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# OVERVIEW

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## Key points

- Parallel Import Restrictions (PIRs) provide territorial protection for the publication of many books in Australia, preventing booksellers from sourcing cheaper or better value-for-money editions of those titles from world markets.
- From the available quantitative and qualitative evidence, the Commission has concluded that the PIRs place upward pressure on book prices and that, at times, the price effect is likely to be substantial. The magnitude of the effect will vary over time and across book genres.
- Most of the benefits of PIR protection accrue to publishers and authors, with demand for local printing also increased.
- Most of the costs are met by consumers, who fund these benefits in a non-transparent manner through higher book prices.
- Some of the effects represent transfers from book purchasers to local copyright holders, but the restrictions also cause economic inefficiencies and a significant transfer of income from Australian consumers to overseas authors and publishers.
- Consumers of culturally significant books directly benefit from their cultural value. At the same time, the PIRs make a contribution to the 'cultural externalities' of books that benefit the broader community.
- PIRs are a poor means of promoting culturally significant Australian works.
  - They do not differentiate between books of high and low cultural value.
  - The bulk of the assistance leaks offshore, and some flows to the printing industry.
- Reform of the current arrangements is necessary, to place downward pressure on book prices, remove constraints on the commercial activities of booksellers and overcome the poor targeting of assistance to the cultural externalities.
- The reform option proposed in the discussion draft was for a 12 month territorial protection within the existing framework. Many participants claimed that it would cause undue distortions between different genres of books. There was also mixed, but critical, commentary about its impact on the industry.
- Having considered industry feedback and undertaken further analysis, the Commission is recommending that the PIR provisions be repealed, and that:
  - Three years notice should be given to facilitate industry adjustment.
  - Current financial assistance for encouraging Australian writing and publishing should be reviewed immediately, and any changes implemented prior to the repeal of the PIRs. The new arrangements should be reviewed after five years.
  - To assist in monitoring the impact of these changes, the ABS should undertake a revised version of its 2003-04 industry survey as soon as possible and update it prior to the five year review.

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# Overview

Australians are avid book readers. New book sales have recently been running at around \$2.5 billion per annum. While books are primarily sources of information, interest and entertainment, they can also be tools of learning or earning, repositories of history or markers of cultural identity. Reading also improves literacy, which is fundamental to individual wellbeing and to the smooth functioning of society and the economy.

The Commission has been requested to examine the various effects of the restrictions on the parallel importation of books that have been published in Australia, and to assess whether the restrictions should be retained, modified or repealed. This final report completes the Commission's analysis. It follows on from the March discussion draft, feedback on that draft and subsequent further analysis by the Commission.

## **The books market**

The books market displays considerable diversity. 'Trade' books, which account for around 60 per cent (by value) of new book sales, range from narratives published in monocolour (novels, histories, biographies etc.) to children's stories and special interest colour books (food, gardening, travel etc.). The other 40 per cent of sales comprise educational, professional and reference texts.

Trade books produced by publishers are sold through a variety of channels. There is strong retail competition on a range of 'front list' titles, with many discount department stores frequently selling bestsellers for substantially less than the recommended retail price. This puts some pricing pressure on the retail book chains, while independent bookstores compete more on levels of customer service. An increasing number of Australians have been bypassing local 'bricks and mortar' bookshops and purchasing online. Consumers can also access books from libraries, friends and family or purchase them second-hand.

In the education sector, competition between publishers for a textbook to be adopted for a particular course is focussed on the lecturer and other decision-makers, rather than on the student purchasers.

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The Commission estimates that around one-third of all trade books sold in Australia are Australian-authored, and that more than two-fifths (by value) of trade books (whether written by local or foreign authors) are locally published. Most of Australia's larger trade publishers are local arms of foreign companies, as are the main specialist education publishers.

A significant proportion of the books published in Australia is also printed here. There are two main plants: one in Adelaide and the other in regional Victoria. They produce predominantly monochrome paperbacks; most colour printing is sourced off-shore.

## **Parallel import restrictions**

The reproduction and first sale of books in Australia is governed by the *Copyright Act 1968*. In essence, copyright law aims to achieve a balance of incentives for the creation and diffusion of creative works, including books. This core copyright protection, which provides incentives for creative endeavour *per se*, is not the subject of this study.

