

Submission to the Gowers Review of UK IP Laws

Warner Bros. Entertainment UK

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About Warner Bros. Entertainment UK

Warner Bros. Entertainment UK is the UK division of Warner Bros. Entertainment Inc., a global leader in the creation, production, distribution, licensing and marketing of all forms of entertainment and their related businesses. Warner Bros., a Time Warner company, stands at the forefront of every aspect of the entertainment industry, from feature films to television, home video/DVD, animation, comic books, interactive entertainment and games, product and brand licensing, international cinemas and broadcasting.

In addition to its long-standing position as the industry's pre-eminent creator and distributor of feature films, television programs, animation, video and DVD, Warner Bros. Studios has also become one of the foremost authorities on utilizing licensing and merchandising to grow and reinforce its brands, on pioneering new forms of distribution, and on marshalling its vast creative and business resources to build innovative and exciting consumer propositions. Today, the vast Warner Bros. library, considered one of the most prestigious and prodigious in the world, consists of more than 6,600 feature films, 40,000 television titles and 14,000 animated titles (including over 1,500 classic animated shorts). The library currently consists of films from such distinguished banners as Warner Bros. Pictures, Castle Rock, Warner Independent Pictures, Lorimar Pictures, RKO and classic MGM (pre-1986).

The UK represents one of Warner Bros. Entertainment's largest markets and is therefore critical to the future growth of the company overall. Our commitment to the UK is best illustrated by the scale of our recent investments in the UK, including the highly successful *Harry Potter* franchise, as well as *Batman Begins* and *Charlie & the Chocolate Factory*.

General Overview

Whilst Warner Bros. welcomes the opportunity to respond to a subset of the questions posed, we believe that the current UK framework represents the right balance between the interests of the consumer and the copyright owner. However, the review provides a valuable opportunity for an informed debate on the legislative framework in the context of the perceived challenge posed by digitalisation and new business models.

The film and TV production sector, like other information-based sectors, can best be characterised as an industry with high fixed costs of production and relatively low marginal costs of distribution. This unusual economic structure provides the source of a market failure. In a normal market the retail price of a product is driven by competitive pressure to the marginal cost of supplying that product. Marginal cost pricing is both productively and allocatively efficient in that context. However, where the difference between the fixed production costs and the marginal distribution costs are significant, as they are in the production of information goods, then marginal cost

pricing is not economically efficient. Where marginal costs are zero or close to zero it is unlikely that an investor could expect to recover the significant fixed costs by charging a retail price based on the marginal cost. The result is that, absent public intervention, potential investors face insufficient incentives to invest in the production of knowledge goods and capital investment will move to other markets.

IP laws are an attempt to remedy the market failure by granting investors in knowledge goods certain exclusive rights to exploit their creation in ways which allows the right owner to raise the retail price above marginal costs, for a specific period of time, and to generate a contribution towards the fixed production costs. IP rights are the cornerstone to facilitating, creating, distributing, and monetizing creative works. If one thinks of the media and entertainment industries as built upon creativity, then the industry looks at protection and growth of creativity as resting upon IP protection.

Theft of IP (piracy) has always existed in the film and TV industries, but the transition to digital media poses a new scale of threat to the legitimate content production and distribution industries. Digitalisation has significantly reduced the cost to those engaged in the illegal copying, storage and distribution of copyright protected works, and also permits a near perfect copying of an original work, with subsequent copies of the first copy also being near perfect. That pirates only have to recoup their marginal costs means that the subsequent “competition” from legitimate producers is significantly undermined.

The theft of IP has broader economic implications in the context of its impact on resource allocation within the content production and distribution industries and on consumers of legitimate content. The point is perhaps best made by Professor Richard A. Epstein in his recent report for the US’ National Association of Manufacturers¹:

“Theft, measured in billions of dollars of lost revenue, has the same disastrous consequences for IP as it does for everyone else. Individuals and firms are denied the legitimate return on their labor. They must devote a substantial fraction of their resources to protecting what they have, which leaves less for research, development, and sales. Legitimate consumers must foot the costs of theft, assuming they remain in the market at all.”

