

PARTS INDICATED IN SQUARE BRACKETS HAVE BEEN OMITTED AND WOULD BE WITHHELD UNDER THE OFFICIAL INFORMATION ACT 1982.

## **Copyright (Infringing File Sharing) Amendment Bill**

### **Regulatory Impact Statement**

#### **EXECUTIVE SUMMARY**

The objective of section 92A is to put in place a regime that effectively deters people illegally engaging in peer-to-peer (P2P) file sharing. A process to deter illegal P2P file sharing needs to be efficient to reflect the relatively low value of most music, movie and software files which are shared illegally. It is often uneconomic for a right holder to take legal action against individuals because of the cost of court action. However, the extent of downloading and uploading by individuals is so prolific that right holders claim that it is having a substantial economic effect on their businesses.

Estimating the sales displacement effect however, is not straightforward. Technology is changing quickly and consumers are reacting to those changes in ways that the creative industry are struggling to understand and cope with. We have some relevant information on sales displacement, based on overseas data, but this should be treated as indicative only.

The best way to reduce illegal P2P file sharing is to amend the Copyright Act 1994 to create a low cost, centrally administered enforcement regime. The proposed amendments will provide for a notice regime warning account holders about the copyright infringement, allowing the Copyright Tribunal to award a penalty after three or more P2P copyright infringements and extend the civil remedies of the court so that an Internet account can be suspended for up to six months.

#### **ADEQUACY STATEMENT**

The RIA and RIS for this proposal was prepared and assessed under the RIA requirements that applied prior to 2 November 2009. In forming its view, the Regulatory Impact Analysis Team (RIAT) acknowledges that MED is working within constraints, in particular prior policy decisions.

The RIAT considers that the analysis shows there is a case for intervention, but that, due to the uncertainty about the scale of harm done by illegal peer-to-peer file sharing, the impact analysis does not point to a preferred option.

The RIS is adequate with respect to the problem definition and consultation.

#### **STATUS QUO AND PROBLEM**

##### **Background**

The UK has just released its impact assessment on P2P file sharing under its Digital Economy Bill. The Assessment notes that an important feature of creative industries like the music, software and film industries is that they are characterised by strong IP rights. Strong IP rights create an incentive to invest in the development of new and more innovative products since it permits individuals to capture the gains from the new products it creates.

However with illegal file-sharing the incentive to invest in new and mainstream artists is undermined because industry cannot capture all the gains generated from its investment. This is because the public good<sup>1</sup> nature of file-sharing and the spillover effects<sup>2</sup> which exist creates a free-riding problem whereby users may enjoy the benefits of file-sharing without paying the product's price<sup>3</sup>. The disincentive to invest in artists as of result of free-riding is a particular problem in the music, film and videogames industries because they are characterised by large investment costs and a relatively high risk of failure.

Other potential costs can also have serious impacts on individuals and businesses. Illegal file sharing sites increase a user's exposure to viruses, loss of business intellectual capital, and identity theft. The technical nature of file sharing technology allows access both ways. In other words, while it opens another server to download material, in return, it allows access to a downloader's computer.

Content companies spend vast amounts of money investing in the success of a product (e.g. film, song or videogame). These costs are typically in production, marketing and promotion of creating and selling content to the consumer (advance payment to artists, advertising costs, retail store positioning fees, press and public relations to the artist, television appearances and travel, publicity and internet marketing). The industry is characterised by large fixed costs and low variable costs. The increasing trend for creative content to be traded digitally may have seen a change in the investment cost structure. Overall, some costs have remained high like marketing costs but distribution and production costs have decreased with an overall effect of increasing variable costs relative to fixed costs which may give small, relatively less known artists more room for manoeuvre.

Record companies, for example, take on considerable risk as not all the artists which they invest money in actually succeed. Typically less than 15% of all sound recordings released will break even and fewer return profits. However when a recording makes it big, the financial returns can be very large and this then goes to finance the next round of investment. The small success rate is due to the nature of mass-media market in which exposure to the public is scarce and firms maximise audience by selecting a relatively small number of potential one-size fits-all super star artists.

The industry has largely blamed file-sharing for declining sales. However, most commentators agree that the decline in sales, particularly in the music industry, cannot be wholly attributed to illegal file-sharing, citing a host of other factors, including general macroeconomic conditions (e.g. consumer confidence, economic growth) and the substitution of traditional forms of entertainment for new activities such as video gaming, internet browsing, social networking and a growing trend for artists to release content for free. In return industry has argued that the fall in sales is so significant that it cannot be explained by these factors alone.

