value that consumers attach to the additional copies", which in economic terms is in principle the entire consumer surplus of private copies, to "lost profit". Absent the PC exception, even very refined pricing schemes for licences would not be able to appropriate the entire consumer surplus and turn it in to revenues for rightholders. As such, the rightholders' "economic harm" as defined by Mr Vitorino should not, from the economic standpoint, be understood as the value that consumers attach to their private copies, as said amount will be in excess of that which would result even from the normal exploitation of exclusive rights through sophisticated price discrimination models.
- 61 Second, using the criteria of the hypothetical situation "which would have occurred had the exception not been in place" introduces the complex question of whether consumer behaviour would really be much different with or without a PC exception. Besides justifications based on fundamental rights such as privacy, this exception is to a large extent based on market failure considerations linked to high transaction costs in connection to the enforcement of previously mass infringing uses.<sup>145</sup> To the best of the authors' knowledge, there is no convincing empirical evidence that, in countries where no PC exceptions have been introduced (such as the UK, although implementation of a narrow uncompensated PC exception is forthcoming<sup>146</sup>), fewer private copies are made. To be sure, this is an empirical question. However, it is submitted that lacking the relevant data, it becomes nearly impossible to establish a realistic baseline from which to calculate harm.
- 62 Third, and related, Mr Vitorino's definition of harm seems to conflate the concepts of *lost profits* and *lost licensing opportunities*. This is made clear by the application of his hypothetical-scenario logic in the context of infringement of exclusive rights. In this scenario, an infringing practice (e.g. unauthorised reproduction) could trigger the payment of damages. Under the Enforcement Directive, it is possible to calculate damages for either lost profits or lost licensing opportunities.<sup>147</sup> Very briefly, lost profits are a primary method for the calculation of damages appropriate to the actual prejudice suffered by rightholders as a result of the infringement, constituting an example of the negative economic consequences of such acts.<sup>148</sup> However, the Enforcement Directive allows for an alternative possibility of calculating damages, namely by setting them as "as a lump sum on the basis of elements such as *at least the amount of royalties or fees* which would have been due if the infringer had requested authorisation to use the intellectual property right in question".<sup>149</sup> This latter possibility bears a strong resemblance to Mr Vitorino's definition of lost licensing opportunities. It is therefore *prima facie* difficult to understand his concept of lost profits as the basis of calculation of the PC harm.
- 63 Moreover, PC is an exception or limitation, meaning that relevant challenges arise when applying methods of calculation native to the infringement of exclusive rights. Chief among these is the fact that, contrary to the case of PC, it is possible in the context of exclusive rights to calculate lost licensing opportunities precisely with reference to information from previous licensing agreements (where these exist) that would encompass the uses in question. Such licensing agreements do not exist for PC purposes and one should be cautious in taking into consideration agreements for equivalent uses under exclusive rights, as their pricing does not reflect the infringer's unwillingness to license at this price. Consequently, levies set according to this method could lead to higher amounts paid by end-users.
- 64 Another issue relates to the definition of economic harm as reflecting lost licensing opportunities for subsequent copies of "lawfully acquired content".<sup>150</sup> This concept is not specified further by Mr Vitorino, and thus it is not possible to discern whether it is meant to apply to copies from content lawfully purchased, rented, streamed or downloaded (either subject to DRM, contractual conditions, payment or neither) or otherwise accessed. Assuming the concept is sufficiently broad to cover all the aforementioned variations, it implies that only PC acts from a lawful (or lawfully accessed) "source" are relevant for purposes of calculating fair compensation. Where national laws do not contain a qualification of this type, it is arguable that all PC acts fall within the scope of the exception or limitation, irrespective of the nature of the source or the access.<sup>151</sup> However, several European countries do contain provisions of this type.<sup>152</sup> In these countries, any copies from content unlawfully acquired, accessed or made available (e.g. in many cases, file sharing of torrent networks, newsgroups, social networks or cyber lockers) are deemed not covered by the exception and thus not exempted acts of PC. In that scenario, it seems to follow that no fair compensation is due, as the acts in question constitute instances of copyright infringement. That much results from Mr Vitorino's argumentation. Notwithstanding, such an interpretation, especially where restricted to instances of content lawfully *acquired strictu sensu*, if harmonized at the EU level brings with it the risk that a significant portion of current online uses – namely, acts of download not covered by licensed services – would be deemed infringing. This will not only raise enforcement costs, but also reduce the scope of the PC exception and potentially diminish the amount of revenues generated by levies. Those direct consequences will bring related concerns of privacy risks caused by additional enforcement, criminalization

of an increasing number of end-users and, in general, reduced scope for innovation that depends on the “breathing space” provided by private acts of online reproduction, mostly related to “dynamic” or “creative” PC.<sup>153</sup>

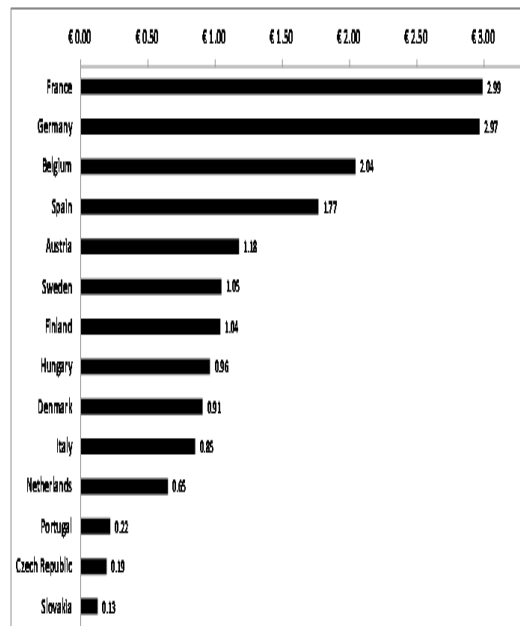
- 65 It is expected that this issue is dealt with in detail by the ECJ in the aforementioned ECJ references for preliminary rulings, which encompass many potential configurations of the unlawful source/access of/to the copies giving rise to subsequent private and non-commercial acts of reproduction.
- 66 A final criticism relates to Mr Vitorino’s understanding that “the ‘harm’ which is subject to fair compensation arises not from one single copy but from a number of a natural person’s activities which, taken together, amount to relevant ‘harm’ caused to right-holders”; as such, it cannot be qualified as *de minimis*.<sup>154</sup> By itself, this raises great legal uncertainty. No clarification is provided on multiple issues, such as where to draw the line for acts to be considered jointly. What are the relevant acts to be aggregated (those of a consumer regarding a specific work, by a specific rightholder, or all works of the same rightholder)? What is the relevant period of time for calculation of aggregate uses? Moreover, even if a broad interpretation on these points is professed so as to secure that a levy system is operational and effective, it then becomes nearly impossible to define the scope of *de minimis* uses.<sup>155</sup> Perhaps a reasonable way to address this uncertainty is to focus on each levied device or blank media, instead of each user. Consequently, calculation through aggregation of uses would be admissible for PC made in each such device of media over its lifetime. Where PC acts for each device or media (even when taken together) are minimal, no levy should be due. If Internet connections were to be levied instead of devices, the consequences of applying this logic would be different.

