
C Reform case studies

The Parallel Import Restrictions (PIRs) on CDs in Australia and books in New Zealand were lifted in 1998. The Commission has explored these reform episodes to see what lessons they may provide for the assessment of the merits of the PIRs on books in Australia, and of options for their reform.

While there are obvious parallels between CDs and books as consumer items, and between Australia and New Zealand as markets, a number of considerations limit the scope and strength of the lessons that can be drawn. These considerations are discussed in the following sections.

C.1 CDs in Australia

Background

There have traditionally been similarities between the books and sound recording industries. Sound recordings in a physical form, like books, are generally mass produced consumer goods, with their production characterised by high fixed costs (the cost of developing the original work) and low variable costs (the costs of producing an extra copy of the CD or book). The music industry's marketing chain is also broadly similar to that of the book industry. In general, physical music products are:

- created by many artists in a wide range of genres and styles
- refined, produced and marketed by a few large record companies and many small ones, with a variety of ownership structures
- distributed through a variety of independent retailers, discount and department stores and chain record shops.

There are also some important differences. For example, more importance is placed in the music industry than the books industry on the live performance and broadcast of creative works, both as a means of promoting the creators and of earning revenue. Further, a high proportion of music sales today, particularly of individual tracks or 'singles', occur through digital channels. And compared to books, musical

recordings are potentially more amenable to piracy — whether through the duplication of CDs or through personal digital file sharing via the internet.

It should also be noted that, prior to 1998, the PIRs on CDs in Australia were more restrictive than for books. Sound recordings were not subject to the 30/90 day rules, as books have been since 1991.

The Australian Government abolished parallel importation restrictions on sound recordings in July 1998, in part because of research that suggested the then relatively high prices for recorded music in Australia reflected an ability of record companies to use their market power to exploit local demand conditions (PSA 1990). In particular, the Prices Surveillance Authority (PSA) found that Australian consumers were paying substantially higher prices for these goods than overseas consumers.

Impacts on prices

There is evidence that consumers benefitted from lower CD prices as a result of the lifting of PIRs on sound recordings. In monitoring the impact of the policy change, the Australian Competition and Consumer Commission (ACCC) observed:

... a gradual rise in competition from lower priced parallel imports. This appeared to result in lower prices of both imported and locally made compact discs. The ACCC also noted the entry of non-traditional suppliers of CDs supplying low-priced imports to Australian consumers. In its 2001 report the ACCC noted a downward trend since August 1998 in the average prices of CDs available at specialist music stores. (ACCC, sub. 260, p. 18)

More specifically, the ACCC found that the average (tax-adjusted) price of top 40 CDs at specialist music stores immediately fell by around eight per cent (Fels 2002).

Gauging the ongoing price effects from the removal of the PIRs is complicated by a number of factors. Among other things, the growth in digital music distribution over the last decade is likely to have contributed to some of the observed low pricing during this period — accordingly, some price reductions for CDs might have occurred regardless of the earlier changes to the PIRs. Also, some participants told a 2001 Senate Committee *Inquiry into the Provisions of the Copyright Amendment (Parallel Importation) Bill* (SLCLC 2001) that the extent and breadth of the price reduction appeared somewhat limited. Indeed, the Full Federal Court¹ later found that both Universal Music Australia and Warner Music Australia had engaged in exclusive dealing in order to reduce competition (thus dampening the price benefits expected to flow from the removal of the restrictions), in breach of section 47 of the

¹ *Universal Music & Ors v Australian Competition and Consumer Commission* [2003] FCAFC 193.

Trade Practices Act 1974. As a result, it is possible that the potential price benefits to consumers of removing the PIRs were not fully realised, at least for a period following the removal of the restrictions.