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<sup>1</sup> Public goods are those goods which are non-rival and non-excludable in consumption. Non-rival in consumption means that one person's consumption of a good or service does not reduce the amount which can be consumed by another person, and non-excludable means that it is not possible to prevent another person from consuming it.

<sup>2</sup> Spillover effects arise when one person's actions have an impact on a third party.

<sup>3</sup> A similar case arises with Research and Development (R&D) whereby a company cannot capture all the benefits of its R&D activity because it cannot fully retain the knowledge that it creates. Knowledge spills over to other companies through various mechanisms, including personnel changing jobs or copying.

The digital provision of content has a number of advantages for consumers compared to more traditional ways of consuming content. Namely, it allows consumers to sample the product before buying it; to discuss the quality of the product online (e.g. social networking); it has lower transaction costs (e.g. lower costs for searching, can purchase it from home realising time savings); and in the case of music, enables unbundling (i.e. purchasing a song rather than the whole album).

It has been argued that some resistance by the content industry to offer content digitally may have exacerbated the problem of consumers turning to illegal downloading. Nearly 70% of illegal music downloaders in the UK agree that a basic reason for their unlawful behaviour is that legal downloading sources don't have the same range of content as illegal sources. The lack of supply of digital content may have led some consumers to use illegal sources of digital consumption. In fact, only in recent years the industry has started to embrace the digital provision of their products as an opportunity rather than a threat.

### **The New Zealand Situation**

Internationally, illegal copyright infringement through P2P file sharing has been increasing, with New Zealand subject to the same trend. The main impacts are felt in the music, film and videogames sectors. As with other countries, however, New Zealand evidence has been difficult to gather.

The music recording industry in New Zealand is represented by the Recording Industry Association of New Zealand (RIANZ)<sup>4</sup>. RIANZ fosters the growth of the industry and provides avenues for artists so that music can be produced, promoted and distributed to the New Zealand public. **[Omitted**

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Screen production mainly consists of feature films and television series. Following on from box office successes such as The Lord of the Rings trilogy and King Kong, New Zealand continues to host many other international feature film, television, and television commercial productions from around the world.

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<sup>4</sup> RIANZ claims to represent approximately 95% of total recording audio market in New Zealand.

Screen production is a growth industry in New Zealand and a significant contributor to the economy. For the 2008 financial year, the screen industry recorded total gross revenue of NZ \$2,743 million. Television broadcasting (including distribution) had the highest gross revenue contributing \$NZ 1,155 million. The screen production sector, comprising screen production companies and contractors had revenue of \$1,266 million. Of the screen production subsectors, feature films was the biggest revenue earner, accounting for half (\$NZ637 million) of all screen production sector revenue.

Software and gaming technology is also affected by illegal P2P file sharing. Sidhe Limited is the largest game production studio in New Zealand, and has produced more than 20 high profile titles.

We are unable to accurately estimate the costs to the industry from illegal P2P file-sharing since attempts to scale the problem have been fragmented or based on limited data sets. It is also complicated by the changing business environment. The industry is in the midst of a technological revolution with an explosion of channels, formats, and business models. As revenues drain away from the industry, businesses are struggling to adapt. Consumers have also reacted to these changes in ways that the industry has not anticipated, increasing uncertainty in the industry.

Despite the lack of quality data, there is information that suggests a substantial problem. For example, the information presented above in the graph on music industry sales shows a dramatic decline in sales which can not be fully explained by the content being accessed in other (fee paying) formats or by consumers switching to other products.

RIANZ also commissioned a study earlier in 2009 to identify infringements by New Zealand users, using only a very limited list of copyright sound recordings. Over a period of 14 days, an average of almost 5,000 potentially infringing users was identified per day. The users are “potentially” infringing because although they were illegal downloads (through Limewire), RIANZ did not substantiate copyright ownership by going back to every copyright owner on the individual downloads. Wholesale trade statistics collected by the RIANZ<sup>5</sup> show a similar trend with digital sales only making up 9% of wholesale sales. This only partially offsets the huge drop in sales since 2001.