Separate and additional to the core copyright protections, the Act contains Parallel Import Restrictions, or 'PIRs', which largely protect publishers and authors who hold the Australian rights to a title from competition by suppliers of foreign editions of that title. The mechanics of the PIRs are set out in box 1.

All major English language markets, including the United Kingdom (UK), the United States (US) and Canada, also have PIRs, although without time requirements for first publication. New Zealand, on the other hand, is an unrestricted market (although it operates, in practice, largely as part of a collective 'ANZ' market).

## **The study's scope and approach**

The terms of reference (set out at the front of the report) have several facets, but in essence the Commission has been requested to assess:

- the benefits and costs of the PIRs
- the merits of options for reform.

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**Box 1      The mechanics of the parallel import restrictions**

For a title to qualify for protection under the PIRs, the Australian territorial rights holder must release the book in Australia within 30 days of it being published elsewhere in the world, and must maintain a capacity to resupply it within 90 days. There are some exceptions to the restrictions — consumers can purchase books from abroad, for example via the internet and, under the ‘single use’ provisions, a bookseller can purchase a single copy of a book that would otherwise be PIR-protected, to fill a specific customer order.

Under the PIRs, if a particular novel or textbook is published in Australia within the 30 day limit, booksellers cannot import and sell stocks of the same book from, say, the UK, the US or Asia. This enables rights holders to charge prices (or obtain royalties) in the Australian market with the certainty that they cannot be undercut by commercial quantities of imports of the same titles.

Assistance from Australia’s PIRs is not limited to Australian publishers and authors. The publishers who benefit from territorial protection can be Australian businesses, Australian arms of international companies or international companies operating from other countries. Likewise, the works of both Australian and foreign authors are equally protected from parallel imports into Australia.

In making such assessments, the Commission interprets ‘benefits’ and ‘costs’ in their fullest sense — that is, covering the value of social, cultural and educational matters, as well as financial or material ones — and assesses them within a community-wide framework. Thus, while the terms of reference require that regard be had to the effects of PIRs on all relevant industry parties, the Commission has not directed its interest only to the impacts on copyright holders or other stakeholders in the books industry. What matters ultimately is the wellbeing of the community as a whole.

In preparing this report, the Commission consulted as widely as possible within the timeframe provided for the study. Prior to the release of the discussion draft, it held discussions with more than 30 industry stakeholders and government bodies, and received more than 270 submissions. Four workshops were convened to facilitate debate about the draft and around 290 further submissions were received. Industry participants also helpfully clarified various issues when approached by the Commission. The Commission was granted an extension of the reporting date to 30 June 2009.

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## Assessing the benefits and costs

Conceptually, PIRs are similar to other import restrictions in that they benefit local producers by cushioning or shielding them from foreign competition. Experience in other sectors has shown that import restrictions can adversely affect consumers through the availability, quality and prices of the goods or services concerned, and can have broader resource efficiency costs.

In terms of availability, as a result of reforms to the PIRs in 1991, most books are now published in Australia in a timely manner. There also appears to be no general problem with the quality of service.

Most of the key impacts of the PIRs therefore stem from their effects on book prices.

### Price impacts

Many previous studies have sought to measure the price impacts of PIRs by comparing book prices in Australia with the prices of the same titles in the UK and the US. Several study participants submitted similar comparisons. While these comparisons reveal no clear and consistent pattern, they suggest at a minimum that some books are available at a lower price overseas. They also demonstrate, unsurprisingly, that the strength of the Australian dollar has a major influence on measured price differences at any point in time.

The Commission has also undertaken its own, more extensive, analysis of international book price data.

The analysis demonstrates that ‘like editions’ of many current list trade books are sold at a lower price in the UK and/or the US than in Australia. In some instances, the price differential is substantial. For example, the Commission’s price comparisons found that, in 2007-08, a selection of around 350 trade books sold in Australia were on average 35 per cent more expensive than like editions sold in the US (even after accounting for the effects of GST). In many cases, the price difference was greater than 50 per cent. And when the Commission extended the range of editions of titles that it was comparing, the price differences widened further.

While recognising the inherent limitations of price comparisons, these results together with other available evidence make it clear that, but for the PIRs, Australian booksellers could have obtained and shipped many trade titles to Australia for significantly less than they are currently charged by Australian publishers. Of course, were PIRs not in place, local publishers may be more attentive to the prices of competing foreign editions when setting their own prices.

