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CONSULTATION ON LEGISLATION TO ADDRESS ILLICIT PEER-TO-PEER (P2P) FILE-SHARING

16TH JUNE 2009

CONSULTATION DOCUMENT ON LEGISLATION TO ADDRESS ILLICIT P2P FILE-SHARING

Explanation of the wider context for the consultation and what it seeks to achieve

This consultation sets out the Government's legislative approach for addressing the problem of illicit use of Peer-to-Peer (P2P) file-sharing technology to exchange unlawful copies of copyright material. This takes forward Recommendation 39 of the Gowers Review of Intellectual Property which addressed the issue of illicit use of P2P, the recent BIS consultation on possible regulatory options and Action 13 of the Digital Britain Interim Report.

The proposals will provide a legislative baseline aimed at changing the behaviour of the majority of file-sharers, provide a mechanism for identifying any further action to be taken against repeat infringers if appropriate, and facilitate rights holder efforts in taking legal action against the most frequent infringers. We hope these will assist industry in devising commercial agreements which both offer consumers the kind of content, when where and how they want it, at a price they are prepared to pay and include bi-lateral solutions which address unlawful file-sharing via a range of technical and other measures.

The implementation and effectiveness of the proposals in this paper would be facilitated by the establishment of some form of industry body representing both rights holders and intermediaries and others with a direct interest, which might correspond to the rights agency floated within the Interim Report. Such a body would be capable of agreeing the relevant codes of practice to support this legislative approach. It could also work on other important issues such as public education and awareness and developing new approaches as online piracy changes. It would seem clear that it is in industry's interests to ensure they are fully engaged in developing such material, and without such a body this legislative framework may only provide a partial solution to online piracy, and the problem as it appears today, rather than being capable of flexing to take into account future developments. However, the legislative arrangements are capable of operating without an industry self-regulatory body.

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Respond by: **15th September 2009**

Enquiries to: Michael Klym / Adrian Brazier
Communications & Content Industries
Department for Business, Innovation and Skills
UG28-30
1 Victoria Street
London SW1H 0ET

Tel: 020 7215 4165 / 1295 Fax: 020 7215 5442
Email: mike.klym@bis.gsi.gov.uk / adrian.brazier@bis.gsi.gov.uk

This consultation is relevant to: industry, in particular ISPs and copyright holders such as music, film, publishing, software, TV, sports and games sectors. Consumers and consumer organisations will also have a close interest.

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1. Executive Summary

Executive Summary

1.1 Unlawful P2P file sharing was identified in Andrew Gowers' Review of Intellectual Property as causing significant damage to the UK's creative industry. Gower's Recommendation 39 called upon Government to take action if no industry solution proved possible. This was accepted by Government and recognised in the Creative Economy Strategy Paper (February 2008). Despite industry efforts, culminating in the Memorandum of Understanding (MOU) signed in July 2008, no voluntary solution was identified, although the MOU process provided much valuable information and experience.

1.2 The Government consulted on possible regulatory solutions in parallel with the MOU process. The outcome of that consultation was announced as Action 13 in the interim Digital Britain Report (January 2009).

1.3 Action 13 sets out two obligations which will apply to ISPs. ISPs will be required to send notifications to subscribers who have been identified in relation to alleged infringements of copyright. The second obligation is for ISPs to maintain (anonymised) records of the number of times an individual subscriber has been so identified and to maintain lists of those most frequently identified. Both obligations would be underpinned by a code drawn up by industry and approved (or imposed in the absence of agreement) by Ofcom. Following further consideration we are now proposing a change to the way in which we construct these obligations. This document sets out an approach whereby a duty will be placed on Ofcom to take steps aimed at reducing online copyright infringement. Specifically they will be required to impose the two obligations on ISPs set out in the Digital Britain Interim Report. Ofcom will also have the power to impose by Statutory Instrument the additional obligations listed in the legislation if they think it necessary. In addition they will be required to put in place a code to support any obligations that are in place.

1.4 Some research and empirical evidence suggests that most people will stop file-sharing if they receive a notification (though other research is more provisional). In addition rights holders will be able to take targeted legal action against those most frequently identified, both as a deterrent and also because these individuals are the ones doing most harm. Rights holders will continue to need a court order to require ISPs to release the personal data of the most frequently identified infringers.

1.5 This consultation is on the approach Government intends to take in legislating to introduce these two obligations, and it based on Annex B of the "Copyright in a digital world – what role for a digital rights agency?" paper published in March this year. The underpinning code will set out the process and standards by which the obligations will be discharged. It must include measures for consumer protection. However there are a number of areas which the code might cover and this consultation seeks views on them. In particular:

- the balance between what the code must cover and areas where there is scope for discretion;
- how costs might be apportioned; and

How to respond

1.6 When responding please state whether you are responding as an individual or whether you are representing the views of an organisation. If responding on behalf of an organisation, please make it clear who the organisation represents and, where applicable, how the views of members were assembled.

1.7 **The closing date for all responses is 15th September 2009**

A response can be submitted by letter, fax or email to:

Michael Klym/Adrian Brazier
Communications & Content Industries
Department for Business, Innovation and Skills
UG28-30
1 Victoria Street
London SW1H 0ET
Tel: 0207 215 4165/1295
Fax: 0207 215 5442

Email: mike.klym@bis.gsi.gov.uk / adrian.brazier@bis.gsi.gov.uk

1.8 **A list of consultation questions can be found at Annex A**

A list of those organisations and individuals consulted is at **Annex B**. We would welcome suggestions of others who may wish to be involved in this consultation process.

1.9 **Help with queries**

Questions about the policy issues raised in the document can be addressed to:

Michael Klym/Adrian Brazier
Department for Business, Innovation and Skills

(Contact details as above)

1.10 **Additional copies**

You may make copies of this document without seeking permission. Further printed copies of the consultation document can be obtained from:

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1.11 **Confidentiality & Data Protection**

Information provided in response to this consultation, including personal information, may be subject to publication or release to other parties or to disclosure in accordance with the access

to information regimes (these are primarily the Freedom of Information Act 2000 (FOIA), the Data Protection Act 1998 (DPA) and the Environmental Information Regulations 2004). If you want information, including personal data that you provide to be treated as confidential, please be aware that, under the FOIA, there is a statutory Code of Practice with which public authorities must comply and which deals, amongst other things, with obligations of confidence.

In view of this it would be helpful if you could explain to us why you regard the information you have provided as confidential. If we receive a request for disclosure of the information we will take full account3 of your explanation, but we cannot give an assurance that confidentiality can be maintained in all circumstances. An automatic confidentiality disclaimer generated by your IT system will not, of itself, be regarded as binding on the Department.

1.12 **Issues relating to the consultation process**

If you have comments or complaints about the way this consultation has been conducted, these should be sent to:

Tunde Idowu, Consultation Co-ordinator
Department of Business, Innovation and Skills
Better Regulation Team
1 Victoria Street
London
SW1H 0ET

E-mail: Babatunde.idowu@bis.gsi.gov.uk
Tel: 020 7215 0412
Fax: 020 7215 0235

More information on the Code of Practice on Consultation is in **Annex E**.

1.13 Next steps

The indicative time line (para 4.39) sets out the anticipated next steps, along with a guideline timetable.

2. Scope

Scope

2.1 This consultation sets out the detailed legislative proposals to address unlawful file-sharing as set out in Action 13 of the interim Digital Britain Report (DBR)[1]. Action 13 states:

"**ACTION 13:** ***Our response to the consultation on peer-to-peer file sharing sets out our intention to legislate, requiring ISPs to notify alleged infringers of rights (subject to reasonable levels of proof from rights- holders) that their conduct is unlawful. We also intend to require ISPs to collect anonymised information on serious repeat infringers (derived from their notification activities), to be made available to rights-holders together with personal details on receipt of a court order. We intend to consult on this approach shortly, setting out our proposals in detail***".

2.2 These obligations will be imposed by Ofcom on ISPs and they will form the central elements of a code on unlawful file-sharing which Industry may put in place, supported by backstop powers exercisable by Ofcom if there is no Industry code. The code would cover among other issues practical supporting measures, including appeals and standards of evidence. It would also cover the provisions for the apportionment of costs.

2.3 This consultation will also seek to identify the key issues of the code and, where appropriate, seek views on alternative options.

2.4 The document 'What role for a rights agency?'[2] set out, in Annex B, our thinking on how the code would work in practical terms, what Ofcom would be expected to take into account in approving or drawing up such a code and what a code would cover. This document takes forward those ideas.

Background

2.5 The problem of "peer-to-peer" (P2P) file-sharing of copyright protected works without permission was identified by Andrew Gowers in his report to HM Treasury in December 2006[3].

"*Recommendation 39: Observe the industry agreement of protocols for sharing data between ISPs and rights holders to remove and disbar users engaged in 'piracy'. If this has not proved operationally successful by the end of 2007, Government should consider whether to legislate.*"

2.6 In its *Creative Britain* strategy document, published on 22 February 2008, the Government stated:

The Government recognises the value of the current discussions between internet service providers (ISPs) and rights holders; we would encourage the adoption of voluntary or commercial agreements between the ISPs and all relevant sectors. While a voluntary industry agreement remains our preferred option, we have made clear that we will not hesitate to legislate in this area if required. To that end, we will consult on the form and content of regulatory arrangements in 2008 with a view to implementing legislation by April 2009. [4]

[1] http://www.culture.gov.uk/what_we_do/broadcasting/5631.aspx
[2] http://www.ipo.gov.uk/digitalbritain.pdf
[3] The report and all papers associated with it can be found at: http://www.hm-treasury.gov.uk/independent_reviews/gowers_review_intellectual_property/gowersreview_index.cfm
[4] Creative Britain: New Talents for the New Economy: www.culture.gov.uk

2.7 The Government carried out the commitment to consult on possible legislative options via the consultation issued on 24th July 2008. This identified a number of possible options, including the Government's then preferred option of co-regulation, and sought views from all stakeholders.

2.8 The consultation received over 80 responses from ISPs, broadcasters, the games, music, film and publications industry, other industry stakeholders, individuals and consumer organisations.[5]

2.9 At the same time an industry Memorandum of Understanding (MOU) was signed between rights holders from the music and film industry and the six main ISPs in the UK. This committed signatories to a notification trial (whereby ISPs wrote to account holders identified as responsible for an alleged infringement) and undertook to investigate possible technical and other measures against repeat infringers. The MOU also covered a commitment to work towards developing new attractive sources of content and ways to educate consumers about the importance of copyright to the creative and wider economy. A copy of the MOU can be found at Annex F.

2.10 However it was clear from consultation that the preferred option had a number of issues which could not easily be resolved. The MOU also demonstrated that reaching a common agreement between the respective parties in the absence of a legal commitment was extremely hard. Nevertheless the MOU group undertook a great deal of good investigative work, particular around technical measures, legal issues and also on the process of notifications and this has helped formulate the proposals in this document.

2.11 As a result of the earlier consultation and the experience of the MOU group, Government has been convinced of the need for some legislative baseline to change the behaviour of the majority of file-sharers via an obligation on ISPs to notify broadband subscribers that their account has been identified as responsible for a copyright infringement. It was also clear from the consultation that most respondents felt rights holders should use existing legal routes to protect their copyright. The second obligation (to maintain a list of those accounts identified most often as responsible for infringements) will help rights holder to take legal action against the most egregious infringers.

2.12 The Government has made it very clear that rights holders and ISPs both have a role to play in tackling the problem of illicit P2P file-sharing. The introduction of these two obligations should help provide a framework to underpin the kinds of bilateral commercial agreements which the Government believes are essential to encouraging users of unlawful services to change their behaviour.

2.13 This document primarily deals with illicit use of P2P technology for copyright infringement. It does not examine the issue of commercial piracy, websites dedicated to unlawful copying (or the encouragement of) or the hosting of such websites. Neither does it examine the issue of format-shifting. All these issues fall outside the scope of DBR Action 13 and Gowers' Recommendation 39 and will instead be addressed separately by the Department of Business, Innovation and Skills and the UK Intellectual Property Office.

2.14 The proposals do refer to the rights agency (Actions 11 and 12 of the interim Digital Britain Report) and suggest a role for the agency in developing the code. Meanwhile, the legislation would place a duty on Ofcom to approve the Code and a back-stop responsibility to develop the code should a rights agency or an alternative industry grouping be unable to undertake this role.

[5] A copy of the consultation along with all non-confidential replies and the Government's response can be found at: http://www.bis.gov.uk/consultations/page47141.html

2.15 This document does not address the other issues and actions contained in the interim Digital Britain Report. These will be dealt with separately as part of the final Digital Britain Report. But it should be emphasised that we continue to see a role for industry to take a direct role in ensuring the successful future of the copyright based digital content industries. The proposed legislation, whilst self-standing and able to operate in the absence of a rights agency or equivalent, would be much more effective as a part of a wider industry attempt to significantly change both public and industry attitudes and behaviours than it would be alone.

3. Current Position & Context

Broadband market in the UK[6]

3.1 In 2007 Ofcom estimated there were some 460 niche ISPs[7] providing connection services, the vast majority of which are small or medium size enterprises. The market for broadband though is dominated by the top 5 ISPs who between them account for just under 90% of the residential and SME fixed broadband connections.

ISP	% share
BT	26.4%
Talk Talk /AOL/Tiscali	25.0%
Virgin Media	21.4%
Sky	10.6%
Orange	6.0%
Other	10.5%

In 2008, retail revenues from fixed residential and SME internet services were £3.4bn in the year to September or about 11% of total reported telecoms revenue (annualised this equates to around £4.5bn).