For screen (movie and television) in New Zealand, NZFACT<sup>6</sup> estimate that there are on average 200,000 file shares per month. LEK Consulting (2005) infer that the piracy costs could be as high as 25% of potential sales (\$70 million) based on overseas trends. Internet piracy via P2P file-sharing networks is a significant concern and accounts for the majority of New Zealand movie industry losses – an estimated \$33 million in lost consumer spending in 2005.<sup>7</sup>

### **Overseas Evidence**

Evidence from overseas markets has been as difficult to gather as it has for New Zealand. However, those who respond to surveys saying they have illegally download content also point to a widespread problem. The Digital Entertainment Survey (2008) estimates 6.5 million UK users have at some stage illegally

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<sup>5</sup> See RIANZ website [www.rianz.org.nz](http://www.rianz.org.nz)

<sup>6</sup> NZFACT was established by the Motion Picture Association (MPA) to protect the film industry in New Zealand from the adverse impact of copyright theft.

<sup>7</sup> NZFACT media statement entitled “NZFACT Coordinates Launch of Te Re Maori Booklet Warning of P2P Filsharing Dangers” 9<sup>th</sup> February 2009.

downloaded content. Most illegal downloads are for music (29% of users), followed by movies and TV (21%) and games/software (15%).<sup>8</sup> (It should be noted that these are the only statistic presented in the UK Impact Assessment for the Digital Economy Bill.)

In the USA, researchers<sup>9</sup> attempted to profile those looking for files that could be illegally downloaded. They found that 15% of those trolling the internet were from government or the recording industry attempting to catch those involved in illegal downloading. This suggests that the industry is hurting enough (or believe it is) to put substantial funds into catching those participating in illegal downloading activity.

Furthermore, the BBC<sup>10</sup> reported that within 10 days of the game Spore being released, more than half a million people had downloaded a pirate version of the game using P2P technology. In comparison, legitimate sales of Spore have passed the 2 million units mark (the game retails for roughly NZ \$75).

Use of P2P file sharing technology is also likely to pose a security threat to corporates and individuals. According to Symantec in the first half of 2007, 15% of all potential infections were propagated by the file sharing software eDonkey in the UK.<sup>11</sup> File sharing has been linked to identify theft, theft of company data, and release of personal information.

According to Ipsos-MORI, in 2007, one in ten office employees are using the workplace to download music, two thirds of them illegally.<sup>12</sup>

With these pieces of information, we do have some indications of the seriousness and spread of illegal file sharing activity. However, there is still heated controversy over the scale of the sales displacement effect of illegal downloads. Any discussion of the subject on the internet produces pointed exchanges from often well informed participants. See for example the blog postings associated with a study by Andersen and Frenz (2007).<sup>13</sup>

Those who claim that the industry are over playing the issue of illegal downloading point to a number of factors which have contributed to the decline in physical sales. Consumers have better things to spend their money on and this has been helped, some claim, by uninspiring CD/DVD releases over the last few years. Also, bands have changed their marketing approach. Instead of going on tour to promote CDs, now bands release free downloads of their music to promote their tours and the merchandising that goes with it. The rise of the internet sellers has also played a part in the demise of high profile CD retailers over the past few years. In particular, Amazon.com has changed the buying behaviour of many consumers.

The costs of illegal downloading include losses to the industry of sales foregone, possible reduction in product offerings as revenues reduce which leads to the reduction of choice for consumers, wider transmission of viruses, security breaches, and possible trade impacts. The benefits are that consumers receive free goods and services.

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[http://www.entertainmentmediaresearch.com/reports/DigitalEntertainmentSurvey2008\\_FullReport.pdf](http://www.entertainmentmediaresearch.com/reports/DigitalEntertainmentSurvey2008_FullReport.pdf)

<sup>9</sup> [http://newsroom.ucr.edu/news\\_item.html?action=page&id=1673](http://newsroom.ucr.edu/news_item.html?action=page&id=1673)

<sup>10</sup> <http://www.news.bbc.co.uk/2/hi/technology/7772962.stm>

<sup>11</sup> Accessed from: [http://www.ifpi.org/content/section\\_news/20080307.html](http://www.ifpi.org/content/section_news/20080307.html)

<sup>12</sup> *ibid*

<sup>13</sup> <http://www.dime-eu.org/node/477>

With no obvious practical or theoretical guidance on the magnitude of the damage, the impact on sales of illegal file-sharing is an empirical question. Below we have set out a selection of studies that have attempted to objectively assess the sales displacement effect.