That the UK’s legislative framework continues to provide sufficient incentives for investment in content production is important. However, legislation alone is unlikely to be sufficient to underpin incentives, or to provide complete protection against the theft of content. Technical protections enabled by Digital Rights Management (DRM) must also play a complementary role in safeguarding the rights of content producers. However, DRM should not be misrepresented as a means of locking up rights. Rather, DRM technologies enable content producers to invest in innovative business models, including video on demand and music and video download services, which serve consumer demands for ever more control over what content they consume, at what time and over what device. By contributing to the growth in the overall market through the offer of differentiated price and product offerings, DRM

¹ See http://www.nam.org/s_nam/bin.asp?CID=202515&DID=236749&DOC=FILE.PDF

solutions serve to raise consumer welfare. Laws prohibiting the circumvention of technological protection measures therefore promote consumer welfare by enabling content producers to multiply consumer choice while securing the requisite protection in the digital environment.

General Questions

1. How IP is used

(a) To what extent does the term of IP rights at the margin affect investment decisions?

It is difficult to specify the impact on our investment decisions, in the context of new productions, of the term of IP rights, but the duration of the right per se is important. For Warner Bros., the term of copyright clearly affects investment decisions with respect to the restoration, preservation and market re-introduction of older, historical films. For example, Warner Bros. has recently spent significant sums in digitally restoring classic Technicolor films such as *Robin Hood*, *The Wizard of OZ*, *Gone with the Wind*, and *Singin' in the Rain*. A significant part of the economic justification for making this large investment in restoration and preservation rests upon the 20 year extension in the term of copyright protection that was enacted in the United States and in Europe in the late 1990s. This extended term of protection affords companies, like Warner Bros., to earn a return on their investment in the restoration and preservation of such older films.

Such investments yield wider economic and social benefits as they enable us to support business models based on new media distribution. For instance, we can now make these restored classic films available in a fit for format condition for a new generation of viewers to enjoy on DVDs and broadband distribution.

Looking forward, new media distribution platforms offer the potential for additional revenue streams and these new streams will undoubtedly impact investment decisions in so far as they impact overall patterns of revenue generation. For instance, should the so-called long tail philosophy prove sufficiently attractive to support new business models then it may be that the planned cost recovery period for a film or TV product will be extended, enabling greater investment in new production or a real reduction in the retail price for consumers within each format or window.

(b) How well does the UK IP system promote innovation?

The decision of Warner Bros. to invest heavily in the UK is based upon a range of variables, including the availability of craft skills and the suitability of production facilities, but the legislative climate, including the framework governing IP, is also an important factor. That we have invested considerable sums in UK film production in recent years (and have chosen to locate our European headquarters in London), helping to stimulate and support a vibrant industry in the UK, is testimony to our belief that the UK IP system currently provides a supportive and pro-investment framework.

2. How IP is challenged and enforced

(a) Are there specific problems with enforcing the main different forms of IP: patents, copyright, trade marks, and designs?

Whilst the illegal copying and distribution of films, commonly known as film piracy, has existed for many years, the impact of this activity has exploded in recent years. Film piracy entails the theft of intellectual property rights in the form of copyrights and, to a lesser extent, trade marks.

The UK video industry, including Warner Home Video, estimates that in 2005 copyright theft resulted in a loss to that industry of around £800 million (IPSOS, Digital and Physical Piracy in Great Britain, 2005). Those losses stem from both physical piracy (i.e. the manufacture and sale of illegal copies of films on DVDs or DVD-Rs) and internet piracy (i.e. the uploading and downloading of illegal copies of films over the internet, often using file-sharing technologies). However it should be recognised that those two forms of piracy are interlinked, as the makers and sellers of physical pirate copies usually obtain their source material from the internet, where new pirate versions usually appear first.