#### D. PC levies in practice in the EU

- 67 Following the Copyright Directive, 22 out of 27 EU Member States have introduced levy systems.<sup>156</sup> As technology used for consuming and storing music and audio-visual material changes rapidly, so do the devices and media levied. All 22 EU countries that introduced PC levies apply these to blank CDs and DVDs. A majority also have levies on memory cards, MP3 players and hard disc DVD recorders. In addition, a number of countries have levies on external hard drives, PCs, tablet computers and smartphones. Game consoles are generally exempted, as the Copyright Directive does not apply to software.<sup>157</sup>
- 68 There are also massive differences in the levels of PC levies. For example, for a blank CD, nominal levies range from € 0.009 in the Czech Republic to € 0.35 in France. Alternatively, several countries have levies

relative to the price of media, ranging from 1.25% in Bulgaria to 6% in Greece. For devices such as MP3 players, nominal levies often depend on the storage capacity. For a 32-GB player, levies range from € 1.42 in Latvia, to € 22.52 in Hungary. Levies for hard-disk DVD recorders range as high as € 50 in France.<sup>158</sup>

- 69 Figure 1 gives the revenues collected per capita in 2010 in several EU Member States. Revenues per capita range from less than € 0.01 in Bulgaria to nearly € 3 in France and Germany. For all EU Member States taken together, revenues totalled about € 648 million in 2010.<sup>159</sup> As a result of rapidly changing technology used for storing and copying content, in combination with a tradition of litigation over the incorporation of new media and devices in levy schemes, revenues tend to vary over time. An upward driver is the rapidly increasing storage capacity of most devices, which implies that revenues based on a fixed amount per MB or GB increase rapidly in time. A downward driver is the dynamic nature of the consumer electronics market. For instance, the use of blank CDs and DVDs has plummeted as they are substituted by USB sticks and memory cards. Likewise, the market for MP3 players is being cannibalized by smartphones.



**Figure 1: Private copying levies collected in 2010 (€ per capita)**

**Source:** Based on WIPO, *International Survey on Private Copying: Law & Practice 2012*. Geneva, Switzerland: World Intellectual Property Organization (2012), pp. 13-14.  
**Notes:** Within the EU, no PC levies exist (at the date of writing) in Cyprus, Ireland, Luxembourg, Malta and the UK; no data is available for Slovenia and Estonia.



## E. The economics of private copying levies

70 Having provided a detailed account of the legal background and ECJ interpretation of the PC exception or limitation, as well as a brief overview of the empirical data on PC levies in the EU, this part will now overlay on the previous legal and empirical blueprint an economic perspective on PC levies, which is often foreign to the legal debate in this field. The focus will be on the definition of types of PC, the articulation of the concept of harm with the economic notion of indirect appropriability and the application of TPMs.

### I. Types of private copying

71 Article 5(2)(b) of the Copyright Directive is phrased in a very generic way with respect to the *types* and *purpose* of private copies: as long as such copies are made by a natural person for private non-commercial use, they can fall under the exception, provided rightholders receive fair compensation. From an economic point of view, however, it is useful to distinguish various types of private copies, as they will have different values for consumers, and any harm for rightholders due to lost sales (or lost licensing opportunities) will also differ between these types. For these analytical purposes, the following typology is proposed:<sup>160</sup>

- a Making copies of broadcasted works for *time shifting*, such as storing radio or TV content on a recording device to watch it another time and if desired repeatedly;
- b Making “clone copies” of or “format shifting” CDs, DVDs and media files, or storing streaming audio and video for offline playback (also known as stream “ripping” or “capture”);
- c Making clone copies or format shifting to *share* works with members of your *household, family and friends*;<sup>161</sup>
- d Making clone copies or format shifting of works from media *rented* or *borrowed* from libraries or commercial renters;
- e Making *backup copies* of works;
- f *Downloading* and storing works from *unauthorised sources* on the Internet (and making subsequent copies thereof).

72 Typically, private copies of type (a)-(e) are allowed under the PC exception or limitation. However, types (b)-(e) may in practice be prohibited or restricted by TPMs and licence or rental agreements. According to a recent WIPO survey, downloading from unau-

thorised sources on the Internet (f) is prohibited in most EU Member States.<sup>162</sup>

73 There are relevant economic differences between all these types of copies. Copies of type (a) and (b) enhance the utility that consumers derive from their legitimate purchase or subscription. It enables them to consume this content at a more convenient time or place, on a more practical device or without carrying discs and devices around. For instance, they can keep a copy of their favourite CDs in their car or vacation home or play them on their computer, smartphone or MP3 player. Time-shifting also enables them to skip advertisements in TV programmes, either manually or by using built-in features in digital video recorders (DVRs) or software. Copies of type (c) and (d) are different from the former in that they extend the circle of consumers who derive utility from an original unit of content.<sup>163</sup> Unauthorised downloading (f) resembles the former types, with the notable difference that the extended circle of consumers is anonymous and potentially unlimited. Backup copies (e) do not provide utility directly but act as an insurance against mishaps.

### II. Harm and indirect appropriability

74 These differences are relevant in light of the *harm* that PC may cause to copyright holders and the concept of *indirect appropriability*. This term refers to the economic mechanism according to which, under certain conditions, the demand for originals will reflect the value that consumers place on both the originals and subsequent copies they may make. Hence, the value of PC can be priced into the initial purchase and by doing so, this value is *indirectly appropriated*. If copyright levies should be understood as a compensation for harm caused by PC, as is the case at least according to EU law, it is important to analyse the economics behind this harm more closely.

75 A seminal contribution to this issue is provided by Stan Liebowitz, who studied the effect of photocopying on the demand for journals.<sup>164</sup> He found that “publishers can indirectly appropriate revenues from users who do not directly purchase journals and that photocopying has not harmed journal publishers”.<sup>165</sup> The value consumers (or scholars) derive from copies contributes to the willingness of libraries to pay. Hence, publishers end up selling fewer originals at a higher price, which may even raise profits. If the number of copies per original differs substantially, such *indirect appropriability* depends on the ability to price-discriminate: charging a higher price for users who are likely to enable extensive copying while preventing arbitrage through a secondary market or other ways to circumvent price discrimination. In practice, this is done by a higher price for libraries and a lower price for individuals.



