



**IFF Research**

# Research Report Impact of UK Copyright Laws on Digital Technology SMEs

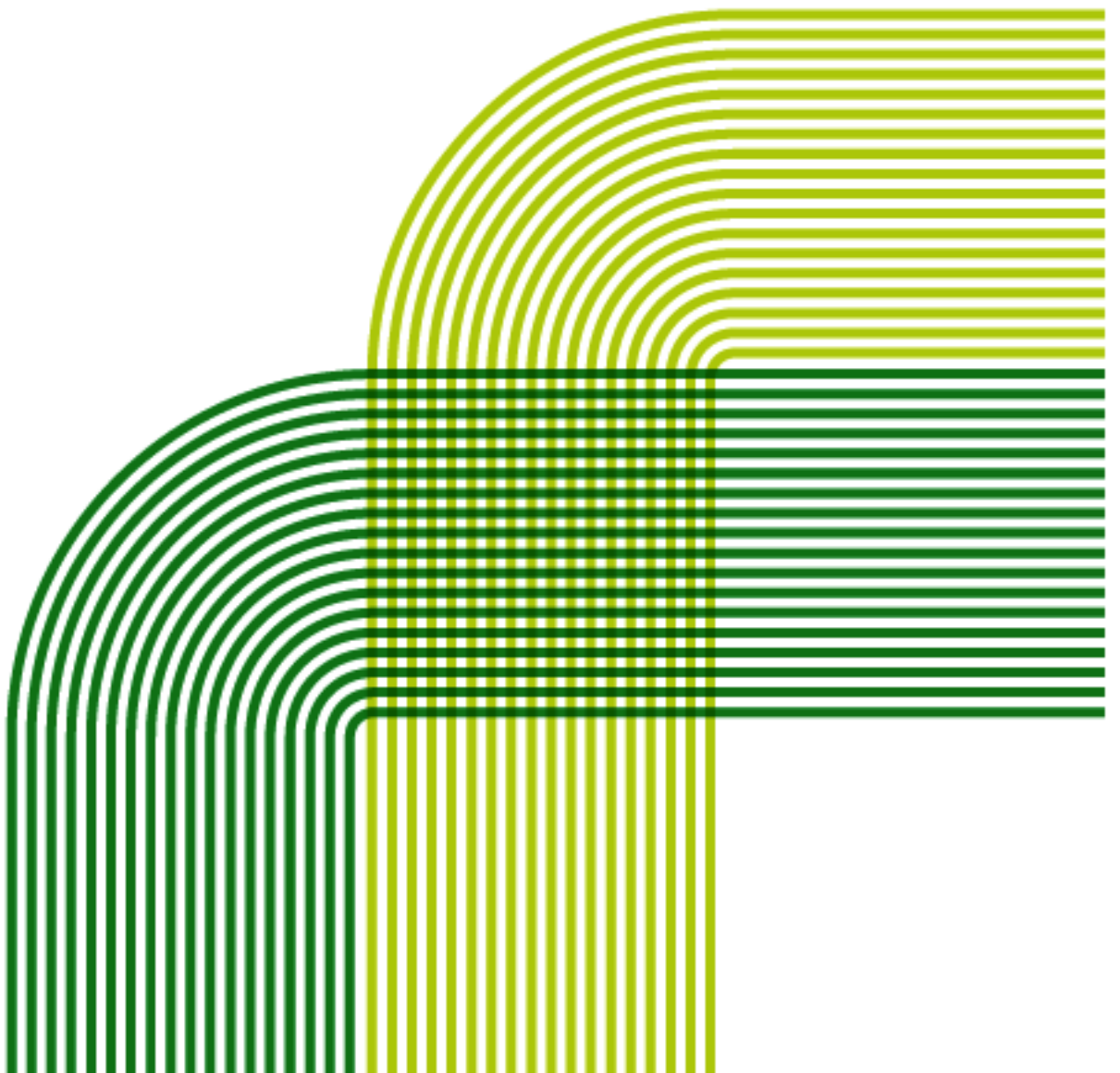
Prepared for Google and the Coalition for Digital Economy (Coadec)  
By IFF Research

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**IFF Research**



# 1 Summary

- 1.1 This report, commissioned by Google and Coadec, deals with the experiences and views of UK copyright law among a representative sample of 500 small and medium sized enterprise (SMEs), and a boost of 300 SMEs specialising in digital technology. In addition, there is qualitative evidence from 10 digital SMEs that are affected by the copyright laws, and 4 venture capital firms (VCs) that specialise in the digital technology sector.

