

# 2013 Review of the Resale Royalty Scheme

Submission: John R Walker

This submission addresses three aspects of the Artist Resale Royalty [ARR] Scheme and the review process itself, all of which are intrinsically problematic. Recommendations are attached to each issue.

Outline of issues:

## **Issue 1: Inadequacy of information supplied by OFTA's Discussion Paper**

The Discussion Paper does not contain critical information needed to evaluate the scheme, despite the fact that OFTA did supply some of this information in answer to Senator Humphries's detailed questions on notice (in Hansard, see attached) in late February of this year. In particular, the Discussion Paper does not state that the average transaction cost to CAL is \$30 per transaction. There are also significant discrepancies in the details of the figures between the answers supplied to the questions on notice and those supplied in the Discussion Paper. A proper evaluation of the scheme needs accurate, reliable and detailed information.

## **Issue 2: adverse affects on artists' market competitiveness & substitution issues**

ARR Scheme is a restriction on the resale of moveable objects. It is much more a Goods and Chattels Law than an individual right. ARR is intrinsically a restriction on artists' terms of trade that raises real and harmful market distortions and substitution issues for many artists affected by the scheme. It is definitely not an encouragement to buying art in the first instance.

This is no less than *Lord Coke* on goods and chattels type restraints of resale:

“... it is against Trade and Traffi[c], and bargaining and contracting betwee[n] man and man: and it is within the reason of our Author that it should oust him of all power given to him...”

There is no way that a restriction of artists' terms of trade could be construed as an inalienable individual economic right of artists.

## **Issue 3: viability of the scheme as it is currently structured.**

By cross-referencing the figures supplied to Senator Humphries and the figures in the Discussion Paper, it is very clear that the scheme, as it is currently designed, has a reverse economies of scale problem. If the scheme grows, costs will expand at a much greater rate than its net income. More than half of the individual payments of the scheme are well below the current economic-to-collect-and-deliver threshold and this is

intrinsic to the scheme's current design. Low value resales will always more common than large resales and the costs of delivering small payments will always be much higher than large, one-off payments to well-known and easily traceable artists (and their estates).

### **Expansion on Issue 1:**

The Discussion Paper does not disclose the critical fact that the average transaction cost, for CAL, is \$30; \$30 is the collection fee due on the \$300 royalty payment raised on a \$6,000 resale. The current minimum resale threshold is \$1,000.

The Discussion Paper does not provide nearly enough information on the breakup by total value of the individual royalty payments. It does not provide the total value of royalty payments of \$100 or less, and it does not provide the total value of royalty payments of \$300 or less (to \$101). The current economic-to-collect-and-deliver royalty payment is \$300. The total number of payments below \$300 is critical for the evaluation of exactly what percentage of the scheme is operating at below an economic-to-collect-and-deliver threshold.

The Discussion Paper does not explicitly state the median value for royalty payments. It is apparent from the Discussion Paper and the answers to the questions on notice that the median payment value is just above \$100. This implies that 50% of the individual payments of the current scheme are well below the economic-to-collect-and-deliver threshold.

The Discussion Paper also does not provide the total value of the top 277 royalties delivered; that is, royalties worth more than \$501 each. It is likely that this top 4% of royalty payments will account for much of total value of royalties collected. ARR has wide-ranging effects, is of doubtful viability and its largest benefits in the long run must go to artists who have sold a lot art in the first instance. The 'why' of this scheme is questionable.

*The gaps in, and inadequacies of, the information contained in the Discussion Paper raise real concerns about the OFTA's commitment to a transparent and dispassionate evaluation of the scheme. Much critical information needed to undertake a proper evaluation has not been supplied in the Discussion Paper.*

### **RECOMMENDATIONS Issue 1:**

**That OFTA provide the following more detailed information to allow for proper analysis:**

- The OFTA should supply the total value of the bottom 2,000 royalty collections; the total value of the next 2,000 group of royalty collections; the total value of

- the top value group of 2,000 royalty collections; and finally the value of the top 800 royalty payments.
- OFTA should also supply the total value of the 277 royalty payments (above \$501 to over \$50,001).
  - What percentage of these top value payments have gone to indigenous artists?
  - OFTA should supply the total value of royalty payments that have not been paid through CAL.

### **Expansion on Issue 2:**

ARR adversely affects the market competitiveness of artists that are affected by this scheme. The scheme is fundamentally a restriction of artists' terms of trade. There will always be plenty of collectible art-like objects that are not affected by this ARR scheme. Because ARR is a much larger and punitive treatment of the eventual resale of artworks than it at first appears to be, it is much more of a disincentive to buying art in the first instance (than it first appears to be).