In the UK physical piracy has undergone a massive increase in the last few years, and is still an enormous threat to legitimate business. In addition, as broadband penetration increases and the movement of large files becomes easier and quicker, so internet piracy is steadily increasing. This has serious implications; today, one person can camcord a movie in a theatre and then upload a digital file to a peer-to-peer network for distribution to an unlimited number of people. Not only is this activity more difficult to detect, but it permits anyone with Internet access and a camcorder or DVD ripping software to become a source of widespread and commercially damaging copyright infringement.

Piracy does not just affect the video industry. The impact of piracy is felt by all sectors of the film industry, and related industries such as film producers, theatrical exhibitors and video rental and retail businesses. In addition, counterfeiting adversely impacts revenues from brand licensing on consumer products.

Against this background Warner Bros. relies on enforcement of its IP rights to combat piracy and protect its business, both in its own name and (more commonly) through industry associations. However there are indeed specific problems with enforcing those rights. In particular, Warner Bros. endorses the following problems relevant to it as identified in the submission by the Alliance Against IP Theft.

- Inadequate resources for trading standards
- Difficulty in recovering proceeds of crime and damages
- Inability to close down markets which persistently allow the sale of fake goods
- Trading standards not having the duty to enforce copyright legislation
- Theft of copyright-protected material in the workplace
- Lack of presumptions of copyright ownership in criminal matters

Warner Bros. does not intend to repeat the detailed comments relating to these issues in the Alliance submission, but we agree with those comments.

In addition there are some specific legal barriers that can be corrected through the implementation of the Directive On The Enforcement Of Intellectual Property Rights (2004/48/EC) (the Enforcement Directive). Again, Warner Bros. endorses the views of the Alliance, as set out in its submission to the Patent Office Consultation Paper that changes are required in relation to the following issues:

- Article 4: Persons entitled to apply for the application of measures, procedures and remedies
- Article 5: Presumption of authorship or ownership
- Article 7: Civil Search and Seizure
- Article 10: Corrective measures
- Article 13: Damages

Warner Bros. does not intend to repeat the detailed comments relating to these issues in the Alliance submission, but we agree with those comments.

(b) Are there barriers to challenging infringement and enforcing your IP rights on grounds of cost? What drives these costs?

The sheer scale of film piracy, both worldwide and in the UK, and the large number of individuals involved in infringing copyright mean that there are practical challenges to enforcing IP rights. In addition, film piracy is so lucrative that it is an attractive source of revenue for organised criminal gangs who are adept at hiding their criminal activities, which only increases the cost of investigating such piracy. Warner Bros. and the other members of the film industry's anti-piracy body, the Federation Against Copyright Theft (FACT), have significantly increased the funding for FACT over the last couple of years to meet the growing piracy threat, but the scale of the problem continues to present a barrier in terms of the costs required to challenging that problem.

This is particularly so in the case of internet piracy, which can and does involve many thousands of individuals engaging in illegal activity, often in a large number of different countries.

(c) To what extent does your organisation make use of other methods than litigation to resolve IP infringement cases, for example the Patent Office opinion service, mediation services, Alternative Dispute Resolution, or the Copyright Tribunal?

In the experience of Warner Bros., such alternative methods are not suitable for resolving film piracy cases. The methods that are suitable are either action by the appropriate law enforcement authority (i.e. Trading Standards, HM Customs or the police) or civil litigation.

(e) What are the principal barriers to efficient and successful challenge and enforcement internationally?

The principal barriers are:

- Failure to accede to, or incomplete or inadequate implementation of international copyright treaties and regional (i.e. EU Directives) legislation.
- Cost.
- Local political issues.
- Perception that copyright infringement and piracy are “victimless” and relatively unimportant infractions of the law.
- Lack of trained professionals (including law enforcement and judges) in the area of copyright enforcement.