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***Selection of studies estimating the sales displacement effect***

Studies	Sales displacement (% of tot revenue)	Industry	Country	Method
Oberholzer-Gee & Strumpf (2007) Journal of Political Economy	0%	Music	US	Actual downloads data
Blackburn (2004), mimeo	0%	Music	US	Actual downloads data
IPSOS (2007)	2%	Film & TV	UK	Survey data
Zenter (2006) Journal of Law and Economics	8%	Music	7 European countries	Survey data
Rob & Waldfogel (2006) Journal of Law and Economics	9%	Music	US	Survey data
Hennig-Thurau, Henning & Henrik Sattler (2007), Journal of Marketing	9%	Film	Germany	Downloads proxies data
Jupiter Research (2007)	17%	Music	UK	Survey data
Peitz and Waelbroeck (2004), mimeo	20%	Music	16 countries	Downloads proxies data

Source: Department for Business Innovation & Skills. Consultation on Legislation to address illicit peer-to-peer (P2P) file-sharing, 16<sup>th</sup> June 2009, p47.

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Estimates range between 0% and 20% of total revenue for music and between 2% and 9% of total revenue for film and television. The figures from these overseas studies are very sensitive to the methodology used and the country and industry examined. It must be born in mind, therefore, that the scale of problem may be lower than some in the industry have claimed. In these circumstances it is important that any policy action taken to address the problem should not unnecessarily impinge on legitimate consumer access to material on the web and in particular, should not unnecessarily inhibit business innovation in the digital environment.

**New Zealand in an International Context**

The issue of illegal P2P file sharing is receiving increasing attention internationally and many governments in other jurisdictions are taking action to address it. The United Kingdom is consulting on a similar regime as proposed in this paper, with notices and remedies including suspension of an internet account. France has passed a law with notices and suspension as the remedy. The United States, Australia, Singapore, and the Republic of Korea have included a provision similar to section 92A in their legislation.

New Zealand will need to ensure its regulations are on a par with its trading partners so that it can access the latest technology and avoid potentially damaging trade disputes. New Zealand is currently involved in negotiations with a number of trade partners to develop a treaty known as the Anti-Counterfeiting Trade Agreement

(ACTA).<sup>14</sup> ACTA aims to establish an international framework for enforcing intellectual property rights to address more efficiently the problem of large scale trade in counterfeit goods and piracy, including copyright piracy on the internet. These negotiations are still in the early stages and it is not clear how the negotiations will proceed, and whether New Zealand will become a party to the agreement once negotiations conclude.

New Zealand is also negotiating a Free Trade Agreement with the Republic of Korea and hopes to shortly begin negotiations on an expanded Trans-Pacific Partnership Agreement (TPP) with a number of countries, including the United States. **[Omitted**

]. While the intellectual property provisions for these trade negotiations are still under negotiation, New Zealand will be required to ensure that its legislation is consistent with the provisions of these agreements, once negotiations have concluded.

However, it should be stressed that New Zealand supports the intent of these negotiations given that we have an interest in our creative industries being able to sell their works in offshore markets and not lose out to illegal peer-to-peer file sharing. In return, our trading partners legitimately expect to New Zealand to enforce its laws in the interests of their creative industries.

#### **Status Quo and Problem: Conclusion**

The proposed legislation will impact on individuals, creative industries, the New Zealand economy, and possibly trade agreements. Although there is an existing legal framework for dealing with copyright infringement under the Copyright Act 1994, for both civil<sup>15</sup> and criminal<sup>16</sup> offences, right holders complain that using the courts is time consuming and costly and it is not providing a sufficient deterrent. It is also not effective given the large number of illegal downloads and uploads taking place.

As shown in all other jurisdictions, it is simply impractical and uneconomic for right holders to take all breaches to court – the costs of court processes far outweigh the benefits of enforcement. For example, a single song purchased and downloaded legally from the iTunes website will cost between 95 cents and \$1.75, a CD between \$11.95 and \$29.95, movie rental 6 to 10 dollars and purchase of movies up to \$30.00. These prices are gross and don't reflect the net revenue flowing back to the creator of the work. However, New Zealand creative content distributors, producers

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<sup>14</sup> The other participants in the ACTA negotiations are Australia, Canada, the European Union, Korea, Japan, Mexico, Morocco, Singapore, Switzerland and the United States.

<sup>15</sup> Section 120 of the Act, which provides that copyright infringement, is actionable by the copyright owner and that "all such relief by way of damages, injunctions, accounts, or otherwise is available to the plaintiff as is available in respect of the infringement of any other property right".