## Experience of copyright

- 1.2 Overall, 18% of SMEs generally, and 23% of digital SMEs, have actively sought to protect their own copyrighted materials against infringement. Nineteen per cent of digital SMEs have some form of registered intellectual property (IP), such as patents, trademarks and designs.
- 1.3 Around half of digital SMEs use copyrighted materials created by others (with permission), a much higher proportion than for SMEs generally (16%). Digital businesses are also more likely to have been affected adversely by copyright in terms of not being able to pursue opportunities because of potential copyright problems (23%), and having to change a product in order to avoid using copyrighted materials (15%).
- 1.4 Of those that have had to change a product to avoid using copyrighted materials, the majority did so because it was illegal, for fear of litigation, or because of the expense or difficulty in getting permission. A quarter of digital SMEs affected in this way had received communications from a lawyer or the copyright holder.

## Awareness, understanding and views on copyright laws

- 1.5 The majority of digital SMEs (60%) claim that they are confident that they understand UK copyright laws, although they are much less likely to understand international copyright, e.g. in the USA (19%).
- 1.6 Qualitative evidence suggests that digital SMEs find UK copyright laws to be very complex, and to lack clarity.
- 1.7 Most digital SMEs think that the current copyright laws are a fair way of protecting the rights of content originators. However, a small but significant minority are of the opinion that their business growth is hampered by the current laws, and one in twenty of the digital SMEs is considering moving their business overseas because of them (c.2,350 businesses).
- 1.8 Some VCs think that UK copyright laws are a barrier to their investment in digital businesses.
- 1.9 The bulk of digital SMEs (63%) are favourable to having a provision in UK copyright law which is similar to that in the USA which allows 'fair use'. Only 13% are against this.
- 1.10 Awareness of the Digital Economy Act is very low, and only 6% of digital SMEs claim to understand it well.

## Impact of UK copyright laws

- 1.11 Three-quarters of digital SMEs that had to change a product because of potential copyright infringement had to spend time or money finding other material that could be used. One in ten claimed their sales were hit because of this.
- 1.12 Although half of those that had to give up on the pursuit of a product because of potential copyright infringement did not feel any impact as a result of this, a quarter felt it had restricted their sales. The VCs and entrepreneurs interviewed in this survey listed a number of ventures that had been abandoned because of possible copyright infringement.



- 1.13 7% of all SMEs, and 13% of digital SMEs have ever used a lawyer to deal with copyright issues. Of those using them, the average spent per year on lawyers each year is £10,675 for SMEs generally (most of whom are protecting their own IP or copyright), and £5,205 for digital SMEs.
- 1.14 However, there is evidence that smaller digital SMEs are unable to afford lawyer fees, and therefore have to spend a good deal of their own time ensuring they are copyright compliant.

### Conclusions

- 1.15 The majority of digital SMEs, and especially the smaller ones, have little awareness and understanding of the details of UK copyright laws. The default reaction is that copyright is a good thing, and they are passionate in their defence of it. However, when the principle of fair use is explained to them, the majority concede that this would be a helpful change to the rules. Among the minority who understand the law well, or who are directly affected by it, UK copyright laws can be very frustrating, and they are a barrier to growth and finance from investors.
- 1.16 Many digital companies are 'born global', and as such the concept that there are stricter copyright laws in some territories compared to others makes little sense. This has led some to consider moving overseas where laws are relaxed. Nobody seems to doubt the principle that content creators should be rewarded for their original work, but the mechanics of how this is done, and how it is policed, are considered by some to be too inflexible.
- 1.17 A number of suggestions were made for further modification of the law by digital companies, and the VCs who invest in this type of firm:
- Simplification and clarification of copyright law, with changes being made internationally in recognition of the fact that digital start-ups tend to operate internationally from the beginning;
  - Considering adopting a Digital Millennium Copyright Act (DMCA) style approach, in which, if any interested party objects to material posted online, and the digital firm responsible agrees to take it down immediately, no copyright breach is considered to have occurred;
  - A 'grace period' for new start-ups, to avoid them being destroyed by enforcement of copyright laws during their early 'copyright naive' phase;
  - Copyright laws offering 'stepped' levels of copyright protection, to allow businesses more flexibility to decide how long they want their material to be protected for; and under what circumstances they are happy for their material to be used;
  - Setting up a repository of 'orphan works', i.e. content for which the copyright owner is unknown. This would allow owners/creators to register as the owner of 'orphan works, thus creating revenue for content creators/owners and broadening the range of material that is available to be used by entrepreneurs.