Because ARR makes no allowance for costs or losses it is anti-progressive and punitive in its effects: the smaller the profit on the eventual resale of an artwork, the larger the percentage of that profit that is taken by ARR and it also applies to losses on resale. For example:

- An artwork is first purchased for \$10,000. It is eventually resold for \$11,000. ARR @ 5% on \$11,000 is \$550; that is, 55% of the \$1000 gross profit on that resale.
- An artwork is first purchased for \$20,000. It is eventually resold for \$21,000. ARR @ 5% on \$21,000 is \$1050; that is, more than 100% of the gross \$1000 profit on that resale.
- An artwork is first purchased for \$10,000. It is eventually resold at a loss for \$9,000. The ARR on \$9,000 @ 5% is \$450, increasing the total loss on that resale to \$1,450.

ARR is definitely not an encouragement to the first purchase of artworks that will eventually be affected by a resale royalty. ARR intrinsically creates market distortion and substitution problems.

There is evidence in the Discussion Paper that ARR is already having an impact on the numbers of artworks being resold that are affected by the scheme. While the collection figures in the Discussion Paper Table 1 are cumulative, when disaggregated on an annual basis, they indicate a decline in the number of royalties generated: from 2,793 in 2011 to 2,546 in 2012 and in the half year to date, 1,059. These figures are evidence that buyers are avoiding artworks affected by the resale royalty. While the general state

of the economy has had an obvious impact on the sales of art, the sales of the art that is most directly affected by ARR – Indigenous art – have been much more affected than an economic downturn alone would explain. It beggars belief that government policy in this area has not had some adverse affects on buyer behaviour.

For many artists ARR is harmful. It should be possible for such artists to opt out altogether. During questioning of the OFTA representatives by the House of Representatives Standing Committee February 2009, the Chair, the Hon. Jenny George asked the 1<sup>st</sup> Assistant Secretary, Ms Lyn Bean about artists who wished to exercise the right to permanently not collect the royalty. Ms Bean answered that this should be administratively possible under the current Act:

**CHAIR**—We have had one submission that an artist may choose to exercise the right never to collect a royalty.

**Ms Bean**—In that case I would expect the artist to notify the collecting society. That would be the sensible thing to do if you did not want to go near it.

**CHAIR**—But my understanding is that the legislation as currently constructed may not adequately allow for that option to be exercised.

**Ms Bean**—We are confident that it does because there is a choice in the legislation. Anything else around that is essentially an issue of process and I think does not need to be in the legislation. ...But you do not need to legislate for that—it is up to them—and discussions as part of the tender process should include straightforward administrative systems. [underlining is mine]

ARR is a restriction of artists' terms of trade. This should never be compulsory or even semi-compulsory (as in case-by-case Opt-out). Artists are diverse in their situations and needs. A one-size-fits-all approach will always cause more harm than good.

RECOMMENDATION Issue 2:

**It is vital that the scheme be modified to a strictly voluntary OPT – IN scheme. Or, at the very least, that artists like myself be free to permanently OPT – OUT altogether.**

### **Expansion on Issue 3:**

The long term viability of the ARR Scheme in its current design is doubtful. It will require public subsidy into the foreseeable future.

The following is my analysis of the more detailed figures supplied in response to Senator Humphries' questions on notice. The figures contained in the Discussion Paper do not have sufficient precision to allow a proper analysis of the distribution pattern of the scheme.

Of the approximately 5,000 royalty payments to December 2012:

- the bottom 2,000 royalty payments totalled \$115,379 - an average value of \$55 each.
- the middle, approximately 2,400 royalty payments, had a total value of \$396,964 - an average value of about \$164 each.
- And the top 600 royalty payments had a total value of \$296,772 - an average value of \$495 each.
- The average transaction cost of the scheme is given as \$30 which equates to a transaction levy (@%10) on a \$300 royalty payment.

Most of the scheme's transactions are well below the current economic-to-collect-and-distribute threshold. Many of the royalty payments to December 2012 (2,000 or 40%) were of an average value of just \$55 each and it is clear that the median value for individual royalty payments is close to \$100. Therefore about half of the scheme's transactions are generating transaction fees that are *one third or less* of the average transaction cost of \$30. Of the top half of individual royalty payments, many would be between \$150 to \$300 each. Therefore many of the scheme's remaining transactions are generating transaction fees that *at best* breakeven with the average transaction cost of \$30. Most of the work being done by the scheme is not economically sustainable without some form of subsidy.