<sup>16</sup> Section 131 provides for criminal liability in relation to copyright infringement. A person who commits an offence against section 131 is liable to a fine of up to \$150,000 or imprisonment of up to 5 years. Criminal offending under the Act applies generally only to commercial infringement. P2P file sharing generally occurs in the domestic setting for personal use. Section 131 would usually only apply where P2P file sharing was occurring for commercial gain.

and other license holders all receive a share of this revenue (including from content produced overseas but sold in New Zealand)<sup>17</sup>.

The current enforcement regime under the Copyright Act needs to be updated to address these problems. At the same time, the above analysis has demonstrated that while it is almost certain that problems exist, their size cannot be accurately measured at this time. This points to the need to adopt solutions to the problem that are low cost and flexible to administer, particularly as it is not at this time clear how many cases will be brought. It is also important that any system does not discourage either consumers from exercising their legitimate rights in the digital environment or businesses from innovating on the internet.

## **OBJECTIVES**

The objective is to significantly reduce illegal P2P file sharing of copyright protected works by ensuring that the Copyright Act provides:

- A more efficient and less costly civil enforcement regime for right holders against illegal P2P copyright infringement; and
- Civil enforcement measures, procedures and remedies that are effective, proportionate and dissuasive.

It should be noted that the options below have not been assessed in terms of their “distributional” impacts (e.g. between domestic and foreign businesses). Copyright law is intended to optimise the level of innovation and creativity that occurs in society. It seeks to provide appropriate levels of protection to all creative industries in all markets and the New Zealand economy benefits from the activities in New Zealand of foreign as well as domestic creative industries. At the same time, New Zealand industries benefit, sometimes significantly, from the presence of similar laws in other markets. It is important in this area that New Zealand recognises that it is part of a global IP protection system which benefits New Zealand creative industries that both seek to sell in the domestic market and to export. Taking a neutral approach in this respect also provides significant benefits to New Zealand consumers who can take advantage of the presence of both domestic and foreign copyright material.

## **ALTERNATIVE OPTIONS**

*Option 1- Deferring legislation until other similar countries have enacted their legislation*

This option would not require legislative change at this time.

This option has the benefit of ensuring that New Zealand is consistent with other countries or that New Zealand could learn from the experiences of other jurisdictions.

A further argument against deferring is that extensive consultation has taken place on the policy proposals contained in this paper and it is judged that while not all groups are completely happy, there is consensus that the proposals represent a reasonable compromise. If the legislation were to be deferred, this process would

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<sup>17</sup> For example, independent New Zealand music distributor Rythmethod has a large roster of both New Zealand Artists and artists from overseas, which they distribute to the New Zealand consumer.

almost certainly need to be repeated and there are no guarantees that the current level of consensus could be repeated in the future.

In the meantime, waiting also means that losses from illegal P2P file sharing are affecting New Zealand's creative industries which in turn has an effect on New Zealand's economy.

*Option 2 – Single Notice (Internet Service Providers would send out an education notice to account holders about illegal copyright infringement occurring over their internet account with no enforcement or enforcement delayed for 12-24 months)*

This option would require legislative change.

Part of the problem is that many small scale illegal file sharers are likely to be unaware that their actions breach copyright.

The majority of small scale infringers may stop infringing after receiving an education notice that informed them their actions were illegal. This may especially be the case in a family context where the infringer may not be actual the account holder. A Digital Britain survey shows that up to 70% of illegal file sharers would, at least initially, stop file sharing if they received an education notice.

However, it is likely that this rate of improvement could not be sustained if it were not backed up by the threat of some form of sanction should illegal file sharing not stop. Illegal file sharers would quickly understand that the only option open to copyright owners was to take them to court and that this would be unlikely in almost all cases of small-scale infringing.

At the same time, the Digital Britain survey and other anecdotal evidence from overseas jurisdictions suggest that 30% of illegal file sharers would not stop infringing if they received an education notice. Furthermore, larger scale infringers who are aware their actions are illegal are likely to infringe intentionally and on a commercial scale; and will affect New Zealand's creative industries the most. This option is therefore unlikely to be effective in reducing infringements from this group of file sharers, without some penalty as a result of ignoring notices. It is considered that a secondary remedy that provides a penalty such as those proposed in the Copyright Tribunal will give some enforceability to the notice system.

*Option 3 – Internet Service Providers would be required to suspend an Internet account for repeat infringement after the account holder is sent three infringement notices by the ISP, in appropriate circumstances*

This option would require legislative change.

