Dear Secretary

Submission to Senate Select Committee on the Free Trade Agreement between Australia and the United States of America

This is a submission in respect of the Australia-United States of America Free Trade Agreement, agreed at Washington on 8 February 2004, due to be signed after 13 May 2004 (FTA) and the current reference of the Senate Select Committee on the Free Trade Agreement between Australia and the United States of America in respect of that Agreement.

Background

My comments relate solely to the creation and expansion of legislative monopolies effected by the provisions of Chapter 17 of the FTA. These comments are the result of concerns expressed to me by members of the open source community and the result of my own analysis of the Chapter. Notes marked in square brackets [] are at the end of this submission.

About Open Source

Open source is a new model for software development which makes creative use of the copyright monopoly to drive innovation while lowering development costs and therefore costs to consumers. It has resulted in substantial cost savings to a number of countries. In Thailand, it has brought a previously unheard of price discipline to that market, with the price for operating and application systems bundles dropping on the order of 85% [1]

Open source effects its success through creating a free market for software. The underlying economics is that substantial components of the end price to consumers are transaction and compliance costs. By using innovative licensing techniques open source software not only permits drastic reductions in pricing to end users, it also permits expenditure on software to be capital expenditure, so all payments produce lasting value. At present, the vast majority of software expenditure is in the nature of rents - with customers never owning what they pay for. In the long run, open source promises to reverse the current deficit run by Australia in relation software purchasing and even to convert that money spent on importing software products into money received for exporting software services.

Concerns

The following provisions of the FTA threaten to seriously damage the open source market in Australia:

(a) anti-circumvention provisions

These are prohibitions on accessing data which has been protected by a technological measure. The explicit purpose of these provisions is to prohibit data interoperability. If open source vendors are not permitted to implement data interoperability, they will face substantial barriers to entry in many important submarkets [2]. In essence, a vendor will be locked out of competition merely because the current incumbent uses a protected format for customers to store

their data in. These provisions unreasonably exacerbate network effects [3] in relation to computer software. The FTA includes exceptions for the "interoperability between computer programs" however these exceptions do not address the issue of reproducing data formats and are not responsive to the issue of interoperability between a single computer program and a set of data. It is important that a data interoperability exception be included in this provision.

These prohibitions were initially created to protect a small minority of content producers from competition from new technologies, particularly in respect of audio and video content. However these provisions have already been subject of much broader implementation in the United States. In particular they have been used to inappropriately attempt to suppress competition in respect of printer cartridges and garage doors [4]. Even pressing the shift key can be a breach of the US version of these laws [5]. They can be used to anti-competitive effect on any article to which a computer chip can be attached - and there is every reason to suspect that if this category does not already encompass all manufactures, it will do so in the not too distant future.

While they have been characterised as applying to prevent unauthorised copying of music, it would be a grave mistake to think they will be restricted to this area in the future. The anti-circumvention provisions are a legislative imprimatur to the reduction of competition across the whole breadth of the economy. No analysis of the economic impacts of the FTA that I am aware of takes into account this extensive anti-competitive effect. At its worst it will shave percentage points off Australia's GDP.

(b) patent provisions

The patent provisions inappropriately expand the rights granted to patentees and inappropriately restrict the circumstances in which licences may be compulsorily acquired. Further, it will do so in a way which is manifestly inferior to and with more cost to the community than the existing alternatives. In particular, open source software effects the disclosure of inventions without the requirement for the grant of state sanctioned monopolies. In other words, open source gives the benefits of a patent system for software without the high social costs (as a result of the absolute monopolies effected by patent law) that come with it. However patenting of software inventions permits the absolute foreclosure of open source implementations. In the United States software patents are issuing at an alarming rate - tens of thousands per year. With the life of a patent being two decades, any SME who wishes to compete in the software area has an impossible compliance task ahead of t hem. These compliance costs are bad enough for SMEs operating under the old model. The legislative approach is in direct contradiction to the approach of lowered transaction costs which underpins the new software development model. It acts as an explicit preference for the old model.