3.2 True mobile broadband is a relatively recent development. All mobile services are carried by one of the five network providers (O2, Orange, Vodafone, 3 and T-Mobile) although there are a number of "virtual" mobile services including Virgin Mobile and Tesco. As of Q3 2008 there were a total of 16.6 million 3G subscribers (ie handset or dongle) but this marked a 21% increase on Q1 2008.

3.3 However, the vast bulk of these will be handset users, rather than those accessing mobile broadband via data card or dongle. Using Q4 2008 tracker data, Ofcom estimate between 9-13% of UK adults have access to mobile broadband. One other point worth stressing is that about 70% of adults have both fixed and mobile connections. This suggests that currently mobile and fixed is more complementary, than competitive. Whether in time as mobile broadband costs decrease and speeds increase there will be a greater level of substitution remains to be seen.

3.4 Unlike fixed broadband services, mobile is not tied to an address. In terms of subscriber numbers, the majority in the UK use pre-pay, although for the higher value services (including 3G and mobile broadband) most have a contract. There will be a significant number of subscribers therefore for whom the mobile operators will either have no record of an address or no means of verifying whether an address is current.

Size of content industry

3.5 The main industries affected are films, TV (including sports rights), music, videogames and software. Films, TV, videogames and music generate joint annual revenues in the UK of over £15 billion. They are all part of the creative industries sector, which accounts for 6.4% of UK GVA[8]. Other sectors such as publishing are likely to be increasingly affected in the future

Music

[6] All figures from Ofcom unless otherwise stated
[7] Communications Market Special Report into Niche ISPs (Jan 2007)
[8] DCMS (2009): Creative Industries Economic Estimates

3.6 Taken as a whole the music industry is one the UK's biggest and most culturally significant creative industries and a big player in the national economy, contributing some £6bn annually (of which £1.3bn comes from exports earnings), and employing some 130,000 people.[9]

3.7 Although some 90% of record labels are SMEs (the independent sector), in economic terms the UK record industry is dominated by the four major labels and these tend to be identified by the public as the "music industry". However this is but one side of the business with live performances and publishing generating significant revenue and employment.

UK record sales 2007 – market share (source BPI)		
Label	**Singles**	**Albums**
Universal	32.2%	32.7%
Sony-BMG	22.6%	19%
EMI	13%	15.7%
Warner	12%	10.4%
Independents	20.2%	22.2%

Film

3.8 The "core UK film industry" - defined as film production in the UK (of both UK and overseas-initiated films) and the distribution and exhibition activities associated with UK films - generated £4.3 billion of the UK's GDP in 2006[10] The sector is dominated by the "big six" US companies.

3.9 According to statistics which cover films with production budgets of £500,000 and above, in 2008 production spending in the UK totalled £578.2 million with the UK involved in the making of 111 feature films (126 in 2007). It also makes a key contribution to UK generated content. Spend on indigenous British films was strong with the total UK spend reaching £192 million, 21% higher than 2007's £158 million.

Games

3.10 Currently there are approximately 160 development studios operating in the UK employing 10,000 people. In 2008, the UK computer games industry (games, software and accessories) recorded sales of £4 billion, compared with £2.2 billion in 2006[11]

Estimated damage caused by P2P file-sharing

3.11 It is impossible to accurately calculate the cost to industry resulting from unlawful P2P file-sharing given that estimates are based on survey data and counterfactual analysis of consumer behaviour. All figures therefore are subject to a degree of challenge and argument, not least due to the range of studies claiming different impacts of P2P on sales (see the Impact Assessment at Annex G).

3.12 However as was made clear in the earlier consultation, even when allowing for some inaccuracy, the level of losses suffered is considerable. The BPI claim P2P file-sharing costs the UK music industry £180m pa (2008) while IPSOS gives a loss in the UK for TV and films of £152m (2007).

3.13 Figures for software – the biggest of the creative industries – are difficult to obtain, but it is estimated by the Business Software Alliance that the global business software industry

[9] http://www.culture.gov.uk/what_we_do/creative_industries/3270.aspx
[10] Oxford Economics, The Economic Impact of the UK Film Industry, 2007
[11] Elspa/Chart track

suffers annual losses of some US$48 billion out of a total market of US$450 billion due to piracy. The bulk of these losses is caused by unauthorised copying of software within businesses, rather than by P2P.

Most downloaded video games in 2008

Spore (1,700,000)
The Sims 2 (1,150,000)
Assassins Creed (1,070,000)
Crysis (940,000)
Command & Conquer 3 (860,000)
Call of Duty 4 (830,000)
GTA San Andreas (740,000)
Fallout 3 (645,000)
Far Cry 2 (585,000)
Pro Evolution Soccer 2009 (470,000)

(source: torrentfreak)

Spore

According to the BBC within 10 days of the games launch, more than half a million people had downloaded a pirated version of the game using P2P technology. In comparison legitimate sales of Spore have passed the 2m mark. Spore retails at £30.

http://news.bbc.co.uk/2/hi/technology/7772962.stm

Commercial Models

3.14 It is widely recognised that any solution that would effectively tackle the majority of file-sharing must include the provision of new business models. There is little point in trying to shift consumer behaviour from the unlawful to the legal if there is no legal source which will allow consumers to access the type of content they want in a form and manner that best suits them and at a price they are willing to pay.

3.15 We recognise that there are a number of such models starting to emerge. In music the dominant iTunes now faces a challenge from new sources. Some offer advertisement funded streaming (eg Spotify and Last FM) with increasing a click through option to buy (download) content. Others, such as Datz, offer unlimited downloads to keep for an annual subscription fee. Elsewhere NBC Universal has had great success in the USA with Hulu. A significant recent development was the decision by the PRS to more than halve its on-demand streaming music rate from 0.22p to 0.085p per track, effective July 1 2009 and lasting for three years. Although this in itself will not automatically result in new commercial models, it should enhance the underlying economics of those models.

3.16 However it appears far too early to hail any of these as the legal alternative to P2P. Taking one of the most popular music models as an example, according to the BBC, Spotify has not succeeded so far in getting sufficient paid subscribers for its ad-free offering and, at the time of drafting, while experimenting in this area is yet to launch on a mobile platform[12].

CPDA

3.17 Section 97(A) of the Copyright Designs and Patents Act 1998 allows rights holders to apply to the High Court (or Court of Sessions in Scotland) to obtain an injunction against an ISP that another person is using its service to infringe copyright. This provision has never yet been tested in the courts, therefore there is no certainty about its effect.

What's happening elsewhere?

3.18 In the July 2008 consultation we highlighted the approach taken in both the US and France. Since then there has been a number of developments in both countries but also elsewhere.

[12] http://news.bbc.co.uk/1/hi/technology/7971784.stm

3.19 **The French** approach to dealing with illicit P2P – often characterised as "3 strikes and you're out", known officially as La Loi HADOPI (Haute autorité pour la diffusion des œuvres et la protection des droits sur l'internet) – met with a significant set-back having suffered an unexpected defeat in the National Assembly. Although the National Assembly passed the bill on 12th May 2009 and the Senate shortly afterwards, the French Constitutional Council overturned part of the legislation. The Council ruled that the decision to suspend Internet connections of digital pirates should be made by the courts as opposed to an administrative authority (HADOPI, which the law plans to create). It argued that current provisions did not comply with French constitutional principles such as presumption of innocence and freedom of speech. It is understood that the Government intends to introduce those parts of the legislation approved by the Constitutional Council, which would set up HADOPI and allow the sending of warnings. The sanction part of the legislation is expected to be reviewed in line with the Council's ruling through a further (short) piece of legislation to be discussed in Parliament during the extraordinary session in July (or, alternatively, by adding articles to an existing text, but this is less likely). The government continues to argue that the gradual response mechanism can only be credible if it includes both prevention and sanctions. We understand that the annual running costs of HADOPI once it is fully operational is currently estimated at around £15 million per year, although the body is likely to be significantly more directly involved than a UK regulator, and depends on what changes may be required as a consequence of the Constitutional Council ruling.

3.20 On 6th May the **European Parliament** passed an amendment to the Telecoms Package which said:

> *"Article 8f(b) applying the principle that no restriction may be imposed on the fundamental rights and freedoms of end-users, without a prior ruling by the judicial authorities, notably in accordance with Article 11 of the Charter of Fundamental Rights of the European Union on freedom of expression and information, save when public security is threatened or for other legitimate reasons in which case the ruling may be subsequent".*

At the time of writing it is not clear whether this amendment will stand, or whether it will be the subject of a conciliation process.

3.21 AT&T in the **US** has agreed to send notifications letters, along the lines of the UK's proposed legislation. The company has indicated is as far as they will go without direction from a court.

3.22 In **Ireland** the main ISP Eircom agreed to adopt a 3-strikes approach as part of a Court settlement. However, all other Irish ISPs have refused to do so. ISPAI (Internet Service providers of Ireland) in their statement of 13th March 2009 made it clear that they would only take such action as required by (existing or future) legislation[13].

3.23 **New Zealand** was set to adopt legislation setting out a 3 strikes approach. Following a concerted consumer campaign, this has been delayed and, at the time of drafting, it is unclear when or if the legislation will be adopted.

3.24 Separate from the on-going court action against the "Pirate Bay", **Sweden** has just adopted legislation which will allow rights holders to go to court to force ISPs to disclose the subscriber details associated with an IP address identified with an infringement. This would allow rights holder to, if they so chose, to take legal action against the subscriber. As such this now appears to mirror the current legal position in the UK whereby rights holders can obtain a court order to force ISP to disclose personal information.

[13] http://www.ispai.ie/docs/20090313copyright.pdf

4. The Proposed Obligations

4.1 Ofcom will be placed under a duty to take steps aimed at reducing online copyright infringement.

4.2 Specifically they will be required to place obligations on ISPs to require them:

- to notify alleged infringers of rights (subject to reasonable levels of proof from rights-holders) that their conduct is unlawful; and
- to collect anonymised information on serious repeat infringers (derived from their notification activities), to be made available to rights-holders together with personal details on receipt of a court order.

4.3 Ofcom will also be given the power to specify, by Statutory Instrument, other conditions to be imposed on ISPs aimed at preventing, deterring or reducing online copyright infringement, such as:

- Blocking (Site, IP, URL)
- Protocol blocking
- Port blocking
- Bandwidth capping (capping the speed of a subscriber's internet connection and/or capping the volume of data traffic which a subscriber can access)
- Bandwidth shaping (limiting the speed of a subscriber's access to selected protocols/services and/or capping the volume of data to selected protocols/services)
- Content identification and filtering

4.4 The exercise of this power would be subject to consultation with stakeholders and subject to annulment by resolution of either House of Parliament. In determining the circumstances in which such an intervention is appropriate in general, we would propose that Ofcom first reviews evidence of the effectiveness of notifications and rights holder legal action against serious repeat infringers. We would expect that the start of a notifications program, under the agreed industry code, would form a baseline with Ofcom conducting its first review of effectiveness of notifications within a year. Similarly, Ofcom would review the effectiveness of targeted rights holder legal action within a year of the start of an orchestrated campaign of targeted legal action against serious repeat infringers. We would also expect Ofcom to consider the impact on infringer behaviour of education initiatives and the availability of legitimate services in assessing the overall effectiveness of the notification and collaboration obligations in reducing copyright infringement

4.5 If Ofcom is satisfied that the obligations and targeted legal action scheme has proved to be insufficient to dissuade serious infringers, then it will have a power to require ISPs to impose specified technical measures against infringing individuals. In deciding whether to exercise that power, Ofcom will have regard to all its relevant duties (including, for example, its general duties and the Community requirements in sections 3 and 4 of the Communications Act 2003) and any other relevant legal requirements (for example in privacy and data protection legislation). It will also have to be satisfied that the imposition of technical measures by ISPs is objectively justified, proportionate, transparent and does not unduly discriminate against particular persons or particular groups of persons. The extent to which those potentially subject to such technical measures will have an effective right of appeal which provides remedies and redress in appropriate circumstances will be a key consideration for Ofcom in deciding whether to exercise the power, and this will need to be reflected in the code (see 4.6 below).

4.6 Finally Ofcom will be placed under a duty to ensure that there is a code of practice, with which ISPs will be under a legal obligation to comply (and rights holders to follow if they wish to trigger action under the code), which has two functions:

- First, to underpin the two specific obligations above; and
- Second, to underpin any additional obligations that Ofcom might impose.

4.7 The expectation would be for this code to be prepared by an industry self-regulatory body and approved by Ofcom. In the absence of an industry code that Ofcom is able to approve (or if an existing industry code is revoked) Ofcom will be obliged to provide a code itself. In light of the urgency of the problem we are minded to oblige Ofcom to have such a code in place within 9 months of the legislation receiving Royal Assent.

We consider each of these obligations in detail below.

Preventing and reducing online copyright infringement: the obligations

4.8 This paper sets out a basic proposal for legislation that would require Ofcom to place specific obligations on ISPs within a framework that requires a code (with which ISPs will be legally required to comply) to establish the detail of how those obligations are to work. Ofcom would also have the power to go further and require ISPs, by statutory instrument, to take specified technical measures in relation to repeat infringers should they consider it necessary, subject to consultation with industry representatives and other interested parties and review by both Houses of Parliament. Ofcom would also need to approve a code of practice covering the operation of all such obligations. Ofcom would need to ensure that the procedures established in the code to impose and trigger such obligations were proportionate, transparent, evidence-based, non-discriminatory and objectively justified. In the absence of such code, Ofcom would be able to exercise backstop powers to draft its own code, which would be subject to stakeholder consultation before adoption.