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February 2011



## 2 Introduction

### Background

The Government is currently reviewing the state of intellectual property rights in the UK and EU with the aim of making IP law more suitable for innovation in the digital age. The review, which was announced by Prime Minister David Cameron in November 2010, is looking at a number of potential reforms of copyright and other IP measures, including the possibility of expanding the UK's 'fair dealing' policy to allow digital technology companies to use content created by others on a fair use basis, which is the case in the US. The review is considering whether current UK laws are barriers to innovative digital companies creating new products and services.

### Objectives

2.1 The objectives of the study are as follows:

- To determine the extent to which the current UK copyright laws affect SMEs and digital SMEs in particular;
- To ascertain awareness and understanding of copyright laws;
- To gauge views on copyright laws;
- To gather evidence on whether SMEs are affected adversely by the current laws;
- To gain views on how the laws could be amended further to benefit digital companies.

### Methodology

2.2 The survey took a multi-stage approach as follows:

1. **Omnibus** – 500 CATI<sup>1</sup> interviews with a representative sample of UK SMEs were conducted between 24<sup>th</sup> January and 2<sup>nd</sup> February 2011. The purpose of this stage was to compare the experiences of UK SMEs generally with those of digital SMEs.
2. A **quantitative survey of digital SMEs** – 300 CATI interviews were undertaken between 31<sup>st</sup> January and 11<sup>th</sup> February 2011. This stage of research examines the views and experiences of UK copyright among specific 'digital' SMEs in certain Standard Industrial Classification (SIC) codes<sup>2</sup>.

23% of these digital businesses can be described as 'disruptively innovative', i.e. those that have a product, service or business model that is substantially different from anybody else's. 18% are 'incrementally innovative' - those who have a product, service or business model that others created, but they built upon. The remaining 59% of digital SMEs interviewed are described as 'non-innovative'.

<sup>1</sup> CATI = Computer Assisted Telephone Interviews

<sup>2</sup> 2007 UKSIC 47.91 (remote retail), 58.20 (software), 59.13 (film & TV), 61.90 (telecommunications), 62.02 (computer consultancy), 62.09 (other IT), 63.10 (data processing), 63.91 (news agency), 73.10 (advertising) and 77.22 (DVD rental). Within the research these have been amalgamated to form four sub-sectors – software, other digital technology, media distribution and other. Full details of those interviewed are found in Section 7.



The 2009 SME Statistics<sup>3</sup> published by the Department for Business, Innovation and Skills estimate that there are approximately 59,000 of these digital technology SMEs in existence in the UK.

3. **Qualitative depths with digital SMEs** – ten face-to-face depth interviews with owners or managers of London-based digital SMEs that have been directly-affected by UK copyright laws.
4. **Qualitative depths with VCs** – four interviews with representatives of VCs that specialise in the digital technology sector<sup>4</sup>.

### Note on the quantitative findings

- 2.3 Except where stated, commentary on a sub-group finding means that the finding is statistically significant at the 95% confidence level against either the total or the comparative survey/question.

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<sup>3</sup> <http://stats.bis.gov.uk/ed/sme/>

<sup>4</sup> There is a degree of overlap between VCs and digital firms: the VCs tended to have made their money through starting technology firms themselves; and often remained directly involved in firms as well as investing in them. The classification of a respondent as a VC rather than as digital firm is sometimes, therefore, purely determined by how a respondent chooses to describe themselves.



### 3 Experience of copyright laws

#### Having Intellectual Property

- 3.1 Overall, 18% of SMEs generally have created their own copyrighted materials and actively sought to protect them against copyright infringement. This is most likely to happen in the manufacturing sector (34%). Twenty-three per cent of digital companies have done this, and whilst there are no major differences by sub-sector, those that are disruptively innovative are more likely to have done this (36%).
- 3.2 A slightly lower proportion of digital SMEs, 19%, already have some form of registered IP, such as patents, registered designs or trademarks. This was most likely to be the case among software companies (28%), digital SMEs with more than 10 employees (42%), and the disruptively innovative (36%). A much lower proportion of 'other' digital technology SMEs hold any IP (10%).
- 3.3 Six per cent of digital SMEs are in the process of applying for any form of registered IP. This proportion rises to 25% among medium sized digital companies (with 50-249 employees).