Nevertheless, as the Australian Publishers Association acknowledged in its submission, ‘since the deregulation of territorial copyright for sound, there has certainly been some reduction in price’ (sub. 244, p. 56). The Association also noted that, in some cases, the downward price pressure following the removal of the PIRs is not dependent on parallel importation actually occurring:

It is the experience of the Australian music industry that there is limited genuine importation of CDs except by the rights holder, particularly in the case of non-top-20 discs. Instead, the changes to the law are used by large-volume retailers as a threat to music publishers, along the lines of: ‘drop the price or we’ll buy offshore’. (sub. 244, p. 58).

Quantitative analysis drawing on data for a range of countries (Chen and Png 2004), also cited by the Association, indicates that the scope to parallel import CDs is typically associated with a reduction of between 7 and 8 per cent in the retail price of music CDs.

Impacts on new Australian music

At the time of the debate on removing PIRs from sound recordings, music publishers argued that the restrictions were necessary to enable investment in local musical talent.

However, as the Network Economics Consulting Group (NECG) subsequently argued, sound recordings may have been potentially less sensitive to parallel importation than books because:

- it is more difficult to parallel import works of local acts which are not widely distributed in countries from which parallel imports of CDs are likely to be sourced (for example, South East Asia)
- the subsequent growth of non-traditional channels for distributing music recordings (following the lifting of PIRs), such as supermarkets and discount stores, may have contributed to the growth of investment in local acts (NECG 2004, p. 27).

Drawing on ‘observations from within the music industry’, the Australian Publishers Association (sub. 244, p. 59) argued that there has been a decline in the Australian music industry as a result of the removal of the PIRs in 1998, with a reduction in employment across the industry of 30–40 per cent in the past decade, fewer bands getting recording deals, and a ‘radical’ reduction in investment in

individual albums. The Association argued that the absence of PIR protection discouraged investment by the local music industry in part due to the risks of free riding by foreign competitors.

As with the reduction in CD prices, other changes affecting the industry in the past decade would make it difficult to isolate the specific impacts of the removal of PIRs in these respects. For example, on the one hand, the growth of digital downloading and file sharing is likely to have had a dampening effect on investment in parts of the music industry. On the other hand, adjustment pressures in the music industry are likely to have been cushioned by the strengthening, in 2000, of the Australian Music Code of Practice (under the *Broadcasting Service Act 1992*). This code aims to increase local Australian music content on commercial radio, in essence providing a certain guaranteed demand (and royalty stream) for newly released Australia music.

Whatever the specific impact of these various factors, evidence suggests that local Australian music continues to enjoy a significant share of the local market, without PIR protection. Six years after the ban was lifted, record numbers of local acts occupied the number one position in the Australia Recording Industry Association charts (NECG 2004). And in the year 2006-07, approximately 17 per cent of all commercially released all tracks were recorded by Australian artists (AMPCOM 2007).²

C.2 Books in New Zealand

Background

For many years, New Zealand, like Australia, imposed a blanket ban on the parallel importation of ‘creative-industries’ goods (such as books, films, music, and more recently DVDs and software) under the *Copyright Act (New Zealand) 1913*. The ban was removed in May 1998. Apart from the reintroduction of a partial ban on the parallel importation of some films, New Zealand’s creative industries continue to operate under an open market regime.

² In a submission following the discussion draft, the Institute of Public Affairs (sub. DR555, p. 11) noted that while CD prices had fallen since the removal of PIR protection, the number of music industry royalty recipients, and the amount they received, had increased every year since 2002. However, royalties collected by APRA and the Australasian Mechanical Copyright Owners Society are for the public performance and mechanical use of musical works, respectively. While the growth in these royalty payments may represent a recent strength in the Australian music industry, no real corollary for this revenue stream exists in the books industry.

The rationale for lifting the ban on the parallel importation of books was to realise welfare gains for the New Zealand economy by promoting a more open and competitive environment (MED 2007). This decision was underpinned, in part, by a New Zealand Institute of Economic Research (NZIER 1998) analysis. At that time (and, indeed, during this study), book producers raised concerns about the lifting of the ban on parallel imports on New Zealand's book industry (box C.1). However, the NZIER concluded that, although lifting the ban would most likely distribute gains and losses unevenly among stakeholders, the benefits to final consumers, as well as producers using copyright materials as intermediate inputs, would, on balance, outweigh other considerations.