Notification obligation

4.9 The specific obligation in terms of notification will sit on ISPs. Any ISP will be obliged to notify an account holder, upon receipt of appropriate evidence (standards to be set by the code) from a rights holder of an alleged copyright infringement on that account, of the existence of such evidence.

4.10 For the purposes of the new legislation, ISPs shall include all providers of electronic communications networks and services for the purposes of section 32 of the Communications Act 2003[14].

4.11 A request in respect of a specific infringement may only be made by the rights holder of that material or someone authorised to act on their behalf. This could include any rights agency acting on behalf of rights holders more generally if such an agency were to exist. There may need to be a time limit as to how long after an infringement occurs a request may be made.

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14 Section 32 of the Communications Act provides that "electronic communications network" means—

(a) a transmission system for the conveyance, by the use of electrical, magnetic or electro-magnetic energy, of signals of any description; and

(b) such of the following as are used, by the person providing the system and in association with it, for the conveyance of the signals—

(i) apparatus comprised in the system;

(ii) apparatus used for the switching or routing of the signals; and

(iii) software and stored data.

(2) "electronic communications service" means a service consisting in, or having as its principal feature, the conveyance by means of an electronic communications network of signals, except in so far as it is a content service.

Question 1: Is this restriction right? Is there anyone else who ought to have a right to trigger the obligation?

Question 2: Should there be a time limit from the date of a specific infringement by which a request needs to be made? If so, what should it be?

4.12 The ISP will have to send a notification to the account holder setting out the details of the alleged infringement. The notification will also have to provide:

- advice and guidance on securing wireless networks where appropriate;
- a statement that the notification is sent pursuant to the legislation;
- advice on how/where to access legitimate content;
- information about copyright and why it is important; and
- anything else specified by the code.

4.13 It will also include a statement informing those notified that data on the number of times they are identified by the rights holder will be kept, and that this information may be disclosed to the rights holder on receipt by the ISP of a court order, which may result in proceedings against the account holder by the rights holder.

Question 3: Is this list right? Is there anything else that should be specifically added to this list? Should there be any more detail on any of these points in the legislation, or is it OK to leave that for the code?

4.14 The standard of evidence required from rights holders should, as a minimum, establish an infringement on the balance of probabilities. The template used by the BPI in the MOU trial should serve as a model for this as it has proved satisfactory to all the ISPs in the trial and has not provoked any particular concerns by consumers affected. This will need to be defined by the code.

Question 4: Does this need to be set out in any more detail in the legislation, or is it sufficient to require it to be set out in the code?

4.15 We anticipate the larger ISPs would seek to automate the process as far as possible. In any event they would need to commit resources sufficient to discharge these obligations and handle any ensuing consumer response (e.g. via call centres). To do so they will need to estimate the likely volumes of notifications they will be receiving.

Question 5: This obligation is specified without any volume limit. Is that right? Should there be a restriction on how many notices a rights holder can serve, or that an ISP needs to honour (either from a specific rights holder or in total)?

Question 6: Alternatively should volumes be agreed (say) 6 months in advance between rights holders, ISPs and Ofcom to allow ISPs to prepare accordingly?

4.16 Costs arise in this process in a number of ways: firstly the cost of identifying the infringements and presenting the evidence in the required format; secondly, the cost of using that data to identify, and notify, specific account holders. In both cases the costs might take the form of capital investment in systems or technology and marginal running costs. There will also

be costs incurred by Ofcom in meeting its obligations to approve the code, including the necessary costs for setting up an appropriate appeal mechanism.

4.17 Better Regulation Principles do not cover the apportionment of costs. The aim should be to keep the costs of regulation on business as a whole to a minimum (and ensure they are proportionate to the desired outcome). As a general principle we believe that the cost should be borne by the party that will benefit, though there may be circumstances where it is appropriate to diverge from that.

4.18 **Costs of notification obligation**. The details of how costs are apportioned between the different players will be worked out as part of the underpinning code. However, in terms of broad principle we consider that the variable costs of notification and Ofcom's costs in carrying out these duties, should be split between rights holders and ISPs with the intention of ensuring that there are appropriate incentives on all parties to seek to improve the cost-effectiveness of the overall programme of activity to prevent online copyright infringement. We also consider that the costs of any additional measures that Ofcom imposes on ISPs should be shared in some way between rights holders and ISPs. We intend to include in the legislation a power for Ofcom to require that ISPs/rights holders jointly contribute to fund certain costs, including those incurred by Ofcom in complying with these duties and exercising these powers. Ideally we would like to see the precise split agreed in the code by industry. However, it has been put to us that it is unrealistic to expect an industry consensus to form on this, and that failure to agree could delay the process. If necessary we could specify the proportions in which costs are to be allocated, but we would prefer to leave some flexibility in how this is reflected in the code, taking into account the underlying principles of proportionality, transparency, effectiveness and fairness

Question 7: Is this approach to costs the right one? Is there anything else in relation to costs that should be taken into account in the legislation? Should the legislation specific exactly how costs are to be shared or is it right to leave some flexibility in how the legislative requirements are reflected to the code?

Serious Infringer Obligation

4.19 The second obligation is to maintain data relating to the notifications sent to their customers on behalf of each rights holder or their designated agent. To be absolutely clear - there is no intention to require ISPs to monitor the activity of their customers. Rather, they will collate information on the number of times they have been requested to send, and have sent, notifications to each customer by each rights holder or their representative.

4.20 In practical terms this means that an ISP would need to know, and be able to provide anonymous data relating to each alleged infringement (based on the underlying subscriber identity), enabling the rights holder to group infringements/notifications and hence identify the IP addresses associated with multiple alleged infringements.

4.21 Rights holders could use this information to select these multiple infringements to go to court to secure the release of the personal details of relevant account holders in order to take legal action against them. The rights holder would be able to present evidence in relation to all the notified alleged infringements by that account holder in any subsequent litigation.

Question 8: Do you see any legal difficulty with linking a new notification with a previously gathered set of anonymised data in this way? If so, what specifically is likely to be the problem?

Question 9: There is some evidence (research and empirical) that further warning letters result in a further reduction in people file-sharing. Do you think multiple letters should be sent (up to a maximum of (say) three) and, if so, what should trigger these? (for example, should this be on a strict, one infringement one letter basis or should there be specified levels (eg 1st letter on 1st infringement, second letter on 10th, third on 20th)

For clarity we would anticipate that multiple letters would escalate in tone.

Please note the Impact Assessment includes the assumption that multiple letters are sent to persisting infringers. Costs in the IA have been calculated under the assumption that a single letter is sent to 70% of infringers and 10 letters are sent to the remaining 30% over a period of 10 years.

4.22 **Costs associated with serious infringer obligation**: There will be costs to the ISPs of collecting and processing this data. There are also significant costs to any rights holders who chose to go to court to apply for identification of a serious infringer and, obviously, substantial costs in any subsequent litigation. We propose that rights holders meet their own costs in this context. However, in recognition of the responsibilities that we are placing here on ISPs we also propose that ISPs should meet their own costs in collecting, maintaining and processing data in pursuit of fulfilling this obligation. None of this should act to prevent companies or parties with interests in common from taking action jointly and sharing the costs at their own agreement. In particular, if a rights agency were to exist, and were to take civil action on behalf of rights owners, the legislation would not constrain how this action could be funded.

Question 10: Do you agree to the approach on costs set out here? Are there any additional factors that we should take into consideration here?

Ofcom power to impose other obligations

4. 23 We are suggesting that Ofcom should have a power to require ISPs to take technical measures (which will be specified in the legislation) against serious repeat infringers aimed at preventing, deterring or reducing online copyright infringement, such as:

- Blocking (Site, IP, URL)
- Protocol blocking
- Port blocking
- Bandwidth capping (capping the speed of a subscriber's internet connection and/or capping the volume of data traffic which a subscriber can access)
- Bandwidth shaping (limiting the speed of a subscriber's access to selected protocols/services and/or capping the volume of data to selected protocols/services)
- Content identification and filtering

This element of the proposal is new and will be contentious. However, technology changes, and the ways that consumers and markets operate also change. It is entirely possible that the obligations on notification and collection of anonymised information on repeat infringers that may lead to legal actions taken by rights holders that we set out here will not, by themselves, deter some infringers. If that is established it is important that Ofcom should have the ability to take further steps to reduce copyright infringement significantly, in line with the long term objective.

4.24 There are a number of factors that Ofcom will need to take into account. In the first instance it will be important for Ofcom to see the effect of the specific obligations set out here. A minimum 12 months period will be required in which the effect of the specific obligations can be assessed against a baseline determined by Ofcom– it is essential that, if further conditions are imposed, it is done on the basis of the best available evidence.

4.25 We also consider that there needs to be some clarity in terms of what would trigger the process of applying further obligations. It needs to be one which gives both rights-holders and ISPs strong incentives to make the notification system work. We intend to use the 70% reduction measure commonly accepted as representing a significant reduction as the benchmark and Proportionate Notification Response as the trigger mechanism. That is, if the baseline unlawful peer to peer universe identified by Ofcom was 100, and notifications were sent to 50 per cent of that universe with prosecutions against serial repeat offenders, the benchmark would be met if there was a 35 per cent reduction in unlawful file-sharing (i.e. 70% of 50%).

4.26 In doing so, they will also need to look at the development of the content market and the extent to which content owners and service providers are actively providing options which offer a real consumer benefit to move people away from unlawful activity. Ofcom will also need to consider the extent to which the owners of copyright have taken effective action to educate consumers and change public attitudes to copyright infringement and engaged in an orchestrated campaign of targeted legal action against serious repeat infringers.

4.27 Crucially, the exercise of this power would be subject to consultation with stakeholders and **subject to annulment by resolution of either House of Parliament**. This should ensure that the power cannot be used frivolously, but is available in the event that the specific earlier options (notification, targeted legal action), together with concerted action from industry to change consumer behaviour, are shown to have failed to change the behaviour of specific infringers, and consequently to reduce copyright infringement significantly, in line with the long term objective.

4.28 In deciding whether to exercise the power, Ofcom will have regard to all its relevant duties (including, for example, its general duties and the Community requirements in sections 3 and 4 of the Communications Act 2003) and any other relevant legal requirements (for example in privacy and data protection legislation and the e-Commerce Directive). It will also have to be satisfied that the imposition of technical measures by ISPs is objectively justified, proportionate, transparent and does not unduly discriminate against particular persons or particular groups of persons. Ofcom would have to be satisfied that there was evidence to demonstrate that the measure would be effective for addressing the behaviour of the targeted, serious repeat infringers and that there was an effective right of appeal which provides remedies and redress in appropriate circumstances for those potentially subject to the measures. The mechanism for handling appeals will therefore need to be set out in the code.

Question 11: Do you agree with the list of further measures that could be imposed and the conditions to which their application must satisfy?

Question 12: Is 12 months about right to allow a proper assessment of the efficacy of obligations? If not, what would be a better period, taking into account the need to react both expeditiously and on the basis of good evidence?

How the notification process and possible court action could work

- Rights holders identify cases of infringement and send details including IP addresses to ISPs

- ISPs verify standard of evidence and link infringement to subscriber account.
- ISPs send (multiple) letters to subscribers identified as infringing. Those identified as the most frequent added to the serious infringers list.
- Rights Holders use the serious infringers list as the basis for a large scale "Norwich Pharmacal" order to obtain the names and addresses of those on the list.
- Rights Holders send "final warning" letter direct to infringer asking them to stop file-sharing. Clear warning of likely court action if warning ignored.
- Rights Holders take court action against those who ignore final warning.

Code of practice

4.29 Finally, the legislation shall provide that ISPs (and rights holders who want to trigger action under this proposal) shall comply with a code prepared by industry and approved by Ofcom, or if no industry code is produced or is not approved or revoked by Ofcom, to comply with a code prepared by Ofcom. **In light of the urgency of the problem we are minded to oblige Ofcom to have such a code in place in time for the common commencement date.**

4.30 For compliance with both, the specific obligations or any new obligations, ISPs would have to abide by the provisions of a code to be approved by Ofcom. Where (i) there is no industry code; or (ii) the industry code is not appropriate; or (iii) where Ofcom revokes an existing code, Ofcom will need to provide an alternative code by statutory instrument.

4.31 As with section 121 of the Communications Act 2003, Ofcom would have the power to approve a code agreed by another person that contains provision enabling ISPs to fulfil their obligations under the legislation aimed at the reduction or prevention of online copyright infringement and that, in the opinion of Ofcom, meets the requirements of a code as set out below and which it would be appropriate to approve.

4.32 Again borrowing from section 121 of the 2003 Act, Ofcom should not approve such a code unless they are satisfied:

a) that there is a person who, under the code, has the function of administering and enforcing it (in this case that will be Ofcom themselves, so (a), (b) and (c) are included for illustrative purposes); and
b) that person is sufficiently independent of both ISPs and rights holders;
c) that adequate arrangements are in force for funding the activities of that person in relation to the code;
d) that the provisions of the code are objectively justifiable in relation to the activities to which it relates;
e) that those provisions are not such as to discriminate unduly against particular persons or against a particular description of persons;
f) that those provisions are proportionate to what they are intended to achieve; and
g) that, in relation to what those provisions are intended to achieve, they are transparent.

In addition, the code will include an appeal mechanism, and provisions for the apportionment of costs between ISPs and rights holders

Question 13: Do you agree with this list of things that Ofcom need to satisfy themselves of before approving a code? Is there anything else that Ofcom should be obliged to consider before approving such a code?

