

# **Regulating copyright contracts: economics and fair remuneration**

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# Overview of economics of copyright

- Copyright fits into two paradigms: market failure (welfare econ) and property rights (Coase).
- Welfare econ – under-production due to free-riding. Implies a move towards ‘optimal’ level; not 1<sup>st</sup> best (Pareto) but 2<sup>nd</sup> best. Social efficiency – max societal wellbeing may require state intervention.
- Property rights – transaction costs, risk, contract theory (incomplete contracts). Private efficiency -> invisible hand.
- Both support copyright as a means to achieve the objective of incentivising creativity as an efficiency measure but see it as a trade-off between incentive to create and disincentive to use (access).
- Copyright leads to price above marginal cost of the marketed work – difference finances the reward to the creator. It only works via the market.
- Capitalism is not a system for fair distribution of income! Economists struggle with analytical rules for fairness.
- Equity measures have efficiency effects – reallocate resources (2<sup>nd</sup> best). Requires evidence not principles.
- Many economists dispute case for copyright law: other policy measures – state support, grants, prizes, tax breaks et al. Old view was that first to market had monopoly; depends on cost of copying ie business model sufficed to protect author/publisher.

# What is the copyright incentive to the author?

- Copyright does not ENSURE reward. If the work is marketed, financial reward MAY be forthcoming. Payment by fixed upfront fee or royalty depends on market value of work (or combination).
- Financial reward may or may not matter to author/performer; so might reputational reward. Intrinsic/extrinsic motivation. Copyright with moral right provides both.
- Many creators/performers are employed, often with payment set by collective-bargained agreements. US 'works made for hire'. Copyright plays small role.
- Extent of employed vs self-employed workforce in creative industries varies with institutional arrangements eg state provision for arts, level of subsidy.
- Royalty is an ex post incentive (grant is ex ante). All that the author knows ex ante is the royalty rate, not even the basis eg retail price of work. The contract is a statement of hope not of the amount of the payment. Both parties share risk.
- Like the publisher, the author has to finance later work by income from former work. The time lags in royalty payments are very long for an individual creator.

# Contracts in creative industries

- Collectively bargained standard contracts exist for many self-employed (freelance/'free') authors eg journalists. Reduce transaction costs. Collectively bargained fees are probably reliable than copyright royalties.
- Principal agent: author contracts with publisher to invest in marketing her work. Uncertainty prevails in launching new (novel?) work (but not in reissuing old catalogue). Asymmetries in willingness to bear risk and time preference. Publisher can wait longer (lower time pref.) than author.
- Contracts trade-off risk between parties – author, publisher. Both risk-averse but author less able to bear risk. Publisher can pool risk.
- Contracts are incomplete - concerned with possible post signing events eg new technology for distribution (some contracts now relate to 'universe' and all unknown technologies - attempt to be complete).
- Creative industries have differing chain of production. Contracting follows investment in the process and risk occurs sequentially eg film. Danger to investor of hold-ups eg film – finance from pre-sales; co-productions. Buy-out fees avert hold-ups.
- Buy-out vs royalty contracts: depends on author's time preference; some prefer money upfront.
- Advance attempts to deal with moral hazard: increases incentive to publisher to comply.

# Contract reversion and fair remuneration

- What parties agree to is mostly regarded as a 'fair deal'. However, copyright now so complex that many authors do not understand it. More tinkering with copyright makes things worse in that respect. Only the successful can pay for advice.
- Labour market for most creative professions – oversupply, superstar, winner-takes all, no career structure (depends on talent), unpredictable type and amount of work etc.
- Competition between authors leads to a race to the bottom: collective bargaining and collective rights management needed to obtain the fairest possible deal. Shapley value – all participants have to accept 'average'. CMOs more or less operate on this rule – threat from cherry-picking.
- Reversion right basically opens up possibility of competition between publishers. In regimes with reversion right, contracts likely to anticipate reversion with lower initial offer.
- What rules can we think of for fairness? Suggestion: Royalty should be proportional to investment by each party. Every one talks about the publisher but not about opportunity cost of authors' time/effort in creating a work. However, strong incentive to cheat and difficult to verify.
- Role of trust and reputation: eg choreographers barely exercise copyright. 'Closed' markets eg diamonds use implicit contracts and social pressure to enforce.
- Research needed to analyse court cases about reversion – terms of contracts, basis for claim, type of work involved and type of author.

# Questions for further research

- Looking at the purely legal aspects (as per the EU docs) ignores the markets (labour and product markets) in which the law operates. Scope for equivalent research similar to the existing studies. Some could be done from official data and some from surveys.
- How extensive are collectively bargained contracts and rates in the creative industries of? How widespread is 'free' contracting? (I suspect a small proportion – depending on how you define the labour force in them).
- What choice authors would make if offered between royalty/buy-out?
- What is effect of reversion on markets? an increase of output? That's what copyright is for - isn't it?
- We must consider whether the law is the best way to support creativity in the digital era. There are other means! Why not conduct the same Reimagining exercise among non-lawyers?