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When the Australian dollar is relatively weaker against other currencies, as it was for much of 2008-09, average price differentials will be smaller or may even reverse in direction. That is, it is possible that the *average* price of trade books in Australia will in some years be lower than the *average* price of equivalent editions in the UK and/or US. However, given the wide spread of price differentials around the average, and the availability at times of cheaper formats overseas, there are still opportunities in such periods to source some current list trade books at a lower cost to booksellers from the UK or US. And while there is already an extensive trade in remainders in Australia, this could extend further were the PIRs to be abolished.

In the educational books sector, English-language textbooks sold in Asia, some of which are essentially identical in content to those sold in Australia, concurrently sell for less than half the price of Australian editions (which, themselves, often sell for 30 per cent below US prices).

In analysing the comparisons, it is relevant to remember that prices in the UK and US markets are themselves inflated by restrictions on parallel book imports. Different import sources might emerge for some titles in the absence of the PIRs in Australia.

More generally, the greater actual or potential overseas competition consequent on the removal of the PIRs would increase the pressure on parts of the local industry to improve their efficiency. This may also lower prices. While there have been productivity gains to date, a number of study participants identified distribution, in particular, as having scope for greater improvement.

In sum, drawing on a range of quantitative and qualitative evidence, the Commission concludes that the PIRs place upward pressure on book prices and that, at times, the price effect is likely to be substantial. The magnitude of the effect will vary over time and across book genres.

## **Effects of the PIRs on the books sector and the broader economy**

The PIRs can benefit activity and employment in the production side of the local books industry in a range of ways:

- By protecting higher monetary returns from rights trading and local publishing activity, the PIRs enable publishers to increase their publishing portfolio and obtain some economies of scale and scope.
- In lessening import competition, PIRs provide greater certainty for local publishers and authors in investing resources in the production and creation of particular titles.
- The 30 day release rule encourages the timely publication of foreign-authored books in Australia, and there is greater demand for book printing in Australia.

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The higher prices charged by publishers that underpin these industry benefits are paid for in the first instance by booksellers, who are constrained in their dealings with publishers. Unlike overseas online book retailers, local booksellers are unable to take advantage of opportunities to supply cheaper imported editions of those titles that are currently protected. Ultimately, these costs flow on to consumers.

The PIRs will also have some diffuse effects on activity and employment in industries outside the books sector. Higher book prices can reduce consumer spending on other goods and services, while the expansion of book production reduces the resources available to other industries.

### **Net community-wide impacts**

Many of the benefits and costs of PIRs represent a transfer of resources from consumers and other industries to book producers. As such, they do not constitute a net benefit or net cost to the Australian economy, although they do have distributional implications. In particular, the higher prices arising from territorial protection disadvantage consumers.

There are also three categories of benefits and costs that do not ‘wash out’. These are central to the calculation of the net benefits or costs of the PIRs.

Support of a larger publishing industry and, as a consequence, more Australian authorship results in a greater portrayal of Australian events, as well as stories that are told by Australian voices.

Much of this cultural value of books is likely to be obtained directly by the readers, and captured in the prices paid in purchasing the books. Consumers typically choose some books because they potentially embody cultural value or may be culturally enriching to read. The Australian community more broadly benefits from these private actions — that is, there is a positive ‘externality’. PIRs contribute to those externalities.

The PIRs poorly target the cultural externalities. At one level, the higher prices benefit all protected titles, whatever their cultural merit, and, indirectly, benefit the broader range of books as well. And much of the ‘assistance’ provided by PIRs does not promote Australian-authored works.

In this context, much of the additional income from the higher book prices goes to overseas authors and publishers whose works are released in Australia. Indicative Commission estimates suggest that the additional income flowing overseas is around 1.5 times that retained by local copyright holders. In effect, PIRs impose a

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private, implicit tax on Australian consumers which is used largely to subsidise foreign copyright holders.

The PIRs also create a range of economic inefficiencies. Among other things, they lessen the imperative for the local book industry to operate at best practice. They also distort economic resources away from their highest value uses. As with trade barriers in other industries, the existence of these costs does not depend on whether other countries also have protected markets.

## **Assessing the policy reform options**

The Commission has concluded that the current arrangements are in need of reform, and has explored four main reform approaches.

### **Reducing the period of territorial protection**

In its discussion draft, the Commission proposed a set of reforms within the existing policy framework to reduce the adverse effects of the current PIR regime on the community while preserving assistance for Australian writing in recognition of the cultural externalities it supports.