Box C.1 Book producers' concerns regarding the impact of lifting PIRs on New Zealand's book industry

New Zealand's book industry raised concerns, both before and after the PIRs applying in that market were lifted, that are similar to those that have been raised in this study. For example, New Zealand publishers around the time the ban was lifted claimed that:

... the investment in publishing local works by the agents of the international publishers would fall dramatically if the parallel importing restrictions were lifted. (NZIER 1998, p. 42)

Some participants in this study have likewise argued the New Zealand book industry has been damaged by moving to an open market:

It is clear that lifting of the ban on parallel importing in New Zealand has had a detrimental effect on publishers and authors. Certain categories, particularly children's and tertiary education have been particularly impacted. (Book Publishers Association of New Zealand, sub. 166, p. 3)

The New Zealand industry today is characterised by little market growth and reduced investment in publishing infrastructure and local authors, particularly unknown and lesser known authors. (Allen & Unwin, sub. 214, p. 7)

Notwithstanding the similarities between the two markets, New Zealand's size and proximity to Australia are likely to confound the extent to which parallels can be drawn between the effects of reforms to its PIRs and what might happen were Australia's PIRs to be reformed. Walker Books Australia (sub. 256) noted that, with a population of under four million, New Zealand is a much smaller market and is more expensive to support. Further, territorial 'rights' to New Zealand sometimes continue to be bought and sold as part of 'ANZ rights', and in many (though not all) respects the market continues to operate as it did prior to the lifting of the PIRs. Peter Donoghue (sub. 8, p. 5) argued that New Zealand can be 'profoundly misleading' as an example of how other 'open markets' might operate. The Australian Publishers Association (sub. 244, p. 52) also commented on some of the difficulties of transferring the New Zealand book industry reform experience across the Tasman.

With these caveats in mind, the following sections explore the effects of the 1998 reforms in New Zealand.

Impacts

Over the past decade, the New Zealand Government has commissioned a number of reviews aimed at monitoring the impacts on the books industry resulting from lifting the ban on parallel importation (NZIER 2000; NECG 2004; LECG 2007). In each instance, the reviewing agency consulted extensively with key stakeholder groups within the New Zealand books industry. The outcomes of these reviews have revealed few deleterious effects on the local books industry (box C.2).

Box C.2 Findings from reviews of the New Zealand book reforms

‘Opponents to the law change predicted a flood of cheap imports, and warned of trade sanctions. Neither has materialised, and the effect of introducing parallel importing, to date, appears muted. However, although tangible impacts on volumes and prices have been small, the possibility of parallel importing has exerted pressure on the market place ... Delivery speed has improved, with customer orders able to be filled in a matter of days instead of weeks or months. Access to a full range of titles is possible, with availability enhanced by electronic links with suppliers around the world.’ (NZIER 2000, p. 269)

‘... there was no evidence of any substantial detriment to the financial performance or investment activity ... income earned by publishers has risen substantially from 1998 to the present while export growth in this sector since liberalisation has exceeded overall export growth.’ (NECG 2004, p. 6)

‘NECG’s assessments of various indicators suggest that there are no adverse impacts on investment in this industry from the liberalisation of parallel importing. Many publishers that were interviewed noted that insofar as there were any major impacts from parallel importing, they arose from the greater availability of remainders.’ (NECG 2004, p. 37)

‘There is agreement among industry that book sellers will generally stock books from New Zealand publishers if they have the titles in stock. Commercial parallel importation is predominantly of niche titles and the bulk purchase of discounted backlist titles (especially bestsellers from the United States).’ (LECG 2007, p. 17)

‘... the bulk purchase via parallel importation of backorder titles (and end of line remaindered books) has allowed book sellers to provide books to consumers at prices that they would not otherwise have been able to. Book sellers do not see this discount selling affecting their sales of new release titles and full price books, and believe that parallel importing has allowed them to service a new market for books (at lower price points).’ (LECG 2007, p. 19)

‘The book industry in New Zealand appears to be growing with no major detrimental impacts as a result of parallel importing ... in the last ten years the number of children’s titles published has trebled with significant export growth in these products.’ (MED 2008)

Impacts on consumers

After a year and a half of the open market regime, the NZIER (2000) concluded that the tangible impacts on prices had been small. It cited a number of reasons for this including that a low New Zealand dollar had effectively reduced any incentive to parallel import.