- 76 In general, selling fewer originals at a higher price introduces two opposing effects which may lead to both higher and lower profits. This issue was further studied by Besen and Kirby, who model PC while distinguishing (i) the extent to which originals and copies are perfect substitutes, and (ii) whether PC has constant or increasing marginal costs.<sup>166</sup> Increasing marginal costs may not only stem from the technology itself, but also from the “costs” of organizing the copying process within sharing groups. Besen and Kirby conclude that the effect of PC on consumer and producer surplus and total welfare depend strongly on the assumptions about substitutability and the costs of copying. When the marginal costs of copying are *constant*, copies will be distributed at marginal costs and the value of copies cannot be appropriated. The introduction of (relatively cheap) copying technology will then lower the price of originals and profits will decline subsequently. Consumer surplus will increase, while the effect on total welfare is ambiguous. If the marginal costs of copies are *increasing*, copying leads to fewer originals sold at a higher price: indirect appropriability. Besen and Kirby conclude that the effect on welfare will depend on whether or not copying is cheaper than producing originals: “in the case where the size of the sharing group is fixed, consumer and producer welfare generally increase when copying is efficient and decline when it is not. When the costs of both originals and copies are low, however, producers will generally lose and consumers will gain from the introduction of copying.”<sup>167</sup>
- 77 The scenario of *constant* (near-zero) marginal costs of copying resembles the situation of unauthorised file sharing over the Internet (type (f) above), even though such file sharing did not occur when Besen and Kirby wrote their paper. Their analysis implies that indirect appropriability is not feasible in the face of online file sharing. This also follows from the fact that the number of copies generated per original sold may differ immensely. Some CDs will not be copied at all, while others will be ripped and uploaded to torrent sites to be seeded to millions of users. This complicates price discrimination.
- 78 The scenario of *increasing* marginal costs will apply to all types of PC except for unauthorised file sharing and may or may not cause harm, depending on the costs and value of copies in comparison to that of originals and the size of sharing groups. Copying may cause no harm at all to copyright holders, but copies may also become competitors to the originals, constraining the price the copyright holder can charge and reducing profits substantially.<sup>168</sup>
- 79 Empirical testing of the net effect of PC on profits is lacking. Surveys carried out in the context of the levy-setting process in various countries typically focus on the number of private copies and the self-reported substitution rate<sup>169</sup> and ignore the effect of PC on the demand for the first original and the complex dynamics of indirect appropriability. The net effect can be expected to differ for the various types of PC discussed above. As mentioned there, private copies of types (a), (b) and (e) do not extend the circle of consumers that derive utility from an original unit of content. No “copying groups” are formed in which copies become competitors to the original. Some additional sales could be foregone as a result of such copying, for instance when a person would have bought his favourite CD twice to play it at home and in his car. But to the extent that consumers can roughly anticipate their copying behaviour, the option to copy can be *priced into the initial purchase* by rightholders. Put differently, the demand curve for originals will reflect the expected utility derived from such private copies. This is an important notion, as it means that in such a case a copyright levy that charges “the value that consumers attach to the additional copies”, as Mr Vitorino suggests, would lead to double payment.<sup>170</sup>
- 80 On the other hand, the demand curve will not reflect the utility of *unforeseen* copying possibilities: in the first decade after the introduction of the CD, consumers would not have expected the possibility that twenty years later, they would be able to make perfect copies of CDs within their home, let alone rip 500 CDs into a portable device the size of a matchbox. Hence, the utility they derive from copying and ripping these CDs will not have been reflected in their initial purchase at the time.<sup>171</sup>
- 81 Turning to copies shared within one’s household, and with family and friends (type (c)), the aforementioned models of Besen and Kirby and Varian are more likely to apply, and PC might be harmful to copyright holders even though some of the additional utility can be appropriated indirectly. This is partly due to the fact that the size of such copying groups is variable and price discrimination according to group size is not possible. The utility of copies of type (d) could in theory be appropriated indirectly by setting the appropriate rental prices, unless restrictions put on the rental price from a public service perspective prohibit doing so.
- 82 To summarize the economic perspective, the utility downloaders derive from *unauthorised file sharing* cannot be priced into the initial purchase. For other types of PC, these benefits can to a large extent be appropriated by using smart pricing, depending on the cost structures. For *time shifting*, *format shifting* and *clone copying* for personal use, this is likely to be the case almost entirely – after an initial shock wave caused by the introduction of cheap digital copying and ripping technology for consumers. Now that both consumers and producers are aware of this technology, indirect appropriability will apply and harm will be minimal. In such cases, levies aimed at compensating for this minimal harm

are ill-advised, given the administrative and transaction costs they incur and their potential effect to take away incentives for smart pricing.

- 83 For copies *made within the accepted circle of family and friends*, on the other hand, indirect appropriation may not be sufficiently possible (e.g. due to varying sharing group size) and harm from such private copies may well occur. However, the problems resulting from the latter for a PC perspective will greatly depend on the definition of the scope of what uses can be qualified as *private* under the exception (as all sharing acts outside that scope are deemed copyright infringement and, thus, not to be dealt with in the PC regime).

### III. The application of DRM

- 84 As a preliminary point, it should be noted that the term DRM encompasses both TPMs – e.g. access and copy control measures (Art. 6 of the Copyright Directive) – and electronic rights management information – such as fingerprinting or watermarking, also known as “social DRM” (Art. 7 of the same Directive). Furthermore, most economics literature applicable to PC levies either does not make the distinction and uses the term interchangeably or uses it solely to mean TPMs.<sup>172</sup> The distinction is relevant insofar as legal rules regulating the effect of these measures on the scope of PC and the calculation of levies mention solely TPMs.<sup>173</sup> Consequently, all arguments on the impact of other types of DRM on the amount of levies must be construed as economic (and normative) by nature. The following paragraphs adopt the broad use of the term DRM, making the distinction with TPMs where relevant.
- 85 Koelman points out that DRM increases the opportunities copyright holders have to appropriate the additional utility derived from PC.<sup>174</sup> This is in line with remarks in the Copyright Directive on the “application or non-application” of TPMs and Mr Vitorino’s recommendation that licenced copies do not require additional remuneration by a levy. However, the distinction between the “application or non-application of technological measures” is not as binary as it may seem at first glance. Due to its rich variety, DRM can be applied with the aim of making any kind of copy impossible, even clone copies or format shifts (type (b)) and backups (type (e)). Or it can be applied in a slightly more lenient way, allowing consumers to make a certain number of copies to other devices and carriers. In the case of *social DRM*, the aim of which is to discourage the distribution of private copies outside a circle of family and friends, copies found on file-sharing sites can be traced back to the original purchaser against whom action could be taken. In practice, several flavours of DRM coexist, sometimes even for the same title: consumers
- can choose the kind of DRM they are willing to accept and pay the corresponding price.
- 86 Many believe that DRM did not and will likely not eradicate all unlicensed copying. As Steve Jobs stated in 2007: “DRM (systems) haven’t worked, and may never work to halt music piracy.”<sup>175</sup> The technical and privacy issues that make strict enforcement problematic and give rise to copyright levies in the first place have not disappeared with the introduction of DRM. Nevertheless, various kinds of DRM are now available to give copyright holders at least a firmer grip on copying and more opportunities for price discrimination and indirect appropriation. Against this background, the decision *not* to apply DRM should also be considered. When consumers started copying and sharing CDs on a large scale, for instance, record labels introduced DRM on CDs, and until 2007, all digital music files bought from Apple’s iTunes store also contained DRM technology to prevent copying.<sup>176</sup> However, consumers did not appreciate the way in which DRM got in the way of supposedly legitimate uses. For instance, DRM sometimes caused computers to crash, which was a nuisance to people trying to play an audio CD with their computer, even without trying to copy it. Also, the use of DRM prevented consumers from format shifting, such as ripping their own CD collection onto their MP3 player. Thus, DRM “impose[s] costs on legal users who have no intentions of doing anything illegal”.<sup>177</sup>
- 87 Therefore, the use of DRM (and in particular TPMs) may create a disutility for consumers and have a negative effect on the demand for originals. For example, consumers who only play music from a hard drive or on their phone may stop buying CDs if TPMs prohibit them to rip these. DRM may even cause consumers to revert to TPM-free content from illegal sources.<sup>178</sup> Over the last few years, the music industry moved away from using DRM.<sup>179</sup> From an economic point of view, this should be a rational choice. Indeed Sinha et al. find that “the music industry can benefit from removing DRM” and that “a DRM-free environment enhances both consumer and producer welfare by increasing the demand for legitimate products as well as consumers’ willingness to pay for these products”.<sup>180</sup> Therefore, the choice *not* to use TPMs should be perceived as a rational choice in the spectrum ranging from more to less restrictive DRM technologies that are currently available.
- 88 Now that rightholders have these options, it makes no longer sense for copyright levies to draw a sharp line between the application and non-application of TPMs as the Copyright Directive seems to suggest. The choice *not* to use TPMs or any other kind of DRM (where they are available) should no more entitle copyright holders to compensation than the choice to use restrictive TPMs. There seems to be legal room to accommodate this economic argument.

For example, Hugenholtz *et al.* propose that “levies are to be phased out not in function of actual use, but of availability of technical measures on the market place.”<sup>181</sup> The point is that the decision not to apply TPMs but less restrictive DRM or no measures at all will enhance the value of the original to the initial consumer. This will increase consumers’ average willingness to pay, which implies the enhanced value of the original can (at least partially) be appropriated indirectly. Therefore, while TPM technology is widely available, its non-application or the application of less restrictive DRM is in many instances in the best interest of both consumers and rightholders.