In particular, the Commission proposed that the restrictions on parallel imports should apply for only 12 months from the date of first publication of a book in Australia, rather than the full term of copyright. This approach to reform would have enabled publishers to develop, publish and market new titles, establish lines of supply with booksellers and have guaranteed rights over all sales in the first year. This first-mover advantage, together with other advantages of local supply, would also have given local publishers a firm basis for competing with other suppliers for the remainder of a book's sales history.

Industry participants generally rejected the Commission's draft proposal, and drew attention to the distortions that it may cause between different genres of books, given their different sales patterns. Many authors, publishers and printers also considered that the outcome from the option proposed in the discussion draft would be much the same as full abolition of PIRs. On the other hand, some booksellers considered that the reform would do little to generate lower prices or improve efficiencies within the industry. In light of this response, the Commission undertook further analysis of the industry, carefully considered all submissions and reassessed the policy alternatives.

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## **Other reforms within the existing framework**

The Commission examined a range of other proposals that, either alone or in conjunction with other measures, might generate further competitive pressure, while retaining the framework of the PIRs.

One proposal was the retention of PIR protection only for books authored by Australian writers. It has some in-principle appeal as it could reduce both book prices and income leakage, while providing some support to realise the cultural externalities associated with local writing and publishing. However, it would run foul of international treaties to which Australia is a party, as would a proposal to protect ‘Australian versions’ of books.

Some participants advocated a price-cap model, wherein Australian publishers, to retain PIR protection on their titles, would need to keep their prices within check of foreign wholesale prices. While this would put some pressure on local prices, such a scheme would be complex to design, may have some unintended pricing impacts, and would remain a blunt instrument for targeting cultural externalities.

While the price cap model, and other proposals such as shortening the 90 day resupply rule, represent a potential improvement on the status quo, more robust reform options are likely to deliver greater net benefits.

## **Repealing the PIRs**

Given the flaws with the existing scheme as outlined earlier, and the lack of viable options for significant reform within the PIR framework, the Commission concludes that the PIRs should be repealed.

Immediate abolition of the PIRs could have significant adjustment costs for book producers, which suggests that there should be an adjustment period for the industry. The Commission is proposing that repeal take effect three years after announcement of the policy change.

## **Revising subsidy arrangements**

Some assistance is presently provided to local authorship and publishing through financial support arrangements such as the Australia Council grants. The grant funding is dispersed on the basis of a panel based selection process which among other things attempts to judge literary merit. The effectiveness of these schemes in generating cultural externalities is not clear.

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The Commission considers that the full range of current grants and financial assistance for the industry should be reviewed as soon as possible, with a view to better targeting cultural externalities, and any new arrangements put in place before the repeal of the PIRs takes effect.

### **Adjustment within the publishing sector**

While the Commission judges that the reforms would generate net benefits for Australia as a whole, abolition of the PIRs would — of themselves — cause some contraction or slowing in the growth in the book production industries. Similar effects have occurred in several other industries where the government has removed import protections or restrictions on competition, although the extent of the pending contraction has often been overstated by those in sectors facing reform.

Many publishers and authors have claimed that removal of PIRs would lead to very significant damage to their local industry, although a number of major publishers indicated that the impact would be more limited. Responses to a survey of 50 publishers indicated that, in the short-term (within 3 years), their Australian sales would contract on average by about 10 per cent. This follows several years of strong growth in the sector.

In the Commission's view, while removal of the PIRs should see an increase in imported books where these represent better value, it is probable that most Australian publishers, including the major publishing houses, would generally adapt to the new regime, that Australian stories and content will continue to be demanded and that talented and marketable Australian authors would continue to be widely published. Any pressure for contraction would also be ameliorated to the extent that subsidy arrangements were made more effective.

### **Monitoring the changes**

There nevertheless is inevitably some uncertainty about how the structure of the industry would change following the abolition of PIRs and any modification to the current subsidy arrangements, and how this would affect the cultural externalities the industry generates.

The Commission therefore proposes that the outcome from the repeal of the PIRs, together with the operation of any revised subsidy arrangements, should be monitored and assessed five years after their implementation. To assist that process, the Australian Bureau of Statistics should revise and update its 2003-04 surveys on the books industry and market prior to the repeal of the PIR provisions, to establish a

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base-line of the sector as it now is, and update them again prior to the commencement of the five year assessment.