Question 14: Do you agree that a code needs to be in place in time for common commencement? Is it realistic to expect such a code to be developed in less than 12 months, could it be done sooner, and if not what would be a realistic estimate?

4.33 Ofcom would of course not approve any part of a code that imposes an obligation on an ISP that would contravene the e-Commerce Directive or any other relevant statute – e.g. data protection, privacy etc.

4.34 Provisions in this code must:

a) provide for a fair and transparent appeals process for consumers, providing remedies and redress in appropriate circumstances;
b) establish the standards of evidence required to trigger a notification under this proposal;
c) set out what has to be covered in the notification and other relevant details about the process of notification including the handling of repeat notifications and, if necessary, the number of notifications that any rights holder can request to be made;
d) apportion costs of any action, including notification, covered by the code between the relevant parties and left open to refinement by the legislation;
e) provide for a dispute resolution mechanism between rights holders, consumers and ISPs; and
f) set out the process for the identification of 'egregious' infringers (i.e. how data is to be kept and in what form and when rights holders should have access to it in anonymous form before a court order is obtained). [N.B. the data referred to here is not personal data – it is an aggregation of the data provided by the rights holders]

Question 15: This list seeks to set out all the requirements of the code to enable the operation of the first two obligations. Does it do so? Is there anything else that the code must cover in order to enable the effective operation of those obligations and if so, what?

4.35 Ofcom should have the power to fine ISPs for failure to comply with the code. Where a rights holder fails to comply with the code, the code would be void in respect of that rights holder's requests to ISPs to take action to prevent or reduce online copyright infringement. Where ISPs have taken action as a result of a request from a rights holder who is in breach of the code, for example, on the basis of incorrect evidence or a flawed identification process, then Ofcom should have the power to fine the rights holder. In addition, the offending rights holder should indemnify fully affected ISP against any subsequent remedies granted to affected consumers.

4.36 Ofcom, as Regulator under the proposed legislation, will abide by the Hampton Principles and the Regulators' Compliance Code:

http://www.bis.gov.uk/files/file45019.pdf

Question 16: Are there any other restrictions or requirements that should be placed on Ofcom in pursuit of their role in relation to this code?

Consumer protection

4.37 As reflected above the Government is conscious that there needs to be protection in place for consumers who consider that they are being targeted wrongly. This should be established for operation during the operation of the original obligations. While there may be few strenuous objections to being notified, the warning that any further notifications received from rights holders will be noted in order that serious infringers can be identified for possible legal action by rights holders might well result in consumers seeking explanations and correction where they consider the evidence to be faulty. It also seems reasonable and appropriate that, should further obligations be imposed, consumers have access to a clear and transparent (and independent) appeals mechanism since such measures may be taken against them without the benefit of a judicial hearing. In those circumstances it may be appropriate for an enhanced consumer appeal process to be introduced along the lines of an ombudsman.

4.38 As indicated, this should be one of the areas covered by the code, and the costs of the independent consumer appeals process should be shared along the same lines as that as Ofcom.

Time line

4.39 In order to help respondees we have included an **indicative** time line below which may help answer the questions about allowing sufficient time and the appropriateness of assessment periods. What this illustrates is that, on the face of it, it may be some time before technical measures are brought into play, assuming they are necessary. However, it is important that such measures are introduced only after careful consideration of the evidence. One way that industry itself can make a real difference at the beginning of the process is by working together to develop the code for approval prior to the legislation coming into effect. That should give the legislation a real head start. Of course some parts of that will be more contentious than others, but progress should nevertheless be possible on a number of important fronts, and the less that Ofcom has to develop from scratch the quicker the final code can be approved, and the obligations introduced.

Indicative Time Line

16 June 2009	ConDoc published. Industry invited to begin process of devising a code for adoption by Ofcom with Government facilitation if welcome.
15 Sept 2009	Closure of consultation
By 15 December 2009	Publication of Government Response Document
Dateline zero	Royal Assent. Ofcom given duty to adopt or develop code by which industry can comply with obligations on which they will consult
Zero + 8 months	Notification to EU of near final version of code under Technical Standards Directive
Zero + 9 months	Commencement of industry obligations. Baseline date for assessment of effectiveness of initial obligations
Zero + 11 months	Two months for system implementation and start of operation
Zero + 17 months	Initial 6 month review – light touch, possibly via a workshop to consider the state of play.
Zero + 23 months	End of review period. If Ofcom has concluded from initial review and other evidence that there is a reasonable likelihood that existing obligations are not sufficient they will have worked in parallel on developing a code to cover additional measures, and consulted on their appropriateness
Zero + 25 months	Ofcom review effectiveness of initial obligations based on 12 months evidence. If the conclusion is that original conditions have: • been fully utilised; • that other factors are consistent with clear effort to bring a thriving legitimate content market into being; and • that the effect on infringement is less than anticipated across a significant part of the digital content • that other technical measure would be efficacious and proportionate etc Ofcom will, based on the previous consultation, make application for a Statutory Instrument to introduce one or more technical measures from the list
Zero + 28 months	Introduction of new measure(s), and beginning of assessment of efficacy of new measures
Zero + 40 months	End of second review period. As above, on request Ofcom will consider evidence and case for any further intervention
Zero + 60 months	Sunset/review requirement in new Act

4.40 This is illustrative only, and there may be further scope for shortening the timeline, such as suggested above where industry is able to co-operate in developing the Code in anticipation of legislation. This would leave Ofcom the more straightforward task of approving

and adopting a Code, rather than developing one from scratch (although of course they would still need to carry out a proper consultation).

4.41 This is based on the assumption that Ofcom will establish a baseline level of unlawful file-sharing activity at the point at which a code covering notifications and identification of egregious offenders becomes operational, and to make a further measure of unlawful file-sharing activity after the code has been operational for 6 and 12 months. Ofcom would also need to satisfy themselves that the other elements of the package such as education and commercial developments have also taken place. If after 6 months there is not significant measurable progress, Ofcom should consult on the detail of the additional measures and their operation and work with industry on drawing up the code of practice that would be needed to support them in practical terms in order to facilitate a quick implementation should the need arise. If at the end of the 12 month period it is clear that there has not been a significant reduction in unlawful file sharing Ofcom should use its backstop powers to introduce those additional measures. However, it should be recognised that working in this way will have significant resource implications for Ofcom, the costs of which they will need to look to recover from industry participants. It might also be the case that the 6 month review point is otiose, or even slows things down, in which case it may be better for Ofcom to develop their reserve position during the whole 12 month period.

Question 17: What are your views on the time line suggested above, and the ways in which it could be reduced? Are there other ways in which this could be shortened without hazarding essential safeguards and the need for decisions to be made on the basis of the best available evidence? Do you think a 6 month review point during the initial assessment period would be useful?

Role of a self regulatory body

4.42 We hope that an industry body (the 'rights agency' envisaged in the Digital Britain Interim Report) will come into being to draft codes under which the obligations would operate for Ofcom to approve. While in response to the Government's consultation on the rights agency 'straw-man', there was no consensus of support for any top down role for an industry body outside the code-drafting area, the Government sees the case for a small industry body with the code framing function which could develop organically (e.g. as an agent for rights-holders in pursuing court orders) if consensus developed between the parties that such functions were desirable and cost-effective. There may also be value in an industry body co-ordinating education and awareness raising.

4.43 Ofcom would be responsible for approving the code and also responsible for ensuring that non-rights agency stakeholders (e.g.) consumer groups have proper input into the process.

4.44 We understand that some industry partners are keen to develop a list of illegal sites to which access could be blocked. This is a matter for industry by agreement, and the rights agency could undertake the role of identifying such sites if industry members wished it to do so. However, if blocking of sites were to be a part of any new obligation imposed by Ofcom the identification of such sites would need to be subject to appropriate court processes to ensure that they were indeed operating illegally before ISPs could be obliged to block them.

4.45 We will not permit the rights agency to share any personal data. We do not intend to place the rights agency on a statutory basis for the purposes of addressing unlawful P2P file-sharing.

Question 18: Do you agree that this is an appropriate role and structure for the rights agency?

Impact on Small Businesses

4.46 The intention is for the obligations to fall on all ISPs in the UK. However we recognise there are a number of arguments for considering exclusions, either on the face of the legislation or by giving Ofcom latitude to consider exclusions in relation to a set of pre-defined criteria.

4.47 The Government announced a new approach to regulating small firms in the 2008 Enterprise Strategy. Under this approach, policy makers are required to consider whether alternative approaches (e.g. simplified inspection, less frequent reporting, exemptions) are appropriate for firms with fewer than 20 full-time employees. This section sets out the issues facing some ISPs and for who a case for exemption might be made.

A risk based approach – a small business exemption

4.48 The broadband market is dominated by a few big ISPs who account for the vast bulk of consumer – and therefore P2P – traffic. Imposing a requirement on all ISPs regardless of traffic or P2P infringements could result in disproportionate costs when set against the volume of infringements the measures were set to combat. The big five ISPs (Carphone Warehouse/Tiscali, Orange, Sky, Virgin Media and BT) account for some 90% of the domestic market. More than 450 ISPs have an annual turnover of less than £1 million each.

4.49 The smaller SMEs fall into a number of different categories. Some might best be described as "community" ISPs whereby the consumers are geographically very concentrated in a small area and where the ISP may have been established with local funds to offer a better local broadband service.

4.50 Others are focused on the B2B market and offer a very different package (typically higher speed and more symmetrical upload/download rates). The business packages are usually higher cost that those aimed at the mass consumer market.

4.51 Many of the small ISPs are "white label" packages bought typically from BT whereby all the network and technical support is contracted back to BT and the ISP simply is a brand. The organisation behind the brand may be far from small – for example Tesco broadband is a re-badged BT package.

4.52 Small ISPs may be directed at a particular segment of the UK's population. Post Office Broadband is a white label ISP whose customer base is skewed towards a particular set of demographics who are less likely to be active file-sharers.

4.53 <u>If the obligations were to apply to all ISPs</u>, this could impose disproportionate costs (of up to 10% of turnover – approximately some £80,000 per business) on the SME ISPs in order to be able to abide by the obligations. Some would be forced to incur costs to be able to carry out notifications themselves whist others would need to re-negotiate contracts with the white-label provider in order to sub-contract the notifications. The impact on SME ISPs would be disproportionately high, set against the low levels of P2P in their customer base. It is likely any additional costs could not be absorbed by SME ISPs and would be passed onto their subscribers thereby making smaller ISPs uncompetitive by pricing themselves out of the market.

We have been considering a number of approaches:

<u>Universal Small Business Exemption</u>

4.54 <u>If there was a small business exemption</u>, possibly based on turnover, this would avoid the disproportionate impact on small businesses. However, there would be the risk of active

file-sharers migrating to these ISPs (although any significant migration would in time move the ISP out of the small business exemption threshold). It would also offer the excluded ISPs a cost advantage as opposed to those caught by the obligation.

4.55 Based on turnover, a small business exemption (using the standard SME criteria of micro business <10 and €2m and small business <50 and €10m) would mean all but the largest ISPs would not have to abide by the obligations. This would mean about 10% of residential broadband consumers would have their internet access provided by an ISP not covered by the obligations.

4.56 Some ISPs, although small in their own right, are operated by a much larger organisation (eg the Post Office, Tesco). In calculating turnover based exclusion, there would be a need to separate out the ISP turnover from that of the parent organisation.

Named Inclusion Order by the Secretary of State

4.57 An alternative would be for the obligations only to apply to ISPs named in an order from the Secretary of State. This would start with the five ISPs who between them account for 90% of residential broadband subscriptions. Other ISPs could be added if identified by Ofcom as, in Ofcom's judgement, they were accounting for significant numbers of P2P infringements. This would ensure that file-sharers did not migrate to smaller ISPs to avoid notifications; it would also ensure that smaller ISPs were not burdened with unnecessary costs. The danger of being added to the order should act as an incentive for smaller ISPs to take voluntary measures to prevent unlawful file-sharing.

Technical Exemption

4.58 Crudely speaking a minimum broadband connection of 1Mb/s is required in order to participate in P2P file-sharing (music is a notable exception although the limits placed by a slow connection or low allowance do restrict the volume of P2P traffic). Specifying a minimum level of broadband would exclude some smaller ISPs and possibly some mobile until such time as speeds increased.

4.59 On balance we are convinced of the case for a small business exemption on the grounds of proportionality and targeting. However, we are open with regard to how such an exemption should be calculated, and would welcome views.

Question 19: Do you agree that we should proceed with an intention to exempt small businesses? If so, have we chosen the right criteria?? Do you have a preferred method of exemption? Please give reasons if you object or if you foresee any unintended consequences not discussed here.

Proportionality

4.60 It is clear from the Impact Assessment that for some broadband providers, complying with the obligations could involve a very significant level of fixed costs. For networks where large numbers of subscribers appear to be engaged in unlawful P2P file-sharing, it is quite likely that such costs would be "proportionate". However it is also possible that there will be ISPs where compliance would require significant additional fixed costs but who have very few subscribers participating in unlawful P2P. Building on the "Named Inclusion Order by the Secretary of State" option, one further approach could be to require Ofcom to consider whether requiring such expenditure is proportionate on an individual basis before agreeing to extend the obligation to cover the ISP. Where an ISP is not named in the inclusion order Ofcom would

need to keep this under review should the volume of unlawful P2P activity on the network increase significantly.

Question 20: Do you consider there to be a case for considering any exclusions on other grounds including technical or proportionality? Please give reasons.

5. Developing regulatory options: better regulation

5.1 The Government has an ambitious and wide-ranging regulatory reform agenda that is one of the most respected programmes in the world.