- 89 The Court’s decision in *VG Wort v. Kyocera* seems oblivious to these considerations by preventing that the availability of TPMs is considered by itself as reason sufficient to eliminate any fair compensation to rightholders.<sup>182</sup> Notwithstanding, Member States retain a wide discretionary margin in defining the extent of fair compensation where TPMs are available but not applied. From a legal standpoint, such discretion must be exercised and, one might argue, on the basis of solid economic reasoning and evidence. Consequently, consideration should be given to the multiple types of TPMs available to rightholders that allow price discrimination and enable indirect appropriability, under the terms described above. Furthermore, nothing seems to *prevent* (although there is no legal imposition to do so) Member States from extending such consideration to other types of DRM that fulfil similar functions, thus allowing for a more holistic approach to the calculation of the applicable levies.
- 90 Finally, harm from PC cannot be equated to harm caused by the possible introduction of a PC exception or limitation to copyright. As pointed out above, consumers’ PC behaviour is to a large extent independent of its legal status, since enforcement is problematic. These acts occur with or without an enabling legal exception or limitation. Much of any harm from PC would thus not be the *result* of the introduction of such an exception. This implies that the suggestion, both in *Padawan* and in Mr Vitorino’s Recommendations, to base compensation on the harm caused by the *introduction* of the PC exception, could leave copyright holders empty-handed. Consequently, it would make more sense for rightholders to more closely follow the letter of Recital 35 of the Copyright Directive and have fair compensation be calculated on the basis of the “use made of their protected works or other subject matter”. If the above arguments on indirect appropriability and the economic analysis of the concept of harm are adopted by national legislators, rightholders would have economic logic on their side in doing so.

## F. Conclusions

- 91 Copyright levies have been introduced to compensate rightholders for the harm caused by PC. However, economic analysis has shown that the utility consumers derive from offline private copies can to a large extent be appropriated indirectly. Hence, the harm caused by these acts will be substantially smaller than the utility consumers derive from private copies or even the sales forgone by such copying. For private copies that do not lead to a proliferation of content – for example, time shifting, format shifting and backup copies – there may be no harm at all, provided consumers are aware of these copying possibilities at the time of their initial purchase.
- 92 TPMs, less restrictive DRM and innovative pricing schemes have improved the possibilities for copyright holders to appropriate the value of private copies. Therefore, charging levies for copies that are licenced by rightholders would lead to double payment. The Court of Justice’s decision in *VG Wort v. Kyocera* ignores this economic reasoning and the inherent link between contractual arrangements and DRM availability. By denying legal effects to acts of authorisation within the scope of PC, the Court opens the door for levying related goods *in addition to license fees*; to be sure, this is detrimental to consumers, who will ultimately bear the burden of payment of both. Moreover, the choice *not* to apply TPMs is nowadays a rational choice that, from an economic perspective, should not be treated differently from the choice to apply TPMs (or any other sort of DRM for that matter). Altogether, the case for levies to compensate for harm caused by “classical” private copies is gradually diminishing.
- 93 The argument of indirect appropriability does not apply to private reproductions made in the context of unauthorised online file sharing, as there is no relation between the uploader (including any unlawful content provider) and the downloader and the number of copies made from an original will vary dramatically. It is an open question in references for preliminary rulings pending at the Court of Justice (in *Constantin Filmverleih v. UPC Telekabel*, *Copydan Båndkopi v. Nokia* and *ACI Adam and Others v. Stichting de Thuis kopie*) whether EU legislation allows levies to account for the harm caused by copies from content unlawfully accessed or from an unlawful source. If the question is answered in the affirmative, copyright levies will continue to have a sound economic basis within the EU. If not, as already happens to different extents in various Member States, the resulting narrow scope of the PC exception or limitation will provide an increasingly weaker economic case for levies in the digital age.

1 Parts of this article are based on: Poort, “Chapter 21: Copyright levies”, in: *Handbook of the Digital Creative Economy*, Towse, & Handke (eds.), Edward Elgar (forthcoming 2013). The authors



thank the editors for useful comments on an earlier draft of that chapter.