Under this option ISPs, rather than the courts, would be required to make a determination on copyright infringement and it may be difficult for them to evaluate or adjudicate the legitimacy of an infringement claim by a right holder. Furthermore, it may not be the actual account holder who is the alleged infringer; it may have been another member of the same household, or in the case of a business, an employee.

This option is likely to provide a quick and easy remedy for rights holders who will be able to go straight to ISPs rather than seeking suspension in the courts. There would however be significant costs to ISPs of setting up systems and personnel to decide whether suspension is appropriate in each case.

This option also raises issues of proportionality because the remedy of suspension of an internet account may not be a proportionate response to the damage caused, and consumers would not be able to defend themselves. ISPs are not in a position to hear counter arguments of account holders which would be required by natural justice principles before limiting their right to access the internet. Such a decision is more appropriately put with an adjudicative body such as a court, not private parties.

Suspension is also inconsistent with statutory remedies for other online conduct, e.g., spam or pornography.

## **PREFERRED OPTION**

### **Description of the preferred option**

Under this option the Copyright Act would be amended to provide a new procedure for right holders to enforce their copyright against a person using an internet account for illegal P2P copyright infringement. This would be a notice regime, whereby notices are sent by ISPs to the internet account holders informing them of the use of their accounts for illegal P2P file sharing purposes based on claims of copyright infringements by right holders.

Right holders currently use software programmes to legally track P2P infringements. These programmes provide them with evidence of P2P infringements, identifying the Internet Protocol number the work was downloaded from, the type of work that has been downloaded and the date it occurred.

IP numbers identify the device that has downloaded the work, but cannot determine who the device belongs to. Only the ISP has the contact details of its customers and can correlate the IP number with the contact details of the account holder. The ISP will not be required to provide the contact details of the account holder to the right holder. This is the reason why the ISP must send the notices to the account holder so as to safeguard the identity of its customers. This preservation of identity continues throughout the process, unless the Tribunal makes an order against a person and then (as is current practice) provides those details as part of publishing its case on the website. Right holders will only obtain the details of the account holder if an account holder chooses to provide them directly, or the right holder obtains an order from the Court.

A first notice would be an educational notice; the second a cease and desist notice; and third an advisory notice, informing the account holder that there have been three or more infringements within the prescribed timeframes and the right holder may take a complaint to the Copyright Tribunal or the Court.

ISPs will act as a conduit and be required to:

- Identify the IP addresses and match it to the account holder;
- Retain data of subscriber internet use for a minimum period of 20 working days so that the ISP can identify the account holder from the information provided by the right holder;
- Retain data on infringements for a minimum period of 12 months so that the ISP will know when repeat infringement has occurred;
- Provide information to right holders about repeat infringement;

- Forward notices to account holders by post or electronically (the usual way ISP corresponds with its customer) within a reasonable timeframe; and
- Communicate with right holders where necessary.

Account holders who receive such notices will be permitted to respond to right holder allegations of infringement through a counter-notice either sent through their ISP or directly to the right holder.

Right holders will be required to pay a fee to the ISP towards the cost of issuing the notice.

The jurisdiction of the Copyright Tribunal would be extended to consider complaints made by right holders about alleged illegal P2P copyright infringement by the account holder, but only after the advisory notice had been sent by the ISP. The Copyright Tribunal would be provided with the power to award a penalty which will be prescribed by regulation. The Tribunal will have the power to obtain customer details from ISPs where necessary to identify the account holder. Any account holder who received a notice that a complaint has been lodged with the Tribunal would be able to defend the allegation of copyright infringement through a hearing. An appeal on a question of law (which is consistent with the current legislation) would be able to be taken to the High Court.

Right holders will be required to pay a filing fee per complaint to the Tribunal.

Regulation making powers will provide for notices, prescribe the evidence from right holders, notice and Tribunal fees and the level of the penalty.

The Copyright Act would also be amended to extend the remedies available to the courts to address repeated P2P copyright infringements to include suspension of an Internet account of up to six months, where appropriate.

Furthermore, the right holder would still be permitted to take an action in accordance with the current enforcement provisions available to the right holders under the Copyright Act to enforce their copyright in the court against an account holder who is alleged to have infringed copyright through the use of P2P file sharing technologies.