5.2 Our aim is to ensure that the regulatory proposals outlined above will be compatible with the regulatory reform agenda, including the following:

a) The five principles of good regulation which state that any regulation should be: transparent , accountable, proportionate, consistent, targeted – only at cases where action is needed

b) The case for Government intervention is supported by a strong evidence-base presented as an Impact Assessment, showing that a number of policy options have been considered and the preferred option is justified.

c) The Impact Assessment clearly demonstrates that the benefits of proposed regulation justify the costs imposed on business, public and third sectors over time.

d) The principles identified by the Hampton Review of effective inspection and Enforcement (e.g. consideration given to how new policies can be enforced using existing systems and data to minimise the administrative burden imposed)

e) "Think Small First" – The Small Firms Impact Test aims to minimise the impact of regulation on small firms through flexibilities such as exemptions, simplified inspection, less frequent reporting etc.

5.3 It is necessary to consider all the issues that regulation could affect, not least so that the regulation is as effective as possible and unintended consequences are avoided. Such issues should be considered in the light of Better Regulation principles[15], and the following list represents the major factors any regulation might need to consider. It should be noted however that not all issues could carry equal weight for all option being considered.:

- clearly defined outcomes
- advance assessment of effects for at least five years after implementation
- full recognition of national, European and international factors
- looking beyond institutional boundaries, in line with the Government's broad strategic objectives
- flexibility, innovation and willingness to question existing procedures and encourage creative ideas
- using the best evidence from a wide range of sources
- constant review to ensure intended effectiveness without detrimental impacts elsewhere
- being fair to everyone affected, directly or indirectly, and recognising wider impacts
- continuing involvement of all key stakeholders from early development onwards
- systematic evaluation to learn from experience what works and what does not

[15] More information about these principles and the Government's commitment to better regulation can be found at: http://www.bis.gov.uk/bre/index.html

Annex A: Summary of Questions

The Proposed Obligations

Notification obligation

Question 1: Is this restriction right? Is there anyone else who ought to have a right to trigger the obligation?

Question 2: Should there be a time limit from the date of a specific infringement by which a require needs to be made? If so, what should it be?

Question 3: Is this list right? Is there anything else that should be specifically added to this list? Should there be any more detail on any of these points in the legislation, or is it OK to leave that for the code?

Question 4: Does this need to be set out in any more detail in the legislation, or is it sufficient to require it to be set out in the code?

Question 5: This obligation is specified without any volume limit. Is that right? Should there be a restriction on how many notices a rights holder can serve, or that an ISP needs to honour (either from a specific rights holder or in total)?

Question 6: Alternatively should volumes be agreed (say) 6 months in advance between rights holders, ISPs and Ofcom to allow ISPs to prepare accordingly?

Question 7: Is this approach to costs the right one? Is there anything else in relation to costs that should be taken into account in the legislation? Should the legislation specific exactly how costs are to be shared or is it right to leave some flexibility in how the legislative requirements are reflected to the code?

Serious Infringer Obligation

Question 8: Do you see any legal difficulty with linking a new notification with a previously gathered set of anonymised data in this way? If so, what specifically is likely to be the problem?

Question 9: There is some evidence (research and empirical) that further warning letters result in a further reduction in people file-sharing. Do you think multiple letters should be sent (up to a maximum of (say) three) and, if so, what should trigger these? (for example, should this be on a strict, one infringement one letter basis or should there be specified levels (eg 1st letter on 1st infringement, second letter on 10th, third on 20th)

For clarity we would anticipate that multiple letters would escalate in tone.

Please note the Impact Assessment includes the assumption that multiple letters are sent to persisting infringers. Costs in the IA have been calculated under the assumption that a single letter is sent to 70% of infringers and 10 letters are sent to the remaining 30% over a period of 10 years.

Question 10: Do you agree to the approach on costs set out here? Are there any additional factors that we should take into consideration here?

Ofcom power to impose other obligations

Question 11: Do you agree with the list of further measures that could be imposed and the conditions to which their application must satisfy?

Question 12: Is 12 months about right to allow a proper assessment of the efficacy of obligations? If not, what would be a better period, taking into account the need to react both expeditiously and on the basis of good evidence?

Code of practice

Question 13: Do you agree with this list of things that Ofcom need to satisfy themselves of before approving a code? Is there anything else that Ofcom should be obliged to consider before approving such a code?

Question 14: Do you agree that a code needs to be in place in time for common commencement? Is it realistic to expect such a code to be developed in less than 12 months, could it be done sooner, and if not what would be a realistic estimate?

Question 15: This list seeks to set out all the requirements of the code to enable the operation of the first two obligations. Does it do so? Is there anything else that the code must cover in order to enable the effective operation of those obligations and if so, what?

Question 16: Are there any other restrictions or requirements that should be placed on Ofcom in pursuit of their role in relation to this code?

Question 17: What are your views on the time line suggested above, and the ways in which it could be reduced? Are there other ways in which this could be shortened without hazarding essential safeguards and the need for decisions to be made on the basis of the best available evidence? Do you think a 6 month review point during the initial assessment period would be useful?

Role of a self regulatory body

Question 18: Do you agree that this is an appropriate role and structure for the rights agency?

Impact on Small Businesses

Question 19: Do you agree that we should proceed with an intention to exempt small businesses? If so, have we chosen the right criteria?? Do you have a preferred method of exemption? Please give reasons if you object or if you foresee any unintended consequences not discussed here.

Proportionality

Question 20: Do you consider there to be a case for considering any exclusions on other grounds including technical or proportionality? Please give reasons.

Annex B: Acknowledgements

We would like to thank the following organisations for their time and efforts in helping us produce this consultation:

- BBC
- British Music Rights (BMR)
- British Phonographic Industry (BPI)
- BSkyB
- BT
- Business Software Alliance
- Carphone Warehouse
- Channel 4
- Consumer Focus
- Federation against software theft (FAST)
- Internet Service Providers' Association (ISPA)
- PRS for Music
- Motion Picture Association (MPA)
- NBC Universal
- NESTA
- John Newbigin
- O2
- Ofcom
- Orange
- Premier Rugby Ltd
- Premier League
- Rugby Football Union
- Sony
- Thus
- Tiscali
- Time Warner
- T Mobile
- Warner Bros
- Universal Music
- Virgin Media

Annex C Identifying the infringer

The process

Rights holders actively search for on-line breaches of copyright. The process is also automated and can deal with and identify a large number of infringements at a given time.[16]

There are several key points:

- The identification process does not identify who had downloaded the material. Rather it identifies who has uploaded and thereby made the material available for copying.

- It is possible the uploader was not aware that they had made the material available. Most P2P software as a default allows other P2P users to access material on a computer. A user who intended to download a single music track in doing so might have made their entire music collection available for copying on-line. Although this is no defence in law, this is something which could be addressed via a notification.

- For a purely fixed broadband connection it is probable, but by no means certain, that the subscriber will know who has access to the account (it is possible for someone to gain remote control of your computer (botnet) via a Trojan programme downloaded onto your system). In contrast, the use of wireless technology means that a broadband subscriber can offer others (including complete strangers) access to the Internet via their connection. This could be deliberate (i.e.) wi-fi access provided in coffee bars, wireless access provided free in an educational or civic environment, or inadvertent (individuals not securing their home wireless hub).

- There is no legal obligation on consumers to secure their wireless routers or to check to ensure their security has been breached. All ISPs as a matter of course offer some form of protection for wireless connections, although they cannot ensure that consumers install or use it correctly. It is also the case that many of the standard or recommended protections can be breached with a little expertise.

In other words, while the process by which rights holders is reliable at identifying the internet connection used, it cannot be regarded as a reliable indication that the broadband subscriber identified was the individual responsible for the infringement or will have knowledge of the individual responsible. This could have implications for any decisions to impose more punitive sanctions under the code, such as requiring a more robust level of evidence.

These issues would need to be addressed as part of the notification – for example giving directions to information on how to properly secure a wireless connection or information on the legal position and the way in which P2P technologies operate.

[16] A fuller description of how infringements were detected was described in the earlier P2P consultation in July 2008.

Annex D What effect will these obligations have?

World-wide very little regulation has been put in place to combat unlawful file-sharing. What measures have been taken are mostly voluntary and have been (relatively) small scale. Decisions on the effectiveness of possible measures are based in no small part on research and survey data ("what would you do if…"). Although these surveys cannot be conclusive and are hard to compare (due to differing methodology and population) they do provide some indication of the likely effects.

Wiggin LLP - 2008 Digital Entertainment Survey [17]

7 out of 10 pirates say they would cease pirating if they received a warning from their ISP

The survey reveals that a warning notification email from an ISP would persuade 7 out of 10 consumers pirating digital content to cease unauthorised downloading.

Key facts on this story from the survey:

- 70% of those pirating digital content say they would stop downloading unauthorised content if they received an email or call from their ISP – this rises to 78% of male and 75% of female teens
- 66% would stop downloading completely if they felt there was a higher chance of being caught
- 62% say they are concerned about stories of prosecution in the news

Empirical experience of THUS (cited in response to the earlier P2P consultation)

"Recently we have also analysed[18] reports from January to December (inclusive) 2006 to see what impact forwarding notices has on our customers' behaviour. It should be noted that we have forwarded on P2P notices since 2005. Our analysis of this period showed that 70% of customers did not infringe again (or at least we did not receive a further notice about them) in the six month period after receiving the first notice; a further 16% stopped after the second notice."

THUS receive about 6,000 such notices per year.

http://www.bis.gov.uk/whatwedo/sectors/digitalcon/p2presponses/page49707.html

However, the survey evidence is by no means uniform and different surveys have produced different results. One of the most recent was produced by Harris and commissioned by the BPI. Based on a survey population of 1,200 file-sharers plus 4,000 non file-sharers it found that (of file-sharers) 33% would stop if they received a notification with a further 28% saying they would do "much less sharing". A hard core of 21% said they would carry on as before. [19] The latest 2009 Wiggins LLP Digital Entertainment Survey found 33% of file-sharers would stop after receipt of a notification. However, it was made clearer than for the 2008 report that there would be no further follow-up action. This is not what the Government is proposing.

Identification of serious repeat infringers

[17] http://www.wiggin.co.uk/upldfiles/Press%20release%20-%20EMR.pdf

[18] Thus applied two rules: (1) notices received within 10 days of each other about the same customer counted as one notice; (2) duplicate notices (i.e. same content, same customer) were notices received within a six month period

[19] BPI Harris March 2009 unpublished. Report cited with kind permission of the BPI.

There are indications that a small hard core is responsible for a high percentage of file-sharing. For example, the Sunday Times (January 2009) identified one individual file-sharer and claimed "one in three movies shared online was attributed to him" [20]

The voluntary MOU agreement between ISPs, music labels and film studios included a trial of a notification system. Some 72,000 notification letters were sent by six ISPs over a 12 week period. Although the trial was designed more to test the process, it was clear that a sizeable minority of subscribers were identified a disproportionately high number of times, given the 6.5m+ estimated population of file-sharers. [21]

It is also clear that a big attraction for file-sharers is pre-release material. Access to such material is limited – typically to studio/label employees, media (journalists) or retail outlets. It is also this material which is arguably the most damaging in terms of revenue to the content industry. The recent release of "Wolverine" was marked by the posting of a pre-release copy. This was downloaded an estimated 100,000 times in one day.[22] U2's most recent album "No line on the horizon" was similarly leaked with some 100,000 downloads within the first 10 hours.[23]

Any action which either reduces the availability of pre-release material or targets those responsible for placing large volumes of copyright material on-line should have a disproportionately large impact on file-sharing, either in terms of dealing with major infringers or by way of an example. There are examples of such action being successful.

IFPI's 2007 Music Report that states: "We have taken some 30,000 actions against illegal file-sharers globally and, as the research in this report shows, these actions clearly work. Illegal file-sharing in Europe was contained last year against a 30 per cent increase in broadband household penetration."[24]

In August 2008, action taken against an individual who placed a video game on-line resulted in a £16,000 fine (£6,000 fine plus £10,000 costs).[25]

[20] http://technology.timesonline.co.uk/tol/news/tech_and_web/personal_tech/article5574162.ece
[21] MOU working group notification trial (unpublished)
[22] http://news.bbc.co.uk/1/hi/entertainment/7978379.stm
[23] http://entertainment.timesonline.co.uk/tol/arts_and_entertainment/music/article5776098.ece
[24] http://www.ifpi.org/content/library/digital-music-report-2007.pdf
[25] http://www.theregister.co.uk/2008/08/19/file_sharing_gamer_fined/

Annex E: Code of Practice on Consultation

All Government consolations must adhere to the Code of Practice on Consultation. In particular they must follow the seven consultation criteria. These are:

1. Formal consultation should take place at a stage when there is scope to influence policy outcome.
2. Consultation should normally last for at least 12 weeks with consideration given to longer timescales where feasible and sensible.
3. Consultation documents should be clear about the consultation process, what is being proposed, the scope to influence and the expected costs and benefits of the proposals.
4. Consultation exercise should be designed to be accessible to, and clearly targeted at, those people the exercise is intended to reach.
5. Keeping the burden of consultation to a minimum is essential if consultations are to be effective and if consultees' buy-in to the process is to be obtained.
6. Consultation responses should be analysed carefully and clear feedback should be provided to participants following the consultation.
7. Officials running consultations should seek guidance in how to run an effective consultation exercise and share what they have learned from the experience.

Annex F

JOINT MEMORANDUM OF UNDERSTANDING ON AN APPROACH TO REDUCE UNLAWFUL FILE-SHARING

This voluntary MOU between key stakeholders from the ISP industry, the content industries, OFCOM and the Government lays the foundations for a self-regulatory regime to address the issue of unlawful P2P file-sharing.