- 2 Grundig Reporter, German Federal Supreme Court (Bundesgerichtshof), 18 May 1955, Case I ZR 8/54, GRUR 492; and German Federal Supreme Court (Bundesgerichtshof), Case I ZR 10/54. While the first case focuses on copyrights managed by the German CMO GEMA, the second addresses related or neighbouring rights in sound recordings held by record companies. See also the follow-on case GEMA-Hinweis, German Federal Supreme Court (Bundesgerichtshof), 22 January 1960, Case I ZR 41/58, GRUR 1960, 340.
- 3 Personalausweise, German Federal Supreme Court (Bundesgerichtshof), 29 May 1964, Case Ib ZR 4/63, GRUR 1965, 104.
- 4 For a detailed analysis of these cases and a legal-historical account of the genesis of PC levies in Europe, see Hugenholtz, “The Story of the Tape Recorder and the History of Copyright Levies”, in *Copyright and the Challenge of the New*, B Sherman & L Wiseman (eds.), Information Law Series, vol. 25 (Alphen aan den Rijn: Kluwer International 2012), pp. 179-196.
- 5 WIPO, “*International Survey on Private Copying: Law & Practice 2012*”, World Intellectual Property Organization (2012), p. 3.
- 6 Green Paper on Copyright and the Challenge of Technology 1988, pp. 99-142.
- 7 The documents resulting from the mentioned stakeholder consultations in 2006 and 2008 can be accessed at European Commission, The EU Single Market, Copyright and Neighbouring Rights, Ongoing Initiatives: Private copying levies, [http://ec.europa.eu/internal\\_market/copyright/levy\\_reform/index\\_en.htm](http://ec.europa.eu/internal_market/copyright/levy_reform/index_en.htm).
- 8 See Communication from the Commission to the European Parliament, the Council, the European Economic and Social Committee and the Committee of the Regions, on a Single Market for Intellectual Property Rights boosting creativity and innovation to provide economic growth, high quality jobs and first class products and services in Europe, COM (2011) 287 final (May 24, 2011) [hereinafter IPR Strategy].
- 9 See European Commission, The EU Single Market..., supra note 7.
- 10 Vitorino, A, *Recommendations resulting from the Mediation on Private Copying and Reprography Levies* (Brussels, Belgium, Jan. 31, 2013), [http://ec.europa.eu/internal\\_market/copyright/docs/levy\\_reform/130131\\_levies-vitorino-recommendations\\_en.pdf](http://ec.europa.eu/internal_market/copyright/docs/levy_reform/130131_levies-vitorino-recommendations_en.pdf). See also *Mediation on private copying and reprography levies: António Vitorino presents his Recommendations to Commissioner Barnier* (IP/13/80), Jan. 31, 2013, [http://europa.eu/rapid/press-release\\_IP-13-80\\_en.htm?locale=en](http://europa.eu/rapid/press-release_IP-13-80_en.htm?locale=en).
- 11 See Competitiveness Council – 29-30 May 2013, MEMO/13/465, Brussels, 28 May 2013, [http://europa.eu/rapid/press-release\\_MEMO-13-465\\_en.htm](http://europa.eu/rapid/press-release_MEMO-13-465_en.htm).
- 12 See COUNCIL OF THE EUROPEAN UNION, Press Release, 3242nd Council meeting Competitiveness (Internal Market, Industry, Research and Space), Brussels, 29-30 May 2013, 10142/13, pp. 2, 8, [http://www.consilium.europa.eu/uedocs/cms\\_data/docs/pressdata/en/intm/137340.pdf](http://www.consilium.europa.eu/uedocs/cms_data/docs/pressdata/en/intm/137340.pdf).
- 13 See Art. 5(2)(b) of Directive 2001/29, 2001 OJ L167/10 [Copyright Directive].
- 14 See Part B.
- 15 The copyright *acquis* in the meaning ascribed to it herein includes the European Parliament and Council Directive 2009/24/EC (codified version), 2009 OJ (L 111/16) [Software Directive], European Parliament and Council Directive 2006/115/EC (codified version), 2006 OJ (L 376/28) [Rental Right Directive], European Parliament and Council Directive 2011/77/EU, 2011 OJ (L 265/1) [Term Directive], Council Directive 93/83/EEC, 1993 OJ (L 248/16) [Sat-Cab. Directive], European Parliament and Council Directive 96/9/EC, 1996 OJ (L 77/20) [Database Directive], the Copyright Directive, European Parliament and Council Directive 2001/84/EC, 2001 OJ (L 272/32) [Resale Right Directive], Directive 2004/48/EC, 2004 O.J. (L 195/16) [Enforcement Directive], and European Parliament and Council Directive 2012/28/EU, 2012 O.J. (L 299/5) [Orphan Works Directive].
- 16 For an in-depth analysis of this topic, see, inter alia, Karapapa, *Private Copying: The Scope of User Freedom In EU Digital Copyright* (Routledge 2012); Senfleben, *Copyright, Limitations and the Three-Step Test. An Analysis of the Three-Step Test in International and EC Copyright Law*, (The Hague, Kluwer Law International, 2004), pp. 246-281; Guibault, “Why Cherry-Picking Never Leads to Harmonization. The Case of the Limitations on Copyright under Directive 2001/29/EC”, JIPITEC (2010), 1 (2), pp. 55-66.; Bechtold, “Comment on Directive 2001/29/EC”, in Dreier & Hugenholtz (eds.), *Concise on European Copyright Law* (Alphen aan den Rijn, Kluwer Law International, 2006); and Walter & von Lewinski (eds.), *European Copyright Law: A Commentary* (Oxford, Oxford University Press, 2010), pp. 921-1141.
- 17 “WIPO Internet Treaties” is meant here as an umbrella term for the WIPO Copyright Treaty, opened for signature 20 December 1996, 2186 U.N.T.S. 121 (entered into force 6 March 2002) [WCT] and the WIPO Performances and Phonograms Treaty, opened for signature 20 December 1996, 2186 U.N.T.S. 203 (entered into force 20 May 2002) [WPPT].
- 18 See Ohly, “Economic rights”, in, *Research Handbook on The Future Of EU Copyright*, (E Derclaye [ed.], Edward Elgar 2009), pp. 212-241, p. 214, noting that “vertical harmonization” of the reproduction right had occurred for specific subject matter in the context of the Software Directive (Art. 4(a)), Database Directive (Art. 5(a)), and the repealed 1992 version of the Rental Right Directive (previous Art. 7, in respect of related rights). On the implementation of the WIPO Internet Treaties, see Recital 15 of the Copyright Directive.
- 19 Under Art. 7 of the Rental Right Directive (“fixation right”), which reads: “1. Member States shall provide for performers the exclusive right to authorise or prohibit the fixation of their performances. 2. Member States shall provide for broadcasting organisations the exclusive right to authorise or prohibit the fixation of their broadcasts, whether these broadcasts are transmitted by wire or over the air, including by cable or satellite. 3. A cable distributor shall not have the right provided for in paragraph 2 where it merely retransmits by cable the broadcasts of broadcasting organisations.”
- 20 See Ohly, supra note 18, pp. 214-215, raising formal and substantive objections to this legislative technique.
- 21 See Art. 9(1) of the Berne Convention for the Protection of Literary and Artistic Works of Sep. 9, 1886, completed at Paris on May 4, 1896, as revised at Paris on Jul. 24, 1971 and amended on Sep. 28, 1979 [Berne Convention], Arts. 7, 10 and 13 of the International Convention for the Protection of Performers, Producers of Phonograms and Broadcasting Organisations of Oct. 26, 1961 [Rome Convention], and 1(4) of the WCT. See also Agreed Statements to Arts. 7 and 11 WPPT.
- 22 See von Lewinsky, *Certain legal problems related to the making available of literary and artistic works and other protected subject matter through digital networks*, UNESCO ECOPYRIGHT BULL. 1, January-March 2005 issue, p. 5.
- 23 See ECJ, Case 5/08, Infopaq, [2009] ECR I-06569 [Infopaq], *passim* (applying such a broad interpretation), ECJ, Case 302/10, Infopaq II [2012] ECR I-00000 (narrowly interpreting exemptions for temporary acts of reproduction) and even ECJ, Joined Cases C-403/08 and C-429/08, Football Association Premier League and Others, [2011] ECR I-00000 [Premier League] (interpreting the reproduction right in Art. 2(a) Copyright Directive as extending to transient fragments of the works within the memory of a satellite decoder and on a television screen, although exempting such acts under Art. 5(1)).
- 24 See ECJ, Infopaq, Case 393/09 *Bezpečnostní Softwarová Asociace* [2010] ECR I-13971, Joined Cases Premier League, Case