Officials consider that the proposed regime is proportionate to the damage infringement causes. Retaining the status quo and taking no action will have an effect on the creative industries due to the cumulative damage resulting from many single infringements, but large fines or internet suspension may be too harsh a penalty to the infringer if the damage from infringement is low. As described above, the proposed regime has several factors that work to ensure a penalty is proportionate, including:

- For an illegal downloader to get to the copyright tribunal, three infringements will need to occur within 9 months. This will increase the value of claims in the tribunal to a not insubstantial amount, and limit the chance for abuse of the process through vexatious claims for small amounts;
- The tribunal system will be quick and inexpensive for both right holder and infringer, in order to limit the danger that the costs of enforcement outweigh the relatively low damage caused by an infringement;

- As internet suspension is a limitation of consumers' rights, a right holder wishing to seek suspension as a remedy will have to go to the Courts, where the costs of enforcement dictate that claimants will only pursue enforcement if substantial damage has occurred.

### **Impacts of the preferred option**

In assessing the impacts of the preferred option, a key consideration is that the absolute harm caused by the problem represented by peer-to-peer file sharing cannot be measured at this stage. Given this situation, it is important that this option delivers an outcome that is "scalable" to the actual harm caused by the problem (ie the amount of activity undertaken by adjudication agencies can adjust in accordance with the number of cases taken). It is also important that consumers have opportunity for redress at each step of the process.

The preferred option should provide for these outcomes. The scale of adjudication activities will be determined by copyright owners and they will be required to meet particular standards of evidence at each stage of the process. For cases brought before the Copyright Tribunal, copyright owners will also need to pay a fee which should deter frivolous cases. For both the notification process and the Copyright Tribunal, consumers will have the ability to contest the allegations that have been made.

Ultimately, it is of vital importance that the size of any sanctions imposed is proportionate with the harm caused by the offending. Remedies will be proportionate to the extent of the infringement. In the notification process, users will not be penalised at all if they choose to stop infringing. The size of the fines that the Copyright Tribunal can impose are modest (ie a maximum of \$15,000) meaning that it will be less appropriate for the Copyright Tribunal to be the ultimate arbiter on cases of serious offending. For lower levels of harm, the options that are available to Copyright Tribunal have been kept quite limited. At the same time, this option leads to potentially serious cases being considered by the court. The court will be required to determine whether the remedy is appropriate in the circumstances of each individual case.

Fiscal implications of extending the jurisdiction of the Copyright Tribunal are estimated to be \$408,000 in 2010/11 and \$838,000 the following years (including out years) plus a one-off capital cost of \$201,000 in 2010/11. If approximately 1800 cases went to the tribunal. This is only an indicative cost because it is unknown how many cases would be brought before the Tribunal.

Although extending the jurisdiction of the Copyright Tribunal may impact on the Ministry of Justice's resources, it is important that such a scheme is implemented, to help reduce the overall amount of illegal P2P file sharing. The Copyright Tribunal will use a fast-track system to reduce costs. Hearings will only be held on the request of the parties. It is anticipated that once this system is implemented there will be a reduction and so the impact on the Copyright Tribunal will be substantially reduced over a period of time. A filing fee to use the Tribunal will also provide some cost recovery to the Crown, although the majority of the cost will be borne by the Crown.

This proposal will place compliance costs on ISP businesses. There are costs involved in developing ISPs customer management systems to implement the regime, plus the per-transaction costs of processing each notice **[Omitted**

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The ongoing yearly costs will be dependent on the number of notices received which is unknown at this time, but right holders will be required to pay a fee towards the administrative cost of issuing a notice to reduce the impact on ISP businesses.

A right holder would be able to enforce the debt through the Ministry of Justice Collections Unit. It is estimated that there may be between 1000 to 2400 cases taken to the Tribunal in the first year, with this reducing in subsequent years. Not all cases will result in an enforceable debt, and not all enforceable debts will need to be enforced. At this level, there would likely be some impact on the volume of civil enforcement proceedings. However, the Ministry of Justice Collections Unit has informed MED that these would appear to be manageable within the current case loads. Therefore no further funding is sought for civil enforcement proceedings as a result of this option.

It is recommended that the civil penalties of the court be extended to include suspension of an Internet service for six months. The Ministry of Justice Collections Unit have advised that it is not anticipated this will have an impact on the current court system.

One benefit of this option is that it will not impede the development of on-line markets in New Zealand and will allow New Zealand creators to distribute their works on the Internet. It will promote confidence in the use of online distribution channels as creators of copyright will have a low cost option available to deal with infringements.