OBJECTIVE

All parties agree that the objective of this MOU is to achieve within 2 to 3 years a significant reduction in the incidence of copyright infringement as a result of peer to peer file-sharing and a change in popular attitude towards infringement.

PRINCIPLES

This MOU establishes five principles under which action will be taken, and it is accepted that further work will be undertaken on individual issues:

1 Signatories believe that a joint industry solution to this problem represents the best way forward. This will enable progress to be made rapidly on an industry solution as back-up regulatory provisions are implemented and will ensure a light touch and flexible regime. Signatories agree to work together with each other and with Ofcom to agree codes of practice.

2 Signatories, led by the creative industries, will work together to ensure that consumers are educated to respect the value of the creative process, and the importance of supporting creators to invest time and resource in developing new work, and understand that unlicensed sharing of others' work is wrong.

3 Many legal online content services already exist as an alternative to unlawful copying and sharing but signatories agree on the importance of competing to make available to consumers commercially available and attractively packaged content in a wide range of user-friendly formats as an alternative to unlawful file-sharing, for example subscription, on demand, or sharing services.

4 Signatories will work together on a process whereby internet service customers are informed when their accounts are being used unlawfully to share copyright material and pointed towards legal alternatives. In the first instance ISP signatories will each put in place a 3 month trial to send notifications to 1000 subscribers per week identified to them by music rights holders, to agreed levels of evidence, as having been engaged in illicit uploading or downloading. Based on evidence from the trial, which will be analysed and assessed by all Signatories, Ofcom will agree with Signatories an escalation in numbers, widening of content coverage, and a process for agreeing a cap.

5 Signatories will be invited by Ofcom to a group to identify effective mechanisms to deal with repeat infringers. The group will report in 4 months and look at solutions including technical measures such as traffic management or filtering, and marking of content to facilitate its identification. In addition, rights holders will consider prosecuting particularly serious infringers in appropriate cases.

CODES OF PRACTICE

Signatories will draw up codes of practice to cover:

- standards of evidence;

- actions against alleged infringers;
- actions against repeat or criminal infringers;
- indemnity resulting from incorrect allegations of file sharing; and
- routes of appeal for consumers.

All codes would require the approval of Ofcom.

The presumption would be that wherever possible the codes should encourage bilateral commercial arrangements between parties.

Engagement in this process would be open [to ISPs and rights holders], but would not be compulsory. The costs incurred in any action against alleged infringers would be shared between parties; the apportionment to be agreed. The intention would be that members would work together to produce standard processes designed to minimise costs whenever possible and appropriate.

COMPLIANCE WITH LEGAL REQUIREMENTS

For the avoidance of doubt this MOU does not affect any of the existing legal rights, remedies or protections of the Signatories, nor does it prevent the Signatories from entering into any agreement, outside the MOU, that they may wish to enter into. Implementation of the MOU will be in compliance with the provisions of the e-Commerce Directive as it affects ISPs and their liability, including mere conduit status, as well as the Copyright Design and Patents Act 1988 and competition legislation.

Dated **24 JULY 2008**

[SIGNED]	**British Phonographic Industry**	**Motion Picture Association**
	BSkyB	**BT**
	Carphone Warehouse	**Orange**
	Tiscali	**VirginMedia**

Department for Business, Enterprise & Regulatory Reform
Department for Innovation, Universities and Skills
Department for Culture, Media and Sport

Annex G Summary: Intervention & Options

Department /Agency: BIS	Title: Impact Assessment of Legislative Options to Address Illicit file-sharing, final stage	
Stage: Consultation	Version: Final draft	Date: 16-06-2009

Related Publications: Consultation on legislative options to address illicit file-sharing (October 2008)
Government response to consultation (January 2009)
Digital Britain Interim Report, Action 13 (January 2009)

Available to view or download at:

Contact for enquiries: Pau Castells/ Tim Hogan **Telephone:** 020 7215 1650/1628

What is the problem under consideration? Why is government intervention necessary?

File-sharing - the exchange of content files containing audio, video, data or anything in digital format between users on a computer network - has increased significantly in the last few years. Government intervention is being proposed to address the rise in unlawful P2P file-sharing which can reduce the incentive for the creative industries to invest in the development, production and distribution of new content. Implementation of the proposed policy will allow right holders to better appropriate returns on their investment.

What are the policy objectives and the intended effects?

The policy objective is to make sure that investment in content is at socially appropriate levels by allowing investors to fully appropriate returns on their investment. The government is looking at the possibility of bringing in legislation aimed at reducing illegal downloading by making it easier and cheaper for rights holders to bring civil actions against suspected illegal file-sharers. The legislation would place an obligation to internet service providers (ISPs), when informed by right holders, to notify subscribers of their unlawful behaviour. It would also place a second obligation on ISPs to maintain records of the most frequent offenders, which would allow right holders to take targeted legal action against these infringers.

What policy options have been considered? Please justify any preferred option.

The Government has previously consulted on a range of possible legislative options, including "do nothing". The current proposal is based on the responses to that consultation and the assumption that notification against infringers allied with the threat of legal action would reduce illegal file-sharing by 70%. The legislation would be accompanied by a Code of Practice which would include agreed standards relating to the notification process, consumer protection, standards of evidence, cost sharing, etc.

Two options are considered in detail in the evidence sheets:

-Option one: Do nothing

-Option two: Preferred policy option outlined in Government Response (January 2009) to previous Consultation (July 2008)

When will the policy be reviewed to establish the actual costs and benefits and the achievement of the desired effects? Progress on the high-level objective to reduce unlawful file-sharing would be reviewed every 6 months by Ofcom.

Ministerial Sign-off For SELECT STAGE Impact Assessments:

I have read the Impact Assessment and I am satisfied that, given the available evidence, it represents a reasonable view of the likely costs, benefits and impact of the leading options.

Signed by the responsible Minister:

....Date:

Summary: Analysis & Evidence

Policy Option: Option two

Description: Preferred policy option outlined in the Government response (January 2009) to previous consultation (July 2008)

COSTS

ANNUAL COSTS		Description and scale of key monetised costs by 'main affected groups'
One-off (Transition)	Yrs	Costs to ISPs of complying with the legislation, including costs of notification to infringers of their unlawful behaviour, capital costs to ISPs, costs of setting up and running a call centre, annual capital and operating cost to MNOs and reduced demand for broadband due to higher prices.
£ 35 million	1	
Average Annual Cost (excluding one-off)		
£ 30-50 million		Total Cost (PV) £ 290-500 million

Other **key non-monetised costs** by 'main affected groups' Costs to low income/low valuation digital product consumers who would stop consuming digital content altogether rather than purchase it; costs to right holders of identifying infringing IP addresses and taking infringers to court.

BENEFITS

ANNUAL BENEFITS		Description and scale of key monetised benefits by 'main affected groups'
One-off	Yrs	Benefits to right holders of recovering displaced sales.
£ N/A		
Average Annual Benefit (excluding one-off)		
£ 200 million		Total Benefit (PV) £ 1700 million

Other **key non-monetised benefits** by 'main affected groups' Benefits to consumers in ensuring that investment in high quality and diverse creative content is at appropriate levels.

Key Assumptions/Sensitivities/Risks Costs to digital product consumers are not monetised since this content is only available illegally; US evidence indicates that were this cost to be monetised it could outweigh the monetised benefits. There are uncertainties around the estimates of the sales displacement effect on right holders, the costs to ISPs and MNOs, and the behaviour of notified infringers.

Price Base Year 2009	Time Period Years 10	**Net Benefit Range** (NPV) **£ 1.2-1.4 billion**	**NET BENEFIT** (NPV Best estimate) **£ 1.2 billion**

Question				Answer
What is the geographic coverage of the policy/option?				United Kingdom
On what date will the policy be implemented?				TBC
Which organisation(s) will enforce the policy?				Ofcom
What is the total annual cost of enforcement for these organisations?				£ TBC
Does enforcement comply with Hampton principles?				Yes
Will implementation go beyond minimum EU requirements?				N/A
What is the value of the proposed offsetting measure per year?				£ 0
What is the value of changes in greenhouse gas emissions?				£ 0
Will the proposal have a significant impact on competition?				TBC
Annual cost (£-£) per organisation (excluding one-off)	Micro	Small	Medium	Large
Are any of these organisations exempt?	Yes/No	Yes/No	N/A	N/A

Impact on Admin Burdens Baseline (2005 Prices) (Increase - Decrease)

Increase of £ 14.7m Decrease of £ 0 **Net Impact** £ 14.7m

Key: **Annual costs and benefits: Constant Prices**

[Use this space (with a recommended maximum of 30 pages) to set out the evidence, analysis and detailed narrative from which you have generated your policy options or proposal. Ensure that the information is organised in such a way as to explain clearly the summary information on the preceding pages of this form.]

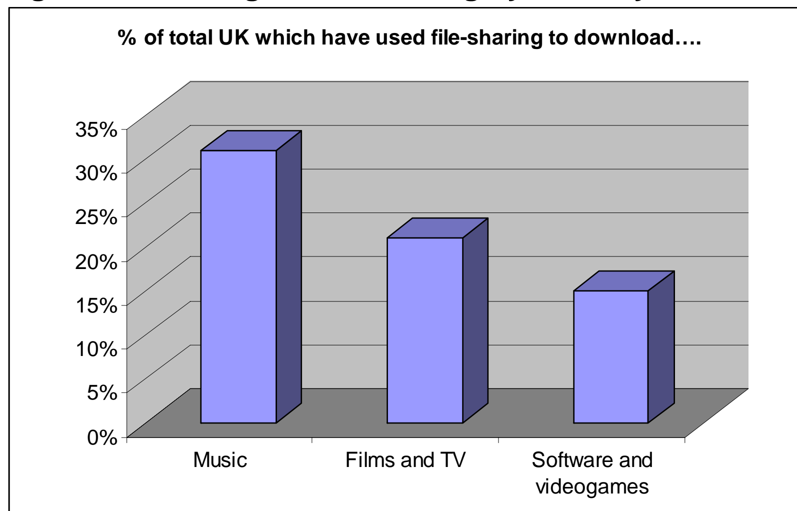
1. Background

P2P file-sharing is where users on a computer network share content files containing audio, video, data or anything in digital format by means of a series of ad hoc connections without the need of a central file server. File-sharing is becoming increasingly widespread, driven by increases in the number of households with broadband connections, quicker upload and download speeds, increasing bandwidth and improved connectivity and reliability of service.

Under the Copyright, Design & Patents Act 1998 making copyright material available for copying without the agreement or permission of the copyright owner is an offence, as is copying without permission. However it is only possible to identify the copyright infringer through personal data held by the ISP. Accessing this data requires a court order.

The sheer scale of P2P file-sharing means it is not practicable to take all those involved to court: right-holders estimate there are some 6.5 million people in the UK who are active unlawful file-sharers. Figure 1 shows that, at some point, 29% in the UK have illegally shared music, 21% have downloaded movies or TV content and 15% software or videogames.

Figure 1. P2P illegal downloading by industry



Source: Digital Entertainment Survey (2008)[26]

Further, due to the nature of the technology and the way in which individual infringements are identified, it is not possible for rights holders to identify who are the most frequent or serious file-sharers, making targeted legal action extremely difficult if not impossible. Legislation is needed to require ISPs to notify subscribers that they appear to be engaged in unlawful activity so that they can alter their behaviour. It is also needed to help rights holders to take targeted action about the most serious infringers.

2. Rationale for Government intervention

[26] http://www.entertainmentmediaresearch.com/reports/DigitalEntertainmentSurvey2008_FullReport.pdf

An important feature of creative industries like the music, software and film industries is that they are characterised by strong intellectual property rights (IPR). Strong IPR creates 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[27] nature of file-sharing and the spillover effects[28] which exist creates a free-riding problem whereby users may enjoy the benefits of file-sharing without paying the product's price[29]. 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.

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.

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 from searching, can purchase it from home realizing 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

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[27] 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 is not possible to prevent another person from consuming it.

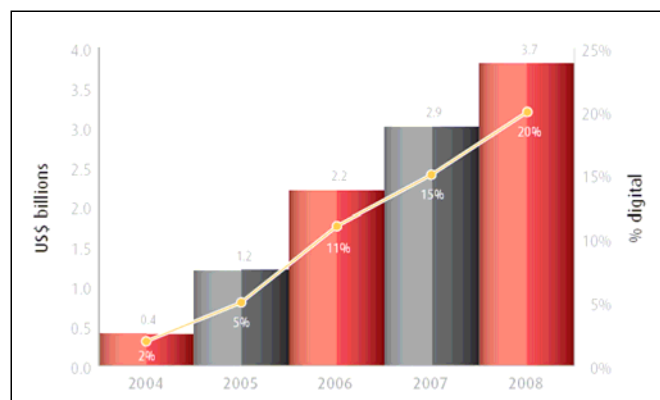
[28] Spillover effects arise when one person's actions have an impact on a third party.

[29] 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.

illegal music downloaders 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[30]. 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 (Figures 2 and 3).

Furthermore, it may result difficult to lead consumers back to legal sources of digital content once they have become familiarized with an illegal one. For example, even though Radiohead's album "In Rainbows" was offered for free in the band's website, over 2 million consumers had downloaded the album via P2P within the first month of commercialization.