- 145/10 Painer [2011] ECR I-00000 [Painer], Case C-604/10 Football Dataco [2012] ECR I-00000, and Case C-406/10 SAS [2012] ECR I-00000.
- 25 As examples of remuneration rights, see e.g. the right for an unwaivable and equitable remuneration for rental (Art. 5 Rental Right Directive) and the rights for single and equitable remuneration for broadcasting and communication to the public (Art. 8(2) Rental Right Directive). Rights of fair compensation for reprographic reproductions, private copying/use, reproductions of broadcasts by non-commercial social institutions and for use of orphan works by specific organizations can be found, respectively, in Arts. 5(2)(a), (b) and (e) of the Copyright Directive, and 6(5) of the Orphan Works Directive.
  - 26 Note also that Recitals 9 and 11 seem to favour an “in dubio pro autore” interpretation of this right. See Ohly, *supra* note 18, p. 217.
  - 27 Art. 5(1) of the Copyright Directive reads: “Temporary acts of reproduction referred to in Article 2, which are transient or incidental [and] an integral and essential part of a technological process and whose sole purpose is to enable: (a) a transmission in a network between third parties by an intermediary, or (b) a lawful use of a work or other subject-matter to be made, and which have no independent economic significance, shall be exempted from the reproduction right provided for in Article 2.”
  - 28 See Hugenholtz, et al.; *The Recasting Of Copyright And Related Rights For The Knowledge Economy*, Final Report, (2006), [http://ec.europa.eu/internal\\_market/copyright/docs/studies/et-d2005imnd195recast\\_report\\_2006.pdf](http://ec.europa.eu/internal_market/copyright/docs/studies/et-d2005imnd195recast_report_2006.pdf), pp. 68-69, arguing that this is a technical and not a normative approach.
  - 29 On the exhaustive nature of the catalogue of exceptions or limitations in Art. 5, see Recital 32 of the Copyright Directive.
  - 30 See Art. 5 (1)-(3) and (5) of the Copyright Directive.
  - 31 *Id.*
  - 32 See Art. 5 (3) and (5) of the Copyright Directive.
  - 33 *Cf.* Recital 36 of the Copyright Directive.
  - 34 The three-step test, which originally applied to the reproduction right, as stated in Art. 9(2) of the Berne Convention, currently extends to all economic rights, by virtue of Arts. 13 TRIPS, 10 WCT (and its Agreed Statements) and 16 WPPT. The Copyright Directive’s broad version of the same states that “[t]he exceptions and limitations provided for in paragraphs 1, 2, 3 and 4 shall only be applied in certain special cases which do not conflict with a normal exploitation of the work or other subject-matter and do not unreasonably prejudice the legitimate interests of the rightholder”. It should be noted that this test also applies to the Software Directive – Art. 6(3) – Database Directive – Art. 6(3) – and Rental Right Directive (by virtue of Art. 11(1)(b) of the Copyright Directive). A comprehensive analysis of the three-step test as implemented by the Copyright Directive is beyond the scope of this article, especially in what concerns the articulation of an open-ended interpretation of the test with an exhaustive catalogue of exceptions or limitations. On this topic, see Senftleben, “*The International Three-Step Test. A Model Provision for EC Fair Use Legislation*”, JIPITEC, Vol. 1 (2010).
  - 35 For in-depth analysis, see Walter & Von Lewinski, *supra* note 16, pp. 1013ff., Karapapa *supra* note 16, *passim*.
  - 36 See Bechtold, *supra* note 16, p. 375, and Walter & Von Lewinski, *supra* note 16, pp.1031-1032.
  - 37 See Art. 1(2)(a) and (e) of the Copyright Directive. See also van Eechoud, Hugenholtz, et al.: *Harmonizing European Copyright Law: The Challenges of Better Lawmaking*, Information Law Series 19 (Alphen aan den Rijn: Kluwer Law International 2009), p. 117. For an explanation of the historical background of this provision and the articulation of the recital with lit. (b), see Walter & Von Lewinski, *supra* note 16, p. 1031.
  - 38 See Walter & Von Lewinski, *supra* note 16, p. 1032, noting also that the term “private use” is present elsewhere in the *acquis* and international copyright law, namely Art. 15(1)(a) of the Rental Right Directive and Arts. 6(2)(a) and 9(a) of the Database Directive.
  - 39 *Id.* pp. 1032-1033.
  - 40 *Id.* p. 1033.
  - 41 *Id.* p. 1033.
  - 42 See Bechtold, *supra* note 16, p. 375.
  - 43 For an overview of the same, see Karapapa, *supra* note 16, pp.53-59.
  - 44 For a detailed analysis, see *id.* pp.49-78, proposing a test for the determination of the private character of the copyright use, which aims at assessing the relationship between the copier and the audience, the perception of the latter by the right-holder vis-à-vis the commercial exploitation of the work, and the (private) nature of the place where the use is made. For the concept of “public” in the *acquis*, see the most recent ECJ rulings dealing with the interpretation of the right of communication to the public, namely Case 306/05SGAE, [2006] ECR I-11519, Premier League, Joined Cases 431/09 and 432/09 Airfield, [2011] ECR I-00000, Case 135/10, Società Consortile Fonografici, [2012] ECR I-00000, and Case 162/10, Phonographic Performance (Ireland) Ltd, [2012] ECR I-00000.
  - 45 For a detailed analysis of this requirement, see Karapapa, *supra* note 16, pp. 79-98,
  - 46 *Id.* p. 80. See also Bernault, & Lebois (under the supervision of Lucas), *Peer-to-peer file-sharing and literary and artistic property: A feasibility study regarding a system of compensation for the exchange of works via the Internet*, trans. Smith & Palatezzi (Nantes: Institute for Research on private law, University of Nantes, 2006), [https://privatkopie.net/files/Feasibility-Study-p2p-acs\\_Nantes.pdf](https://privatkopie.net/files/Feasibility-Study-p2p-acs_Nantes.pdf), p.30.
  - 47 See Karapapa, *supra* note 16, p. 82.
  - 48 *Id.* p. 91, noting that the examination of the copier’s intent of commercial exploitation means that the judicial test for non-commerciality is not the exact counterpart of the definition of commerciality.
  - 49 For an attempt, see *id.* p. 98.
  - 50 See B.II.
  - 51 See Bechtold, *supra* note 16, p. 374, noting that both time and space-shifting might be covered by such *de minimis* cases.
  - 52 See, to this effect, *id.* p. 373 (“This link to the notion of harm, which is part of the concept of ‘fair compensation’ is alien to the concept of equitable remuneration”).
  - 53 See, concerning Art. 8(2) of the Rental and Lending Directive, ECJ, Case 245/00, Sena v. Nos, [2003] ECR I-1251, [2005] 3 CMLR 36 [Sena], paras 36-37, and ECJ, Case 192/04, Lagardère, [2005] ECR I-7199, [2005] 3 CMLR 48, p. 50.
  - 54 Art. 6(3) of the Copyright Directive.
  - 55 *Id.*
  - 56 Art. 6(1) and (2) of the Copyright Directive.
  - 57 In this sense, see Walter & Von Lewinski, *supra* note 16, p.1073.
  - 58 See Art. 6(4), first and second subparagraphs, of the Copyright Directive.
  - 59 Art. 6(4), third subparagraph, of the Copyright Directive.
  - 60 In this respect, Recital 39 of the Copyright Directive addresses the articulation of TPMs and digital private copying and remuneration schemes, urging Member States to take into consideration “technological and economic developments” when applying this exception and limitation, noting that the latter “should not inhibit the use of technological measures or their enforcement against circumvention”.
  - 61 Art. 6(4), fourth subparagraph, and Recital 53 of the Copyright Directive. It is the authors’ view that the term “interac-