Specific Questions

2. Copyright exceptions - fair use / fair dealing

Background: There are a number of exceptions to copyright that allow limited use of copyright works without the permission of the copyright holder.

(a) What are your views on the current exceptions in copyright law?

The current exceptions provided for under the Copyright, Designs and Patents Act 1988 (as amended) are satisfactory and do not require amendment.

(b) Could more be done to clarify the various exceptions?

No.

(c) Are there other areas where copyright exceptions should apply?

No.

(d) Are the current exceptions adequate or in need of updating to reflect technological change? For example copyright law in the UK does not currently have a private “fair use” exception. Such an exception might allow individuals to copy music CDs onto their PC and MP3 player for their personal use. Should UK law include a statutory exception for “fair use”?

Warner Bros. does not believe that there is any justification for introducing a “fair use” exception in the UK and that the current framework represents a fair and reasonable balance between the interests of legitimate consumers and rights owners. While we cannot comment on the specific examples regarding music works (save to say that it is our observation that the vast majority of such content providers do not use technological means to prohibit the making of a limited number of copies for the purposes of enjoying music on different devices), we believe that content producers are sufficiently incentivised to meet consumer demand for greater flexibility without the need for additional intervention. We are working to provide a managed copy facility for consumers with regard to audio visual products, in addition to other differentiated product offerings. In commercial licensing deals that we have already struck we allow multiple copies to be made both to the PC and to mobile devices. We also include the ability for consumers to gain access to digital backups of the material for instances where their PC or authorized device may fail or be corrupted.

In addition, the problem with allowing a fair use exception for private copying in the digital environment is that each digital copy that is permitted to be made in the clear can effectively become a master that can be the source of unlimited generations of perfect copies. So the risks involved for infringement in permitting a private copy exception is far greater in the digital world than in the analogue world.

(e) How would you see content owners being compensated for such use?

Our view is that a private copying regime is not warranted in UK law, and so we make no comment on how such a regime may be administered to compensate content owners. However, within an industry provided managed copy scheme (such as that described above), the content owners are able to cover their costs via the revenues from a variety of consumer propositions. For instance, the consumer can decide which offering and price point is right for them based upon the content format and user device e.g. VOD, electronic sell thought (EST), EST/DVD bundle.

3. Copyright – digital rights management

Background: Increasingly digital media content is distributed with digital rights management (DRM) technologies that can enable rights-holders to track usage and prevent unlicensed copying by technological means. However concerns have been raised about interoperability and that such technologies may impair the content consumer's legal rights. For example they may be unable to take into account exceptions to copyright, the ultimate expiry of copyright term, or the future evolution of technology. They may therefore undermine legitimate rights to access digital content, now and in the future. (NB: We are aware of all formal submissions that have been made to the All Party Parliamentary Internet Group on this issue.)

(a) Do you have a view on how the use of digital rights management technologies should be regulated?

DRM provides both content protection and the ability to manage and execute offers made to consumers. DRM has been described as “*a systematic approach to copyright protection for digital media*”², though this does not quite explain what DRM is, or how it might evolve in the future. From a technical perspective DRM can encompass “*the description, identification, trading, protecting, monitoring and tracking of all forms of usages over both tangible and intangible assets.*”³ More simply, DRM is a suite of solutions that allow for the technical identification and protection of intellectual property (to date this has focussed primarily on the prevention of unauthorised copying of digital works).

DRM technologies employ a number of discrete tools, which may be combined in a variety of ways in order to provide the kinds of functionality described above. The primary tools are briefly described in Table 1.

² See the IT encyclopaedia web site, www.whatis.com.

³ See Iannella, R. (2001), “Digital Rights Management (DRM) Architectures”, D-Lib Magazine, Vol. 7.