Figure 2. Global digital revenues, music industry



Source: Digital Music Report (2009)[31]

Figure 3. Global digital revenues by industry

	Digital share
Games	35%
Recorded music	20%
Newspapers	4%
Films	4%
Magazines	1%

Source: PWC Global Entertainment and Media Report (2008)[32]

3. Options considered

The earlier consultation ("Consultation on legislative options to address illicit peer-to-peer (P2P) file-sharing", July 2008) included various options and an initial government preferred option. The Government response to the consultation on January 2009 stated that after reviewing the responses to the consultation, it now proposed that legislation should "require ISPs to take direct action against users who are identified as infringing copyright through P2P". The CBA (Cost Benefit Analysis) below discusses costs and benefits of the preferred option against the counterfactual option of doing nothing.

4. Scope of proposals

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[30] 2008 Digital Entertainment Survey; http://www.entertainmentmediaresearch.com/reports/DigitalEntertainmentSurvey2008_FullReport.pdf

[31] http://www.ifpi.org/content/library/DMR2009.pdf

[32] http://www.pwc.co.uk/eng/publications/global_entertainment_media_outlook_2008_2012.html

The business sectors affected by the proposed legislation are:

- Internet Service Providers (ISPs) and Mobile Network Operators (MNOs), including both fixed and mobile broadband service providers[33]. There are over 450 fixed ISPs in the UK which jointly generate revenues in excess of £3 billion a year, with the top 6 ISPs[34] accounting for around 90% of the market share[35].

  Mobile broadband connections are increasingly becoming widespread. The latest available data indicates that there are over 13 million subscribers to mobile broadband connections[36] in the UK, with new subscriptions to mobile broadband being already higher than new subscriptions to fixed broadband.

- The creative content industries (right holders). More specifically, those creative industries that supply or distribute goods or services susceptible of being copied digitally. The main industries affected are Films and TV (including sports rights), Music, Videogames and Software. Films, TV, videogames and music generate joint annual revenues of over £15 billion. They are all part of the creative industries sector, which accounts for 6.4% of UK GVA[37].

- To a lesser extent, the publishing industry would also be affected. Even though magazines and books are increasingly being traded digitally, the digital share of revenues in the publishing industry is still small due to strong consumer resistance to non-printed forms of reading (Figure 3). However, the publishing industry is not completely immune to illegal p2p downloading as indicated by the increasing availability of high quality electronic readers (e.g. Amazon's Kindle) and some anecdotal evidence showing that downloading of textbooks amongst the youngest has recently increased.

5. Policy options

Option 1. Do nothing

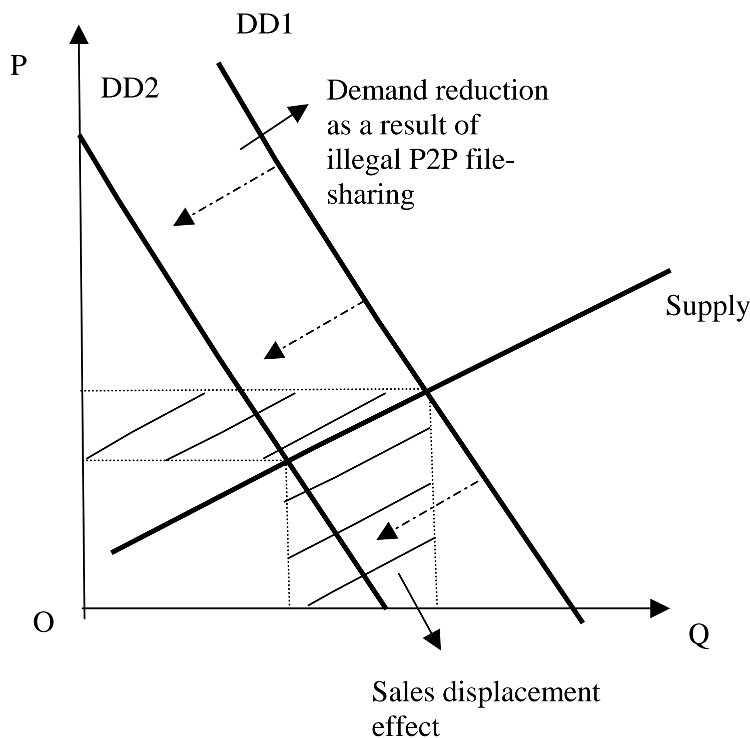
If no action is taken, we estimate costs for the creative content industries[38] to be in the region of £400 million per annum in displaced sales (see Figure 4)[39]. This figure includes estimates provided by the music, film and TV industries and our own estimate of the impact on the entertainment software and videogames industry under the assumption that the sales displacement effect is similar to that of the TV and film industry.

Figure 4 shows how the demand for legal digital content decreases as a result of some consumers shifting to illegal P2P downloading. The graph shows how the demand shifts from its original level at DD1 to a lower level at DD2. As a result the new market equilibrium (i.e. the intersection of demand and supply) produces lower total revenues for the digital content industry. This reduction (i.e. the sales displacement effect) is represented in Figure 4 by the striped area.

[33] The assumption is that unlawful file-sharing by dial-up internet subscribers is negligible since only broadband users are able to use P2P networks at reasonable speeds.
[34] BT, Virgin, Talk Talk/AOL, Sky, Tiscali and Orange (TIscali is in the process of being bought and ultimately merged with Tiscali)
[35] Ofcom estimates
[36] Mobile broadband connections include internet connection through either dongles (an electronic device that attached to a computer provides mobile broadband connection) or handsets
[37] DCMS (2009): Creative Industries Economic Estimates; http://www.culture.gov.uk/reference_library/research_and_statistics/4848.aspx
[38] Including TV, cinema, music, entertainment software and videogames.
[39] See Option 2 for a more extended discussion.

IPSOS (2007)[40] estimates a sales displacement effect of £152 million for the film and TV industry in 2007; JupiterResearch (2007) estimates a sales displacement effect of £160 million for the music industry in 2007. Research by the Digital Entertainment Survey (2008) suggests that levels of file-sharing in videogames and software are lower than those in music, TV and films. It is therefore reasonable to assume that the sales displacement effect for videogames is in the worst case scenario as large as that of the film and TV industry. Assuming a sales displacement effect of 2%, the leisure software and videogames industry lost approximately £80 million due to P2P downloading in 2007. It follows that the total sales displacement impact on the creative content industries is of approximately £400 million (£152+£160+£80).

Figure 4. Sales displacement effect. Lawful digital content market



There are reasons to believe that this figure may not be a completely accurate estimate of the displacement effect. In the first place, we haven't been able to fully assess the reliability of the methodology used in the music, TV and film studies. Even though both estimates fall into the range of values generally found in the literature (Table 1), estimates are proven to be very sensitive to the methodology used. Finally, this figure may be underestimating the effects of illegal file-sharing by not including the impact of illegal P2P file-sharing on publishing and live sports broadcasting.

File-sharing is likely to increase further in coming years driven by faster download speeds, additional bandwidth and improved reliability of services. This may lead to a rise in illegal downloading and a further increase in lost revenue and reduced investment in artists and new material since right holders are not currently able to reap all the benefits derived from their investment.

In the long-run, these costs could outweigh the welfare enhancing attributes of P2P file-sharing such as:

[40] http://www.ukfilmcouncil.org.uk/media/pdf/g/m/Ipsos_Piracy_UK_2007.pdf

- Enable consumers with low income or low willingness to pay for creative content to reap the benefits of consuming entertainment at a low or zero cost[41].

- Users have a wider choice of content since they are able to access music from less well-known artists (increasing consumer welfare)

- Easier access to a greater number of sources of information on content than previously possible

- Stimulating competition by providing a less expensive means of obtaining different forms of media, potentially reducing the physical formats and the market power of key players in the music film, software and computer games industries

- Increasing social welfare by helping to deliver broader social objectives such as improvements in media literacy

However, there is much uncertainty as to the long-run impact of illegal downloading as it is still a relatively new phenomenon. It is possible that industry and internet service providers (ISP) may respond to revenue losses by adopting new business models which can reduce the size of any revenue losses (e.g. Spotify for the music industry). Alternatively, new and improved technologies like DRM (Digital Rights Management) may be more effective in reducing the size of any revenue losses.

Option 2. Require ISPs to take direct action against users identified by right holders as infringing copyright through P2P

Benefits to right holders

Rights holders have estimated there are at least 6.5 million illegal file-sharers in the UK. With the increasing popularity of P2P downloading some file-sharers may have substituted legal purchases for illegal downloads, reducing legal sales. The expected effect of the legislation is to increase the revenues of the content producing industries by reducing unlawful file-sharing.

Under the assumption that 70% of infringers would stop downloading illegally following notification by letter of their unlawful activity[42], and based on trial data from the Memorandum of Understanding which indicates that this would reduce the volume of illegal downloading by 55%[43], we estimate industry annual revenues could increase by approximately £200 million[44].

However, the theoretical impact of P2P downloading on sales is disputed. Even though some file-sharers will have substituted legal purchases for illegal downloads, there are positive spillover effects from file-sharing that may increase sales of the creative content industries. These positive spillovers would be lost when implementing legislation. There are two main spillover effects:

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[41] See Option 2 for a more extended discussion.

[42] Results of the Digital Entertainment Survey (2008) suggest that 70% of infringers would stop illegal P2P downloads after being notified by their ISP.

[43] Aggregate statistics of letters sent to individuals during the trial suggest that 30% of infringers account for 45% of total illegal downloads. This suggests that those infringers downloading the most will be more resistant to stop their unlawful behaviour.

[44] approximately 55% of £400 million

- Sampling effects: File-sharing enables consumers to learn about new music, films or videogames by exploring and sampling new content at a zero cost. When consumers discover new content that they like they may decide to purchase it legally[45].

- Network effects: A product has network effects when consumers value a product more when the number of users increases. For example, on-line gamers benefit from the fact that more users are playing a videogame. Since file-sharing increases the number of users, the experience of videogaming improves and the willingness to pay for new games increases as well. This may lead to an increase in the number of legal units purchased.

With no clear theoretical prediction, the impact of illegal file-sharing on sales is an empirical question. Table 1[46] presents a selection of independent studies from industry and academia that have attempted to estimate the displacement effect on sales. Estimates of sales displacement range from 0% to 20% of total revenues since figures are very sensitive to the methodology used and the country and industry analysed[47].

Table 1. Selection of studies estimating the sales displacement effect

Studies on the effect of unlawful p2p downloading on industry revenues	Sales displacement effect (as % of total revenues)	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 and TV series industry	UK	Survey data
Zentner (2006), Journal of Law and Economics	8%	Music	7 European countries, including the UK	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 industry	Germany	Downloads proxies data
JupiterResearch (2007)	17%	Music	UK	Survey data
Peitz and Waelbroeck (2004), mimeo	20%	Music	16 countries, including the UK	Downloads proxies data

Benefits to Government

Part of the revenue regained by the industry will be realized in increased VAT revenue for the exchequer. We estimate these revenues to be in the region of £35 million from 2010[48] onwards. This VAT revenue does not add up to the total amount of annual benefits described in the right holders section but it refers to a fraction of the recovered sales which would be appropriated by Government through taxation.

Benefits to consumers

Implementation of the proposed policy will allow right holders to better appropriate the returns on their investment, subsequently fostering further investment in content and ensuring the long

[45] RD Gopal, S Bhattacharjee, GL Sanders (2006): “Do artists benefit from online music sharing?”; The Journal of Business, 2006

[46] Far from being an exhaustive review, the table provides an illustration of the variety of results that are obtained when using different methodologies

[47] If the displacement effect of P2P downloading on sales is zero, as a number of studies find (see Table 1), the costs of implementing legislation would outweigh the benefits, which would be negligible. Nevertheless, there would still be a case to be made around implementing the legislation if it is considered that the benefits surrounding a better long term sustainability of the industry outweigh the costs in welfare loss that new digital content consumers would experience.

[48] VAT rate of 17.5% from 2010.

term sustainability of the industry. This will ensure that high quality and diverse content is available to consumers.

Illegal P2P downloading undermines the positive effects that intellectual property rights (IPR) play in the economy. Creative content products have characteristics of public goods and can be copied at a very low cost, which makes free-riding (i.e. piracy) very easy. Copyright laws enable businesses which invest in creative content to appropriate the profits that derive from it by granting a monopoly to the exploitation of the product for a number of years. In a hypothetical extreme situation where everyone free-rides investors would not be able to appropriate any returns and investment in creative contents would cease.

<u>Cost to ISPs and MNOs</u>

1. Cost of compliance (ISPs and MNOs)

Evidence from the earlier consultation indicates that the costs of notification (identification of the infringer, postal costs, development of the letter, staff time and training) are in the region of between £3-10 per letter.

Results from the Digital Entertainment Survey (2008) indicate that 70% of unlawful P2P file-sharers would stop downloading digital products if they received a call or letter from their Internet Service Provider. The policy objective is to achieve this reduction within 2 years. Assuming that this objective is achieved by sending one letter to the 6.5 million illegal downloaders in the UK during one year, we estimate a range of one-off costs for the ISP industry between £20 and £65 million[49].

There may be additional costs if right holders ask ISPs to send further letters to those infringers that keep on downloading digital content illegally after being notified of their unlawful behaviour. According to the Digital Entertainment Survey (2008)[50], 30% of infringers would not stop unlawfully downloading content after receiving notification by the ISP, prompting further letters to be sent at a total cost of between £6 and £20 million per year[51]. Over a period of 10 years annual average costs are likely to be in the region of between £7.5m-24.5m.

Compliance cost figures are very sensitive to the underlying assumptions. If only 50% instead of 70% of infringers stopped, annual costs of compliance would increase from a range of £6-20 million to a range of £10-30 million. If instead of one letter a year right holders required two letters a year to be sent to serious infringers, the costs would double.