- tive” makes reference to uses covered by the making available right under Art. 3 of the Copyright Directive.
- 62 “Agreed contractual terms” in this context seems to have a broad construction and likely applies also to standard form contracts such as typical online end-user license agreements. See Walter & Von Lewinski, *supra* note 16, p. 1074, (n. 482). For a more restrictive view, arguing for the application of the provision solely to negotiated and agreed terms, see Guibault, Westkamp, et al.; *Study on the Implementation and Effect in Member States’ laws of Directive 2001/29/EC on the Harmonisation of Certain Aspects of Copyright and Related Rights in the Information Society, report to the European Commission, DG Internal Market* (February 2007), p.112 (“the exception to the main rule of article 6(4) of the Directive could be interpreted as applying only in respect of the supply of online services for which the contracting parties have negotiated the terms of use...”).
- 63 See van Eechoud, Hugenholtz, et al.; *supra* note 37, p. 118, raising the possibility that, for cases where the application of TPMs makes PC activities impossible or near impossible (e.g. copy controls on DVDs), no compensation should be claimed as it would be unjustified.
- 64 See Hugenholtz, Guibault, & Van Geffen, “*The Future of Levies in a Digital Environment*”, Institute for Information Law (March 2003), *passim*, and Van Eechoud, Hugenholtz, et al.; *supra* note 37, p. 118. *Contra* the argument that the Directive provides for automatic phasing out of levies, see Walter & Von Lewinski, *supra* note 16, p.1034.
- 65 See ECJ, Case 467/08, *Padawan SL v. SGAE*, [2011] ECDR 1 [Padawan],
- 66 See ECJ, Case 462/09, *Stichting de ThuisKopie v. Opus Supplies Deutschland GmbH*, [2011] 3 C.M.L.R. [Stichting de ThuisKopie], *passim*.
- 67 Joined ECJ, Cases C-457/11, C-458/11, C-459/11, C-460/11, *Verwertungsgesellschaft Wort (VG Wort) v. KYOCERA Document Solutions Deutschland GmbH and Others, Canon Deutschland GmbH and Fujitsu Technology Solutions GmbH, and Hewlett-Packard GmbH v. Verwertungsgesellschaft Wort (VG Wort)*, [2013] I-00000 [VG Wort v. Kyocera]. This judgement results from references for a preliminary ruling from the Bundesgerichtshof (Germany) made in the context of proceedings between a German collecting society (VG Wort) and several intermediary suppliers (Kyocera, Epson, Xerox, Fujitsu and Hewlett Packard) concerning the compensation to be paid to the first by the latter as a consequence of the placement on the market of devices capable of copying, such as printers, plotters and personal computers
- 68 Opinion of Advocate General Sharpston delivered on 24 January 2013, Joined Cases C-457/11, C-458/11, C-459/11 and C-460/11 [A.G. Sharpston Opinion].
- 69 See ECJ, Case C-521/11, *Amazon.com International Sales Inc. and Others v. Austro-Mechana Gesellschaft zur Wahrnehmung mechanisch-musikalischer Urheberrechte Gesellschaft m.b.H.*, [2013] I-00000 [Amazon.com v. Austro-Mechana]. This judgement deals with the interpretation of “fair compensation” in the context of a national levy scheme that targets all recording media, irrespective of their purposive use, but provides debtors with an (enforceable) right of ex post reimbursement against the CMOs collecting where the levied media is exported before it is sold to consumers. See also Opinion of Advocate General Paolo Mengozzi delivered on 7 March 2013, Case C-521/11.
- 70 See Padawan, paras. 44-45.
- 71 *Id.* para. 46.
- 72 *Id.* noting that the referred intermediaries are responsible for discharging the private copying levy.
- 73 *Id.* para. 57, referring that the incompatibility with the Copyright Directive occurs when the levy is applied to equipment/devices/media “clearly reserved for uses other than private copying” (emphasis added). Stichting de ThuisKopie tested this rule in the context of cross-border sales within the EU of equipment/devices/media through distance-selling arrangements, elucidating that the relevant harm occurs in the territory of residence of the end-user. See Stichting de ThuisKopie, para. 35. *Amazon.com v. Austro-Mechana* clarified *inter alia* that indiscriminate application of the levy is only admissible subject to a specific set of cumulative conditions, including the provision of an enforceable right of reimbursement of the intermediary first placing a recorded media on the market. See *Amazon.com v. Austro-Mechana*, paras. 16-37.
- 74 See Padawan, para. 31.
- 75 *Id.* para. 32. See also: ECJ, Case 327/82, *Ekro* [1984] ECR 107, para. 11; ECJ, Case 287/98, *Linster*, [2000] ECR I-6917, para. 43; and ECJ, Case 523/07 A, [2009] ECR I-2805, para. 34.
- 76 See Padawan, paras. 32 and 37, applying by analogy to the concept of “equitable remuneration” in Art. 8(2) of the Rental Right Directive. See also Sena, para. 24.
- 77 See Padawan, paras. 34-35. See also Premier League, para. 186, identifying the principal objective of the Copyright Directive as the establishment of a “high level of protection of authors, allowing them to obtain an appropriate reward for the use of their works”. See also ECJ, Case 510/10, *DR and TV2 Danmark*, [2012] ECR I-00000, para. 35.
- 78 See Recital 31 of the Copyright Directive. For the use of the fair balance criteria in Recital 31 within the context of the Court’s systematic interpretation of provisions in the directive, see Painer, para. 132.
- 79 See ECJ, Case 277/10, *Luksan*, [2012] ECR I-00000 [Luksan], para. 100.
- 80 *Id.* para. 102.
- 81 *Id.* paras. 104-105.
- 82 See Stichting de ThuisKopie, para. 34.
- 83 See Luksan, para. 106.
- 84 See Padawan, para. 7.
- 85 *Id.* paras. 39-41. Recital 38 allows Member States, in the context of analogue PC, to keep in place or introduce “remuneration schemes to compensate for the prejudice to right-holders”, as these would only have a negligible impact on the functioning of the internal market. Conversely, digital PC, due to its likelihood “to be more widespread and have a greater economic impact”, requires fair compensation to be assessed differently.
- 86 See Padawan, para. 40, and Stichting de ThuisKopie, para. 24.
- 87 See Padawan, para. 42.
- 88 See B.II.
- 89 See discussion at C.II, E.II and E.III.
- 90 See VG Wort v. Kyocera, para. 40
- 91 *Id.* paras. 34-35
- 92 *Id.* para. 36.
- 93 *Id.* paras 37-39.
- 94 *Id.* paras 37-39.
- 95 A.G. Sharpston Opinion, para. 119.
- 96 *Id.* paras 119-121 and 137, fourth indent.
- 97 See Part C. This is namely the case of the recommendation that copies made by “end users for private purposes in the context of a service that has been licensed by rightholders do not cause any harm that would require additional remuneration in the form of private copying levies”.
- 98 See VG Wort v. Kyocera, paras. 48-52.
- 99 *Id.* paras. 48-57.
- 100 *Id.* para 58.
- 101 A.G. Sharpston Opinion, para. 104.