At the same time, a major issue for some New Zealand creators previously was that the reliance on suspension by ISPs as a penalty would significantly impede access by consumers to their works as well as their ability to effectively distribute their works on the internet. These creators point out that the internet provides them with major new opportunities to develop and distribute their works in an innovative fashion. It is important therefore that any regulatory options do not cut across the ability of these creators to innovate and to exploit the advantages provided by the internet. They are not against regulation per se (indeed they support sensible regulation) but state that the regulation needs to be facilitative of the new environment. In this respect, they have a particular problem with option 3 which provides for ISPs suspending the accounts of repeat infringers. We believe that these views have significant merit.

This preferred option has the advantage that suspension will be used only in very limited circumstances, for cases of serious offending as determined by the court. As such, only a very small number of consumers would be impeded from accessing the Internet. Otherwise a range of measures would be used (ie notices and fines) that would allow almost all infringers to continue to use the internet unimpeded. (The option is in fact quite close to an option put forward by the Creative Freedom Foundation in the course of submissions to the Minister, although this body still opposes any sanctions based on suspension. The Creative Freedom Foundation represents New Zealand artists that are seeking to use the internet to distribute their works.)

The bringing into force of s92A is likely to increase the production of music, movies and games in New Zealand, as the producers of these works will have larger budgets to spread across the respective creative industries. Right holders also submit that there are increasingly less opportunities for new creators of content to be funded and introduced into the industry as a result of lower revenue. Right holders will therefore benefit as they will have more opportunities to create new works, and develop a larger base of creators.

It is also important that bringing s92A into force is likely to increase legal sales of music, movies and games in New Zealand. There is now some evidence that this is likely to occur. In Sweden for example, legal sales of music on the internet have increased since new anti-piracy legislation was introduced in April and the peer-to-peer file sharing website Pirate Bay was closed down. In the first 9 months of 2009, legal music sales increased by 18 percent with an 80 percent increase in digital sales and a 9 percent increase in physical sales (figures supplied by Billboard Magazine).

A follow on benefit is that the more the creative industries in New Zealand expand, the more opportunities for employment in the production, marketing and distribution of New Zealand works will arise. New Zealand creative industries are seen on a world stage as being at the forefront of innovation in the industry. Weta Digital in Wellington is an internationally renowned digital production company as a result of the *Lord of the Rings Trilogy*. By limiting the effects of illegal P2P file sharing on the creative industries' revenue, producers of creative works will have the budgets to be able to maintain their status as innovators, and in turn continue to bring the investment of large international customers into the New Zealand Market by offering technologically advanced production solutions.

The main benefit to New Zealand consumers is that more creative works will be available for purchase. This does not only apply to New Zealand works, as limiting the effects of illegal P2P sharing on distributors also allows them to bring more overseas works to the New Zealand market. Limiting the effects of illegal P2P sharing will also allow new creators to provide a wider variety and choice to the market for New Zealand produced music, films and games.

Implementation of section 92A may also increase the variety of ways consumers can access creative works in New Zealand. Limiting the effects of illegal P2P file sharing on the creative industries' revenue will give these industries the budgets to focus on new methods of access to works (for example paid Internet radio and web subscriptions to catalogues). These services are often slow to reach New Zealand consumers (for example the iTunes Store).

## **IMPLEMENTATION AND REVIEW**

It is proposed that there be an implementation period of three months after the Bill is enacted to enable ISPs to upgrade their systems, and the Ministry of Justice to prepare for the extension to the Copyright Tribunal. Regulations will also be required to provide for template notices, set out the evidence that right holders must provide ISPs and set the level of liquidated damages.

The effectiveness and efficiency of this legislation would be evaluated through any changes in the:

- Trends and volumes of notices sent by ISPs;
- Evidence provided by right holders;

- Number and type of cases taken to the Tribunal (fast-track vs. hearings) and
- Number of complaints received about the process.

## **CONSULTATION**

The proposal to create a notice process including right holders and Internet service providers and the Copyright Tribunal being the enforcement agency was consulted on in July 2009 by the MED. 113 submissions were received from right holders (Recording Industry Australia and New Zealand, New Zealand Film etc, MPA), the Telecommunications Carrier Forum (representing ISPs) and the public.

Stakeholders were broadly supportive of the proposal, although right holders preferred that ISPs were to terminate or suspend an Internet account after repeat infringement. ISPs and the public were generally not supportive of termination or suspension of Internet accounts at all.

In developing this proposal, the Ministry of Economic Development has consulted with the following government departments: The Ministry of Justice, The Ministry of Foreign Affairs and Trade, Privacy Commissioner and the Treasury. The Department of the Prime Minister and Cabinet has been informed.