The collection fee structure of the ARR scheme is not cost based. Rather, it is a large cross-subsidy levy. Currently the scheme charges just \$5 to deliver a \$50 royalty payment but then charges \$1,000 to deliver a \$10,000 royalty payment. In Australia, for good constitutional and legislative reasons this cross-subsidy is not compulsory for artist right-holders, therefore it is unlikely that many large royalty payments will ever be paid through CAL when it is so much cheaper to simply transfer the money directly to the artist's bank account. Most of the current collection work is uneconomic; the scheme can only become self-supporting if the very large profits generated by massively over-charging on the delivery of large royalty payments somehow become sufficient to underwrite the costs of the entire scheme. This was intrinsic to the design of ARR as it was lobbied for.

The design of the scheme also ignored the fact that many artists, myself included, regard ARR as fundamentally harmful to young and unestablished artists and damaging to the market in which we are trying to make living. I simply want nothing to do with it at all, ever.

#### RECOMMENDATIONS Issue 3:

1. The current collection threshold is way below an economically justifiable level. It is creating very large net costs to right-holders who wish to participate in the scheme. The figures supplied to Senator Humphries indicate that the bottom 2,000 royalty payments were only worth \$115,000 in total; that is about 12% of all the money collected (as of

December 2012) whilst constituting more than 35% of the work done by the scheme. **Raising the threshold to a much more economic-to-collect-and-distribute amount is vital if the scheme is to have any chance of becoming self-sustaining over time.**

2. The requirement that CAL collect royalties for artists who are not registered with CAL simply increases the costs for those who are registered with CAL, for no good reason. Artists who are not, or do not want to be, registered with CAL will always be more costly to find, and why should payments to artists who are registered be wasted upon trying to find those who have chosen not to register. **Modifying the scheme to a strictly voluntary OPT- IN scheme is also needed to reign in excessive costs.** The Australian Law Reform Commission has recently released a discussion paper on copyright issues in the digital age and I quote:

*'the ALRC paper (§6.3, when speaking of statutory licensing schemes) acknowledges that "voluntary licences—whether direct or collective—are less prescriptive, more efficient and better suited to a digital age".'*

I heartily agree with this recommendation.

3. The current flat 10% fee structure is a big disincentive to using CAL's services to deliver large royalty payments. **The scheme should be amended so that artists who wish to participate in collective management by CAL should have the right to negotiate collection fee structures that are more related to actual costs than the current flat 10% levy.** If the ARR's current 'fee-for-service' structure was charged by a bank, it would be illegal.

## CONCLUSION

In his 1995 report to the Australian government, renowned IP lawyer Shane Simpson analysed the merits of statutory, compulsory collective, management of copyright (and of 'neighbouring rights') versus the merits of voluntary collective management. I quote:

*"experience shows that statutory licences drafted without appropriate industry consultation are often unworkable and voluntary licences are required to replace them."*

While well-intentioned, ARR was introduced without proper wide consultation – especially with individual artists directly involved in the making and selling of their art, their representative galleries and their collectors. Further, the legislation was also brought in without a proper Regulatory Impact Statement [RIS] as required by the government's own Office of Best Practice Regulation. The result has been pretty much in line with Shane Simpson's historical knowledge.

ARR creates significant market distortion and substitution issues that are harmful to many of the artists affected by this legislation. This is a predictable problem. If an RIS had been done properly and prior to bringing in the legislation, it is unlikely that an ARR scheme that was in any way compulsory for artists would have ever been enacted.

There has never been a coherent 'WHY' for ARR. At various times it has been promoted as a superannuation scheme, an important individual right that is compulsory, a scheme to generate 'an appropriate level of income' for its administration and as a 'much needed', so-called regulation of the art market. The 'WHY' of this scheme is an incoherent mess. The reality of art resales by value is that in the long run about 80% of all the money will always go to about 20 best-selling, often dead artists. The costs of ARR will always fall upon younger, more vulnerable artists because it will inevitably cause a reduction in net demand for art at the primary market level and also reinforce risk-aversion amongst buyers. A healthy resale market is intimately linked to the health of the primary sales market.

The scheme has been implemented and would be difficult to undo. The best that can be done, in the circumstances, would be to modify it into a true individual right that is voluntary and has a realistic collection threshold – at the very least \$3,000 or more.

Attachment:

Hansard:

SENATE QUESTION  
Resale Royalty Scheme  
Question No. 2677

## RECOMMENDATIONS Summary

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- What percentage of these top value payments have gone to indigenous artists?
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**It is vital that the scheme be modified to a strictly voluntary OPT – IN scheme.**

**Modifying the scheme to a strictly voluntary OPT- IN scheme is also needed to reign in excessive costs.**

**Raising the threshold to a much more economic-to-collect-and-distribute amount is vital if the scheme is to have any chance of becoming self-sustaining over time.**

**The scheme should be amended so that artists who wish to participate in collective management by CAL should have the right to negotiate collection fee structures that are more related to actual costs than the current flat 10% levy.**