- 102 Reference for a preliminary ruling from the Oberster Gerichtshof (Austria) lodged on 29 June 2012, Case C-314/12, UPC Telekabel Wien GmbH v. Constantin Film Verleih GmbH, Munich (Germany), Wega Filmproduktionsgesellschaft mbH [UPC Telekabel v. Constantin Film].
- 103 Reference for a preliminary ruling from the Østre Landsret (Denmark) lodged on 16 October 2012, Case C-463/12, Copydan Båndkopi v. Nokia Danmark A/S [Copydan Båndkopi v. Nokia].
- 104 Reference for a preliminary ruling from the Hoge Raad der Nederlanden (Netherlands) lodged on 26 September 2012, Case C-435/12, ACI Adam BV and Others v. Stichting de ThuisKopie and Others [ACI Adam and Others v. Stichting de ThuisKopie].
- 105 See Copydan Båndkopi v. Nokia.
- 106 See *id.*, respectively, questions one through six and variations thereof.
- 107 See ACI Adam and Others v. Stichting de ThuisKopie.
- 108 See UPC Telekabel v. Constantin Film, second question: “... Are reproduction for private use (Article 5(2)(b) of the Information Directive) and transient and incidental reproduction (Article 5(1) of the Information Directive) permissible only if the original of the reproduction was lawfully reproduced, distributed or made available to the public?”
- 109 An issue dealt with in detail in ACI Adam and Others v. Stichting de ThuisKopie, UPC Telekabel v. Constantin Film, Copydan Båndkopi v. Nokia, and only indirectly mentioned in the Recommendations.
- 110 See VG Wort v. Kyocera, paras 48-59. See also A.G. Sharpston’s Opinion, paras. 94-104.
- 111 See *supra* note 11.
- 112 See Vitorino, *supra* note 10, pp. 2-4.
- 113 *Id.* p. 3.
- 114 *Id.* p. 3.
- 115 *Id.* p. 3.
- 116 *Id.* pp. 3-4.
- 117 *Id.* pp. 6-9.
- 118 *Id.* pp. 10-23.
- 119 *Id.* p. 9.
- 120 *Id.* p. 6.
- 121 *Id.* pp. 7-8.
- 122 *Id.* pp. 8-9.
- 123 See A.G. Sharpston Opinion, paras. 105-121.
- 124 *Id.* paras. 120-121, and 137, fourth indent.
- 125 VG Wort v. Kyocera, paras. 37-40. See above B.II.3.
- 126 See Vitorino, *supra* note 10, p. 8.
- 127 See Communication from the Commission on content in the Digital Single Market, COM(2012) 789 final, Brussels, 18.12.2012. See also Licenses for Europe, [http://ec.europa.eu/internal\\_market/copyright/licensing-europe/index\\_en.htm](http://ec.europa.eu/internal_market/copyright/licensing-europe/index_en.htm).
- 128 See Vitorino, *supra* note 10, pp. 10-11.
- 129 *Id.* p.11.
- 130 *Id.* p.11.
- 131 Because this article does not focus on the exception/limitation of reprography, Mr Vitorino’s recommendations that “more emphasis should be placed on operator levies than on hardware based levies” shall not be addressed. See Vitorino, *supra* note 10, p. 16-17.
- 132 *Id.* p. 12.
- 133 *Id.* pp. 15-18.
- 134 *Id.* pp. 18-19.
- 135 *Id.* p. 19.
- 136 *Id.* pp. 21-23.
- 137 *Id.* p. 22. In this context, Mr Vitorino set forth the following minimum standards for the tariff-setting process: (i) decisions on the application of a levy to a product are to be taken within one month post-market introduction; (ii) provisional/transitional tariff levels should be set within three months post-market introduction; (iii) the definitive tariff level is to be set within six months post-market introduction; (iv) in principle, the definitive level should be equal or inferior to the provisional level; if superior, the payment of the difference should be gradual.
- 138 *Id.* pp. 21 and 23.
- 139 *Id.* p. 20.
- 140 *Id.* p. 20.
- 141 *Id.* p. 20.
- 142 *Id.* p. 20.
- 143 *Id.* pp. 20-21.
- 144 *Id.* p. 21.
- 145 See Karapapa, *supra* note 16, pp. 15-27, and Hugenholtz, *supra* note 4, *passim*.
- 146 At the time of writing, the UK is in the process of implementing into law a narrow and uncompensated private copying exception. See Technical review of draft legislation on copyright exceptions, Private Copying (7 June 2013), UK Intellectual Property Office, <http://www.ipso.gov.uk/techreview-private-copying.pdf>.
- 147 See Art. 13 of the Enforcement Directive.
- 148 Art. 13(1)(a) of the Enforcement Directive.
- 149 See Art. 13(1)(b) of the Enforcement Directive; emphasis added.
- 150 See Vitorino, *supra* note 10, p. 20.
- 151 See WIPO, International Survey..., *supra* note 5, p. 4. The WIPO survey explicitly identifies a number of countries – The Netherlands, Russia, Switzerland and Canada – as not having a specific rule on the lawful nature of the source of PC acts. However, it should be noted that other countries not expressly identified, such as Portugal, also lack such a provision, which raises concerns as to accuracy of the survey. In such cases where the source or access are deemed irrelevant, rightholders are still entitled to pursue parties responsible for the unlawful making available (and in certain cases access) of their works.
- 152 See, e.g. §53(1) of the German Copyright Act (UrhG) and Art. L 122-5 (2) of the French Intellectual Property Code (Code de la Propriété Intellectuelle).
- 153 These terms are usually used in the broader discussion of private uses. See Senftleben, *supra* note 16, pp. 204-206, *presciently* discussing private uses which, although primarily consumptive in nature, form the basis of future creations. For the author, these uses (which cover many modalities of PC) must remain within the scope of exceptions or limitations, for reasons of intergenerational equity. On the concept of dynamic PC, see Karapapa, *supra* note 16, pp. 40-48, which distinguishes between “passive” private use (giving rise to “permitted” uses) and “dynamic” private use, affective both the reproduction right and other exclusive rights, which gives rise to “permissible” uses.
- 154 See Vitorino, *supra* note 10, p. 21.
- 155 Importantly, guidance on the *de minimis* qualification of the prejudice is forthcoming in Copydan Båndkopi v. Nokia.
- 156 Exceptions include the UK and Ireland, which so far have not introduced a private copying exception other than for time-shifting TV content; and Malta, Cyprus and Luxembourg, which treated private copying as *de minimis*. See M. Kretschmer, Private Copying and Fair Compensation. An empirical study of copyright levies in Europe, UK Intellectual Property Office (2011), p. 10. On the narrow uncompensated private

copying exception to be introduced into UK law, see Technical review of draft legislation on copyright exceptions, *Private Copying*, supra note 146.

- 157 See Art. 1(2)(a) of the Copyright Directive.
- 158 See WIPO, *International Survey...*, supra note 5, pp. 13-14.
- 159 Id.
- 160 A somewhat different typology can be found in Kretschmer, supra note 156, pp. 9, 70, which sums up activities that users may consider private. Kretschmer also mentions user-generated content, uploading and online publication, performance and distribution within networks of friends as separate categories. These are ignored here as they are not considered to fall under the PC exception. The reason is that they partially or wholly involve acts that can be legally qualified as communication/making available to the public under Art. 3 of the Copyright Directive.
- 161 Insofar as these activities are covered by the PC exception due to an extended definition of the requirement “private” (which may include, e.g., the circle of people mentioned). See B.I.2.
- 162 See WIPO, *International Survey...*, supra note 5, p. 4.
- 163 One could also argue that making copies of legally borrowed or rented content – type (d) – is a form of time shifting (beyond the rental period) rather than an extension of the circle of consumers.
- 164 See Liebowitz, “*Copying and Indirect Appropriability: Photocopying of Journals*”, *Journal of Political Economy*, 93 (5), 945-957 (1985).
- 165 Id. p. 945.
- 166 Besen & Kirby, “*Private Copying, Appropriability, and Optimal Copying Royalties*”, *J. Law Econ.* 32 (2), 255-280 (1989). Like other models discussed in this article, the models Besen and Kirby develop ignore possible positive dynamic effects of the consumption of copies on future sales (the so-called “sampling effect”) and negative effects of lost sales on the future production of content.
- 167 Id. p. 280.
- 168 Varian, “*Copying and Copyright*”, *Journal of Economic Perspectives*, 19 (2), 121-138 (2005).
- 169 In relation to the Dutch PC levies, see e.g. Verhue & Hillhorst, *Gebruik van opslagmedia: twintigste meting* (Amsterdam: Veldkamp) (2012) and PwC, *Thuiskopie: Onderzoek naar gedeerde inkomsten door huiskopie thuiskopieën* (2012).
- 170 Time shifting of TV content is a somewhat different issue: advertisers will be aware that some of their ads will be skipped when consumer watch programmes they recorded. This will lower advertising revenues for channels, while increasing consumers’ willingness to pay for TV channels and recorders.
- 171 Not everyone would agree that RHs have a natural claim to any benefits from these unforeseen uses.
- 172 For an example of the first, see Koelman, “*The Levitation of Copyright: An Economic View of Digital Home Copying, Levies and DRM*”, *Entertainment Law Review*, 4, 75-76-81 (2005). For an example of the second, see Elkin-Koren & Salzberger, *The Law and economics of intellectual property in the Digital Age – The limits of analysis* (Routledge, 2013), pp. 184-185.
- 173 See explanation of the extant legal framework above at B.I.2.
- 174 See Koelman, supra note 172, pp. 75-76 and 81.
- 175 Quoted in Sinha, Machado & Sellman, “*Don’t Think Twice, It’s All Right: Music Piracy and Pricing in a DRM-Free Environment*”, *Journal of Marketing*, 74 (2), 40-54 (2010).
- 176 See id.
- 177 See Vernik, Purohit & Desai, “*Music Downloads and the Flip Side of Digital Rights Management*”, *Marketing Science*, 30 (6), 1011-1027 (2011).
- 178 See Sinha et al., supra note 175, passim, and Vernik et al., supra note 177, passim.
- 179 See Sinha et al., supra note 175, passim.
- 180 Id. p. 40.
- 181 Hugenholtz, Guibault et al., supra note 64, p. 4.
- 182 See B.II.4.