Table 1. Some Common DRM Tools

Tool	Purpose
Secure containers	Restricts access to devices with authorisation
Rights expression languages	Establishes rights associated with the content
Content description	Unique description of content for search purposes
User ID	Allows for the access by authorized users
Authentication	Determines if a device is licensed and will treat content appropriately
Fingerprinting/Watermarking	Complementary tools allowing the originator to forensically trace compromised content or to more securely embed information into active picture area of content
Payment	Billing and payment mechanism

The precise choice of tools in any DRM solution will depend on the purpose of the DRM and the nature of the content that is to be protected. Tools used to protect documents differ from those used to protect a Hollywood movie. For instance, Adobe Acrobat is software that utilises secure containers to set permissions on how protected documents can be used and distributed. Copy Generation Management System (CGMS) uses a combination of bit settings to indicate whether content may be copied or copied further, as do copy management settings for DAT and minidisk players which are managed by the Serial Copy Management System (SCMS).

DRMs are commonly misunderstood. They are not designed and employed to “lock away” content or to prevent consumer choice. Quite the contrary. We at Warner Bros. use DRM technology in order to increase consumer choice and to offer our content to consumers in a greater number of distribution channels and at a greater variety of price points. Movie content, for example, is traditionally released via a series of time-dependent windows. This is an economically and commercially efficient business model due to the need to recoup high fixed production costs and a legitimate exercise of the holder of the intellectual property rights. The implementation of DRM solutions may potentially support more refined forms of price differentiation. DRM enables service providers to increase consumer choice by offering a variety options at different price points. Consumers could be offered a menu of pricing/product combinations which more accurately reflect their effective demand than is than is the case with windowing. Consumers, rather than content owners may be able to dictate when and how they consume the content. For example, should a consumer wish to watch a film only once then DRM may enable that consumer to pay less to download the film than another consumer who wants to watch the film many times. A consumer wanting to watch a film many times may be charged less than a consumer who wants to burn the film to a DVD.

Where such price differentiation expands the market, economists point out that it almost always leads to an increase in economic welfare. DRMs help to make more, not less content available to the public. For example, the DVD is an encrypted, DRM protected home video format. Without DRM, film studios would have been unwilling to release their films on this digital format. But because of DRM, a vast number of movie titles are now available to the public in this format that delivers not only superior visual and audio quality, but also multiple language tracks, subtitles, bonus

features, etc. To provide some evidence of the massive growth in the availability of movie content in recent years, the British Video Association (BVA) reports that approximately 5,600 titles were released in the retail sector during 1996. For 2006, the BVA expects to report that 8,679 titles were released on DVD, increase of more than 54% over the ten year period.

However, like any technology DRM solutions are not immune from attacks by those looking to undermine the technical protections. As such, it is vital to enact and enforce robust anti-circumvention legal protections covering DRM's that control access to digital works, as well as those that control copying. Any exceptions to such protection should be carefully considered in light of the substantial potential for harm in the event that a protection circumvented for one use may be digitally distributed for any number of potential uses.

In general, DRMs do not need to be regulated. The marketplace is well equipped to ensure that DRMs do not operate in an overly restrictive manner. If consumers are dissatisfied with works protected by a certain DRM technology on a particular format, then they will simply not purchase such works on that format. Competition exists between windows and formats to the extent that film and TV content is generally available in multiple channels of distribution and in different formats. That consumers can "vote with their feet" place sufficient competitive pressure on content producers to ensure that consumer demand is met.

Warner Bros. does not believe that there is a case for legislative intervention to ensure interoperability of DRM solutions. Rather, we believe that this is an issue best left to the market to settle. Intervention at this nascent stage in the development of a complex technology, supporting even more complex business models, carries significant risks of undermining the very benefits of DRM outlined above. We believe that content producers and consumers have a shared interest in content being available across as many legitimate platforms as the market will sustain. Likewise, we support the growth in legitimate value added benefits, such as being able to forward content to friends or transfer content between devices. We believe that market forces will therefore deliver interoperability and that, in this context, policy makers should support the work of standardisation bodies rather than seek to introduce legislation.

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