However, the NZIER (2000) observed that the lifting of the ban had made the book market more contestable because, although retailers preferred to source through their local wholesalers, they would, in some cases, explore other channels to improve timeliness of supply. It went on to conclude that, as a result, the quality of retail services available to New Zealand consumers had been enhanced, including:

- improved speed in filling customer orders
- improved availability and access
- earlier release of new titles. (NZIER 2000, p. 282)

It should be noted, however, that significant benefits of this nature have already been realised in Australia through the 1991 reforms.

In 2007, the LECG found that greater parallel importing was occurring, predominantly in relation to niche titles and the bulk purchase of discounted backlist titles (especially bestsellers from the United States). It found that while the prices of new release titles had increased over the preceding years, due to higher fuel and transportation costs, parallel importing had ‘allowed book sellers to provide books to consumers at prices that they would not otherwise have been able to’ (LECG 2007, p. 19).

Following the release of the Commission’s discussion draft, the Australian Publisher’s Association submitted a study on the impact that abolition of PIRs had on the New Zealand book industry (sub. DR513, att. 1). In that study, Castalia Strategic Advisors found that the measured price margin between NZ and US titles was narrower in 2009 than in NZIER’s previous study. Castalia noted that the results it found were ‘highly dependent’ on the prevailing exchange rate at the time of the comparisons, and argued that the measured differences were ‘within the margin of error’ (sub. DR513, att. 1, p. i).

Impacts on industry

The impact on local publishing appears to have been much less than many predicted at the time of the reforms. As HarperCollins noted during the course of the 2004 NECG study:

The only real impact has been on the availability of overseas remainders and whilst these can be a distraction there is no evidence in my view that they have an overall positive or negative effect on the market, with the exception of children's books. Regular monitoring of the New Zealand bestseller lists will confirm that almost without exception the titles which appear on such lists are being supplied through traditional rights channels. (HarperCollins, as quoted in NECG 2004, p. 37)

A weak New Zealand exchange rate, in the years following liberalisation, no doubt played a role in this, by making parallel imports less price competitive. Another factor is the range of services provided by local publishers. For example, REDgroup Retail noted that many bookstores ordered from local rather than international publishers because:

Local suppliers offer a range of useful benefits and services for booksellers, including sale or return terms of trade, rebates, free into store delivery, author tours and marketing support ... (sub. 175, p. 4)

In recent years, the revenue share of imported titles (as distinct from New Zealand published titles) has generally increased across the publishing sector. A survey of 34 publishers in 2008 indicated that their revenue share from imported titles had increased from 39 per cent to 62 per cent between 2005 and 2008 (Colmar Brunton 2008). The strengthening New Zealand dollar over this period is likely to have been a significant factor in this shift, although abolition of the PIRs is also likely to have had some effect.

Nevertheless, the 2009 Castalia paper found that the number of titles published in New Zealand, rather than declining following the abolition of the PIRs, actually grew between 1998 and 2008, albeit on one measure³ by less than 1 per cent annually (Australian Publisher's Association, sub. DR513, att. 1, p. 9).