This cost would mostly fall on the 6 largest ISPs, with average one-off costs between £3-10 million for each of these ISPs and annual costs from sending further letters in the region of £1-3 million per ISP.

2. Cost of running a call centre/hotline (ISPs and MNOs)

A fraction of the infringers will want to contact the ISPs to query the letter and find out about legal implications. According to preliminary results from the Memorandum of Understanding trial, 1.5% of infringers did reply to the notification either by e-mail or telephone[52].

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[49] Calculated by multiplying the cost of sending a letter (£3-£10) by the total number of letters sent (6.5 million)
[50] See footnote 5
[51] Calculated by multiplying the cost of sending a letter (£3-£10) by the total number of letters sent to the remaining infringers (30% of 6.5 million). The assumption is that such letters are sent once a year. It may obviously be the case that some downloaders stop infringing copyrights after receiving a second letter; or that more than one letter is sent to the same infringer in a given year.
[52] Data provided by Ofcom

We assume that ISPs jointly set up a call centre to deal with the expected flow of calls (hence avoiding duplication costs). If we also assume that every call or e-mail reply is going to occupy an average of 10 minutes of an ISP operator's time, we estimate that the total amount of hours of staff required to deal with the level of calls derived from sending the first letter would be approximately 15,000 hours[53], representing an initial cost to the ISP industry as a whole of approximately £150k[54]. Under the assumptions we operate, these costs would be reduced in following years to under £50k[55] per annum.

3. Capital and operating cost to ISPs

There will likely be one-off capital costs to ISPs from the investment in the development of software and systems to automate the process of identification and notification of infringement. Preliminary indications by industry suggest that one-off capital costs could be in the region of £80k per ISP. Assuming that these capital costs are fixed for all ISPs, we estimate fixed costs from implementing the preferred policy option to be in the region of £35 million[56].

ISPs have indicated that there would be further costs derived from keeping the records of infringers as requested by the proposed legislation. It is not possible to provide an estimate of such expenditures since no cost estimates have been provided by the industry at this stage of the consultation process.

4. Capital and operating cost to MNOs

ISPs offering mobile broadband services will have additional costs due to technical difficulties arising from detecting infringers using mobile technologies.

Identification of infringers is technically more complex for mobile network operators. A single customer does not use a unique IP address as in fixed broadband networks. Instead, an IP address is shared by multiple costumers, therefore making it very difficult to distinguish the real infringers from the rest of users. Additionally, in order to identify infringers mobile network operators must monitor all the data activities undertaken by their subscribers. This implies that the costs are going to be necessarily higher and that there could also be data protection implications.

Capital and operating costs of designing and developing a system to link up IP addresses through mobile broadband are estimated to be in the region of £35 million[57] for the five mobile network operators[58] as a whole in its first year. This figure would be reduced to approximately £17.5 million per annum[59] from the second year onwards. Over a period of 10 years this represents annual average costs of approximately £19 million.

Additionally, it may not be feasible to detect some infringers since personal details of mobile broadband users are not necessarily registered with the ISP (pay-as-you-go costumers). Industry sources indicate that approximately 70% of mobile broadband costumers are pay-as-you-go, where registration of personal details is not compulsory. Therefore, even if the mobile ISPs are able to identify the IP address of the infringer, there may not be a way to match these IP address with a user's name, making legislation ineffective to tackle such users.

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[53] Total number of hours of work by staff is calculated by multiplying the total number of calls (1.5% of 6.5 million) by the average 10 minutes that we assume a call lasts or an e-mail reply takes to write

[54] Total cost is calculated by multiplying the total number of hours by the median labour cost per hour of customer services occupations in ASHE (2008) of £7.75 and an additional 21% of overhead costs.

[55] Total cost is calculated by multiplying the total number of hours derived from sending a second letter (5,000 hours) by the median labour cost per hour of customer services occupations in ASHE (2008) and an additional 21% of overhead costs.

[56] Calculated under the assumption that there are approximately 450 ISP which have fixed costs of £80k each

[57] Cost estimates provided by industry sources

[58] Vodafone, O2, T-Mobile, Orange, Hutchinson 3G

[59] Cost estimates provided by industry sources

Cost to consumers

Under the assumption that ISPs fully pass down to consumers the annual increase in costs, we expect broadband retail prices to increase between 0.2% and 0.6%[60]. Studies on the price elasticity of demand have shown that demand for broadband is not very sensitive to price increases. Nonetheless, we estimate that this cost would have a relatively small but permanent effect of reducing demand for broadband connection between 10,000- 40,000[61]. This would represent additional revenue lost by the ISP industry between £2 and £9 million per annum.

Additionally some consumers, especially those with low income or those that derive a relatively low welfare from creative content, only consume creative content at a price of zero or close to zero[62]. As a result it is likely that the policy will have an impact on equality (i.e. those on the lowest incomes are likely to lose the most). However, it must be noted that the impact will only be to those that were illegally downloading digital content.

These consumers will experience a net welfare loss as a result of the proposed policy option since they will stop consuming creative content altogether. It is not possible to estimate such welfare loss with current data availability, but estimates for the US[63] show that this welfare loss could be twice as large as the benefit derived from reducing the displacement effect to industry revenues.

Cost to right holders

We expect there may be a cost to right holders to identify illegal P2P downloads of copyrighted digital products and further costs were right holders to decide to take forward legal actions. It is not possible at this time to estimate these costs with the information that has been provided to us.

Cost to Government regulators of monitoring and reviewing legislation

There may be additional costs to Ofcom to set up, enforce and monitor the development of the Code of Practice. Current uncertainties around the final design of the Code of Practice prevents us from monetising these costs at this stage.

Table 2. Policy costs

Type	**Description**	**Amount**
One-off	Capital cost to ISPs	£35m
Annual average costs	Cost of notification	£7.5-24.5m
Annual average costs	Cost of running a call centre	£60k
Annual average costs	Cost to consumers	£2-9m
Annual average costs	Capital and operating cost to mobile network operators	£19m
Annual average costs	Operating cost to ISPs	-

[60] According to the OECD, the average monthly broadband retail price in 2007 in the UK was about £20, £240 annually. Broadband Stakeholder Group estimates that the number of UK broadband connections in the same year was of 14.5 million. Following our assumption that annual costs to ISPs increase by £6-£20 million per year and that this cost is fully transferred to consumer prices, broadband retail prices would increase between £0.40 and £1.40 per year. This represents an increase of the annual price between 0.2% and 0.6%.

[61] Calculated by assuming a long term price elasticity of demand of -0.43 as estimated by a study of SPC Network (2008); www.spcnetwork.co.uk/uploads/Broadband_Elasticity_Paper_2008.pdf

[62] For example, a consumer that derives a monetised welfare of £1 from a CD is now able to download it illegally at a cost of zero but would not purchase a legal copy if it had to pay a legal price of £10 (Peitz and Waelborek, 2003: http://papers.ssrn.com/sol3/papers.cfm?abstract_id=466063.

[63] Rob & Waldfogel (2006): http://www.journals.uchicago.edu/doi/abs/10.1086/430809

6. Monitoring and enforcement

Ofcom will be responsible to monitor and enforce the policy. Specifically they will be required to place obligations on ISPs to require them:

- to notify alleged infringers of rights (subject to reasonable levels of proof from rights-holders) that their conduct is unlawful; and
- to collect anonymised information on serious repeat infringers (derived from their notification activities), to be made available to rights-holders together with personal details on receipt of a court order.

If Ofcom is satisfied that the obligations and targeted legal action scheme has proved to be insufficient to dissuade serious infringers, then it will have a power to require ISPs to impose specified technical measures against infringing individuals. In deciding whether to exercise that power, Ofcom will have regard to all its relevant duties (including, for example, its general duties and the Community requirements in sections 3 and 4 of the Communications Act 2003) and any other relevant legal requirements (for example in privacy and data protection legislation). It will also have to be satisfied that the imposition of technical measures by ISPs is objectively justified, proportionate, transparent and does not unduly discriminate against particular persons or particular groups of persons.

Finally Ofcom will be placed under a duty to ensure that there is a code of practice, with which ISPs will be under a legal obligation to comply (and Rights holders to follow if they wish to trigger action under the Code).

The expectation would be for this code to be prepared by an industry self-regulatory body and approved by Ofcom. In the absence of an industry code that Ofcom is able to approve (or if an existing industry code is revoked) Ofcom will be obliged to provide a code itself.

Specific Impact Tests: Checklist

Use the table below to demonstrate how broadly you have considered the potential impacts of your policy options.

Ensure that the results of any tests that impact on the cost-benefit analysis are contained within the main evidence base; other results may be annexed.

Type of testing undertaken	***Results in Evidence Base?***	***Results annexed?***
Competition Assessment	Yes	Yes
Small Firms Impact Test	Yes	Yes
Legal Aid	No	No
Sustainable Development	No	No
Carbon Assessment	No	No
Other Environment	No	No
Health Impact Assessment	No	No
Race Equality	No	No
Disability Equality	No	No
Gender Equality	No	No
Human Rights	No	No
Rural Proofing	No	No

Annexes

Annex 1. Competition assessment

MNOs vs fixed ISPs

MNOs increasingly compete directly with ISPs in the broadband market due to their competitive speeds, large take-up of mobile broadband handsets amongst users, and growing popularity of dongles. The growth of mobile broadband market share over the last 3 years has been substantial, with annual growth rates of approximately 100%[64]. This has had an overall positive impact on competition in the broadband market.

Cost estimates indicate that the impact of legislation could be disproportionately high for MNOs as compared to ISPs, which could place the latter with a competitive advantage. MNOs could be forced to increase prices which could have as a result that the increasingly strong competition in the broadband market could be reduced.

It has been suggested that MNOs could potentially be excluded from such obligation. Reasons for that include not only the disproportionate cost that MNOs would face but also the difficulty of implementing the legislation to MNOs (see Costs section). However, it is likely that such exclusion could also place MNOs in a competitive advantage compared to ISPs, not only because of not having to potentially bear the costs of implementing the legislation but also through the possibility of offering a more competitive product to costumers which could allow unlawful P2P file-sharing without the risk of being prosecuted legally.

Small vs Large ISPs

It has been suggested that ISPs of smaller size may be excluded from the obligation to notify subscribers of their unlawful behaviour due to the higher costs per connection that they would face (i.e. de minimus legislation).

This exemption may place small ISPs in a position of competitive advantage over larger ISPs. ISPs excluded from the legal obligation would be able to offer a lower subscription price to customers than larger ISPs since they wouldn't need to bear the costs of implementing the legislation.

Additionally, smaller ISPs could offer a differentiated product potentially more valued by consumers than larger competitors. Broadband connections of small ISPs (or those ISPs such as mobile operators which could potentially be excluded from the obligation) would allow subscribers that wish to do so to keep on using P2P networks to illegally download digital products with a higher legal security.

These advantages could potentially lead to an artificial displacement of broadband subscriptions from larger ISPs to smaller ISPs. The large number of illegal downloaders in the UK suggests that exempt ISPs could attract a large number of subscribers.

However any significant shift in subscribers to a smaller ISP would have two impacts. First, if sufficient subscribers switched this could lead to the ISP breaching the de minimus threshold and thereby liable to follow the legal obligations with associated costs. Secondly it would have an impact on the volume of traffic over the network (it is generally recognised that the most active P2P file-sharers do take up a large volume of bandwidth). This would have implications for the effective operation and management of the network – and potentially higher costs.

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[64] Ofcom

Finally any ISP gathering significant volumes of unlawful P2P traffic and users would soon be identified. One option is for the obligations to apply to specific ISPs and in such a case an ISP with a predominance of unlawful P2P users would soon have the obligations applied to them.

Annex 2: Small Firms Impact Test

If ISPs have to assume capital costs to automate the process of detecting infringers, these costs would have a disproportionate impact on SMEs in a per unit basis. Approximately 450 ISPs have an average turnover of less than £1 million each. If capital costs are high, these would have a disproportionately high impact on such businesses compared to the impact on the 6 largest ISPs. For example, assuming that fixed costs are £80k per ISP, fixed costs would represent nearly 10% of the turnover for an average SME in the first year of implementation of the legislation. This compares with a nearly negligible effect on larger ISPs.

A de minimus exclusion of ISPs from the obligation is being considered to alleviate this problem, but more information is required in order to make an informed decision.

A complicating factor is the involvement of some very large firms (e.g. Tesco, Royal Mail) who offer broadband services. In terms of overall size, such firms are not SMEs. However the scale of purely broadband operations they offer could be considered small (in terms of subscribers or turnover).

There is also a potential impact on SMEs in the right holders industry. Since the process of identifying infringers falls on right-holders, were the process to involve large fixed costs these costs would disproportionately affect small producers and distributors (e.g. costs of implementing the technology that enables right-holders to detect IP addresses).

If fixed costs to right-holders are high some smaller size firms may not be able in practice to reap the benefits derived from the policy, namely reducing the sales displacement effect. This would place such businesses in a disadvantageous competitive situation with larger right-holders. This is particularly relevant considering the general industry trend of lower distribution costs which has allowed smaller competitors to directly compete with larger businesses (e.g. distribute digital content to a worldwide market).

Annex 3. Other specific impact tests

Other specific impact tests have been considered, including Legal Aid, Sustainable Development, Carbon Assessment, Other Environment, Health Impact Assessment, Race Equality, Disability Equality, Gender Equality, Human Rights and Rural Proofing.

After careful analysis it has been concluded that no significant impact is anticipated in any case.

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