The worst thing about these provisions is that independent invention is no defence to a patent. Historically, SMEs in the software market have been able to meet their compliance requirements by adopting cheaply implemented development processes - eg clean room environments, where all material is created independently by the SME. These processes permitted an SME total peace of mind (from copyright claims). Expanded patent protection will render these processes useless because this independent invention is not a defence. Instead,

they will be forced to conduct expensive patent searches which do not assure them peace of mind, as patent searches are not a perfect science. These compliance costs must be incurred even where the work is entirely non-infringing.

(c) Enforcement provisions.

The enforcement provisions fail most tests of reasonableness in that, in civil cases, they consistently require the payment of damages in excess of the damage actually suffered by a plaintiff. This means that monopoly infringements must be elevated above other commercial risks to be considered by a business decision maker.

The enforcement provisions also include definitions of "wilful infringements on a commercial scale" which clearly encompass non-commercial infringements. In particular, infringements for which there is no "direct or indirect financial benefit" to the infringer can be considered to be on a "commercial scale", exposing the citizen to subsantially increased liability.

Comments on Underlying Basis for Chapter 17

Traditional Justifications no longer valid

The copyright monopoly has covered computer software for less than 20 years. In that time the market has seen the emergence of serial monopolies, consolidation and a long term decline in competition in any given product area. The only development model which appears to be introducing competition and reinvigorating SME participation is open source.[6]

The underlying philosophy of open source is that a free market for software development through collaboration produces better results more cheaply than the operation of centrally controlled economies (at a product level) backed by government mandated monopolies. This poses direct challenges to the whole theory of government monpolies in this area. According to the theories that are used to justify Chapter 17, open source, like the bumblebee, cannot fly. The fact that open source not only flies but soars means that traditional justifications for Chapter 17 must be reevaluated. At the very least they should not be relied upon by parliament now at such a critical time and in a manner which will entrench old development models and lock out competition from innovative models such as open source.

Unrelated to freedom of trade

The most widespread implementation of the anticircumvention provisions in existing law is in relation to region coding on DVDs, computer games and computer software. The express purposes of region coding is to restrict the supply of these materials to Australian consumers and to charge higher prices to Australian consumers than to consumers in other markets. The provisions will have the direct effect of preventing Australians (region 4) from buying US (Region 1) DVDs. These purposes are in direct contradiction to the objects of the FTA.

Unreal approach

If enforced today, Chapter 17 of the FTA would make a criminal out of everyone who played a DVD (other than a zone 4 DVD) and out of everyone who has an mp3 player (as there are no legitimate ways to acquire an mp3 in Australia - unless of course, that person only plays out-of-copyright material). The complete disconnection between reality and the approach to policy evidenced by Chapter 17 is disturbing.

Unnecessary
"It has not been demonstrated, in any meaningful sense, that the objective of the Digital Agenda Act to provide a practical enforcement regime has not been met." Paragraph 1.6 Digital Agenda Review Report and Recommendations, Phillips Fox, Attorney General's Department dated January 2004, released 28 April 2004. A number of the provisions in the FTA run directly contrary to the proposals in this report (such as temporary copying and anticircumvention exceptions).

Additional comments
Presumptions as to copyright

Chapter 17 includes a provision which effectively requires a defendant to disprove a plaintiff's right to bring an action rather than having the plaintiff prove it (through presumptions as to the subsistence of copyright and as to who holds that copyright). This is broadly consistent with a recommendation of the House of Representatives Standing Committee on Legal and Constitutional Affairs (cracking down on copycats report). The justification for this provision appears to be that, because a plaintiff has trouble proving that what they are suing on is theirs, the onus ought to be placed on the defendant to disprove a plaintiff's holding. This is remarkable, and poor, policy.

Conclusion

It is very concerning that the FTA seeks to entrench ways of doing things which are fast becoming outdated. They increase compliance costs and push those costs onto smaller and smaller enterprises. Historically market activity was primarily conducted by large organisations, which permitted the aggregation of search and compliance costs. More recently there has been a higher level of disaggregation and community participation than has been evident in the past. We are in a state of transition at the moment and now is exactly the wrong time to be entrenching particular ways of doing things, especially where they are likely to be inappropriate to new modes of production. Chapter 17 does not include provisions to change the terms to reflect (eg) agreements at the WTO, should an international body arrive at a different way of doling out monopolies which leads to better market outcomes but which are inconsistent with the provisions of Chapter 17.