Although there have been some significant changes in the nature of the New Zealand book industry (such as a shift from New Zealand to Australia of investment

³ Castalia interviewed senior managers of the five largest publishers in New Zealand, which represent 90 per cent of New Zealand's domestic publications. Castalia argued that the data obtained is therefore representative for the whole industry. However, the growth figure excludes changes in 'subsidised' and 'export-oriented educational titles'. In relation to the latter, Castalia noted that a number of New Zealand companies have been successful in providing English language and literacy services internationally, and the publishing industry 'has supported that growth with appropriate titles'. Castalia justified the exclusion of these titles on the basis they are not sold in New Zealand and enjoy PIR protection in other markets.

in warehousing and distribution), publishers and booksellers acknowledged that these may have arisen in any case:

... the Book Publishers Association does not attribute this rationalisation solely to the effects of parallel importation, although they feel the uncertainty introduced by the potential threat of parallel importing is likely to have been an influence on decisions.

[Booksellers] also see the move to Australia as part of a global trend of distribution chain rationalisation (to reduce costs), rather than being directly related to the effects of parallel importing. (LECG 2007, pp. 17, 19)

Booksellers in New Zealand also believe that lifting the ban on parallel imports has improved service, title range and availability (LECG 2007; MED 2008). In their opinion, the opportunity to parallel import has allowed them to target a new consumer market that would have otherwise turned to online purchasing channels. (Indeed, according to LECG (2007, p. 18), the main issue currently facing New Zealand booksellers is competition from online buying direct from foreign publishers.)

Impacts on New Zealand authorship

There is a range of views regarding the nature and extent of the impacts on New Zealand authorship and culture arising from the abolition of PIRs.

Submissions from some booksellers indicated that demand for locally authored books had not been affected by the reforms:

Bookstore customers do seek books, fiction and non-fiction, which relate to the country they live in. Our experience in New Zealand pre and post the introduction of an 'open market' for parallel imports is that this local reader demand for New Zealand books has not altered in any significant way. (REDgroup Retail, sub. 175, p. 2)

However, the Managing Director of Hachette New Zealand, Kevin Chapman, recently described New Zealand's adoption of an open market as being "like a cancer, an insidious thing" that had worked against protection of the country's culture' (BPANZ 2008). One concern expressed by New Zealand publishers in this respect is that parallel imports may have constrained growth in the promotion of local titles. Hence, while noting that the actual level of publishing and promotion of New Zealand titles seemed not to have been affected by the advent of parallel importation, LECG reported that:

... book publishers believe that the level of promotion may have been greater if they were able to increase their margins (without the threat of parallel importing). (2007, p. 19)

Further, a participant in the current study contended that:

... since parallel importation has been approved, many publishers have ceased to exist and few people would be able to list more than 5 New Zealand children's book authors

simply because there are now so few opportunities for publication in their country. (Peter Taylor, sub. 247, p. 1)

And according to the Castalia paper, in contrast to the overall growth in domestic titles published in the ten years to 2008, the number of New Zealand children's titles published decreased 'very significantly'. (Australian Publisher's Association, sub. DR513, att. 1, p. 9).

On the other hand, New Zealand Trade and Enterprise, the New Zealand Government's economic development agency, recently noted the nation's continued strengths in producing locally authored works, including some with significant cultural content:

Publishing is a significant creative industry in New Zealand, with strengths in fiction, poetry, art, New Zealand history and biography, and a growing range of titles by and about Maori.

New Zealand authors have garnered international recognition, including fiction writers Lloyd Jones (Booker-shortlisted *Mr Pip*), Witi Ihimaera (*The Whale Rider*) and Keri Hulme (Booker prizewinner *The Bone People*). The domestic and international success of Ian Brodie's non-fiction *Lord of the Rings Location Guide* is a good example of the publishing and tourism industries leveraging off each other.

Children's writing is another major strength, with Margaret Mahy, Lynley Dodd (creator of the ever-popular *Hairy Maclary* series), Joy Cowley, VM Jones and Sherryl Jordan all successful internationally. (New Zealand Trade and Enterprise 2008)

The MED (2008) paper indicated that the number of children's titles published over the previous decade had trebled with a significant growth in exports. And census data indicates a large increase in the number of people whose main job is that of an author or critic over the past three New Zealand censuses, from 1170 in 1996 to 1689 in 2006 (MCH 2009, p. 8).