Open source methodologies have scored substantial victories over the past 18 months and are increasingly being adopted by countries from Europe, to SE Asia to South America who are seeking to jump start their software industries. While I do not believe that the Chapter 17 provisions will have an immediate impact on open source, I do strongly believe that the medium to long term outlook is extremely concerning. In the worst case scenarios these provisions have the potential to literally shut down open source development in

Australia, especially among SMEs. It is extremely important for Australia to preserve its policy making flexibility in these areas.

Yours faithfully

Brendan Scott

Brendan is a lawyer with over 10 years of practical experience in the areas of information and communications technology law. He runs a practice in Sydney called Open Source Law and is an active participant in the open source community within Australia. He has extensive experience working for the private and public sectors and for vendors and customers of ICT and has worked on substantial transactions in this area.

Notes:
[1] http://www.infoworld.com/article/03/05/23/HNthailinux_1.html, http://news.com.com/2100-1012_3-1019067.html
[2] These arguments apply equally to non open source vendors. The effect on competition is generally debilitating. [3] A network effect occurs where the size of a participant's market share entrenches their market power. For example, new telecommunications entrants would have great trouble getting subscribers if the existing incumbents did not interconnect with them because any subscriber to the new entrant's system would not be able to call (or receive calls from) anyone on the incumbent's network. [4] see:
http://www.wired.com/news/technology/0,1282,60383,00.html?tw=wn_story_related
http://news.com.com/2100-1028-990501.html
(Apparently each of these cases have had adverse, but not ultimate, findings against the plaintiffs.) [5] See: "Under the law, it is illegal to bypass any technology measure in place that protects copyright material -- perhaps even by pressing the Shift key." http://www.wired.com/news/digiwood/0,1412,60780,00.html. The paper is here: http://www.cs.princeton.edu/~jhalderm/cd3/
[6] see, for sample news reports from the last two months:

Is Microsoft finally about to face real competition in desktop-computer software?
http://www.economist.com/business/displayStory.cfm?story_id=2594309

Brazil's left-leaning federal government is set to adopt free software on a big scale in an effort to save taxpayers billions of dollars and increase independence from multinational suppliers such as Microsoft.
http://news.ft.com/servlet/ContentServer?pagename=FT.com/StoryFT/FullStory&c=StoryFT&cid=1079420520379

According to to reports from London, one of Microsoft's leading engineers is very happy to see Linux challenging Microsoft on the desktop. It will merely sharpen Microsoft's game, in his view.
http://linuxworld.com/story/44578.htm

Could it be that Microsoft's core business, the Windows operating system on desktops and laptops, is really under threat from Linux?
http://www.electricnews.net/ffocus.html?code=9407565

Linux, having established itself as a worthy rival to Microsoft in the server market, is maturing on the desktop as well. It's much

simpler to use. It can perform most of the basic tasks of a Windows-based system. It's also being backed by the likes of IBM, Hewlett-Packard and Sun Microsystems, ultimately making customers more comfortable with the technology.
http://www.thestar.com/NASApp/cs/ContentServer?pagename=thestar/Layout/Article_Type1&c=Article&cid=1081681264496&call_pageid=968350072197&col=969048863851

Officials from China, Japan and South Korea are to meet in Beijing today to map out plans to promote the Linux computer-operating system and other ''open-source'' software as alternatives to the products of the US software giant Microsoft.
http://www.miami.com/mld/miamiherald/business/international/8343362.htm

The Linux market has grown tremendously as a result of support from Hewlett-Packard, IBM and Oracle, resulting in predictions that it will soon replace other operating systems, particularly Unix.
http://www.itweb.co.za/sections/software/2004/0404051037.asp??O=FPQQ

Lower acquisition costs, lower total cost of ownership and greater flexibility in choosing hardware and software are the top reasons companies are deploying open source software, according to a recent survey.
http://www.computerworld.com.au/index.php?id=600985259&fp=16&fpid=0

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