#### Experience of copyright

- 3.4 The table below shows SME experience of UK copyright laws, for SMEs generally, and for digital SMEs.

<b>Table 1: Experience of UK copyright law</b>		
Base = All SMEs/Digital SMEs	<b>All SMEs</b>	<b>Digital SMEs</b>
n=	500	300
	%	%
Created own copyrighted materials, actively sought to protect against copyright	18	23
Used copyrighted materials created by others in product development, with permission	<b>16</b>	<b>52</b>
Decided not to pursue a product or opportunity because of the possibility of copyright problems	<b>11</b>	<b>23</b>
Changed a product to avoid using copyrighted material	<b>2</b>	<b>15</b>
Used copyrighted materials created by others in product development, without permission	*	<b>5</b>
None of these	<b>66</b>	<b>33</b>
Refused/don't know	2	2

Figures in bold are statistically significant findings between the two groups  
 \* = a figure which is more than 0%, but less than 0.5%



## 3.5

## Using copyrighted materials created by others

- 3.6 Sixteen per cent of all SMEs have used copyrighted materials created by others in product development, with permission, whilst less than 1% admit to using them without permission. Using copyrighted materials with permission is most common in the business services sector (22%). Digital SMEs are much more likely to have done this: 52% using the copyrighted material of others with permission, 5% without permission.
- 3.7 Most likely to have used copyrighted material with permission are those with turnover of £250k or more (78%), and the incrementally innovative (71%). There are no significant differences by sub-sector.

## Changing or not pursuing a product or opportunity because of copyright

- 3.8 Eleven per cent of all SMEs and 23% of digital SMEs have at one time decided not to pursue a product or opportunity because of the possibility of copyright problems, whilst 2% of all SMEs and 15% of digital SMEs have changed a product to avoid using copyrighted material.
- 3.9 Thirty-seven per cent of media distribution SMEs have at some stage not pursued a product or opportunity because of the possibility of copyright infringement, compared to 22% of other digital technology businesses and 17% of software SMEs. The disruptively innovative (31%) and incrementally innovative (36%) are also more likely than average to have not pursued this because of copyright law.
- 3.10 The media distribution SMEs are also more likely than average to have changed a product to avoid using copyrighted material (23%), which compares to 16% of other digital technology SMEs and 8% of software SMEs.
- 3.11 The reasons for changing a product are given below. The main reasons, among SMEs generally and the digital SMEs, are that it is illegal, too expensive to get permission, and because they fear litigation. Although sample sizes are small for this question, digital SMEs are significantly more likely than SMEs generally to have received communication from lawyers or copyright holders telling them to stop using the material (23%, compared to 6% of all SMEs).

**Table 2: Reasons for changing a product in order to avoid using copyrighted material**

Base = All SMEs/Digital SMEs who have changed a product in order to avoid using copyrighted material	All SMEs	Digital SMEs
n=	20	47
	%	%
Because it was against the law	67	66
Too expensive or difficult to get permission to use the material	35	58
Fear of litigation	63	54
Too expensive or difficult to get legal advice	29	52
Tried and failed to get permission to use it	25	24
Received communication from lawyer or copyright holder	<b>6</b>	<b>23</b>
Other	29	9
Figures in bold are statistically significant findings between the two groups		





## 4 Awareness and understanding

### Understanding of copyright law

- 4.1 The majority of digital SMEs agree that they understand the copyright laws in the UK. Thirty per cent agree strongly that they confidently understand the laws, with a further 30% agreeing slightly.

<b>Table 3: Agreement with statement; “I am confident I understand the laws regarding the creation of copyrighted materials, and the use of others’ copyrighted materials by businesses....”</b>		
Base = All Digital SMEs	....In the UK	....Outside of the UK, e.g. in the USA
n=	300	300
	%	%
Agree strongly	<b>30</b>	<b>7</b>
Agree slightly	<b>30</b>	<b>12</b>
Neither agree nor disagree	11	16
Disagree slightly	11	13
Disagree strongly	<b>16</b>	<b>48</b>
Don't know	2	4
TOTAL AGREE	<b>60</b>	<b>19</b>
TOTAL DISAGREE	<b>27</b>	<b>61</b>
NET (Agree minus disagree)	<b>+34</b>	<b>-42</b>
Figures in bold are statistically significant findings between the two groups		

- 4.2 Most likely to agree that they understand the laws are employers (77%, compared to just 57% of those with no employees) and the disruptively innovative (72%). There was no one sub-sector more likely to understand the laws, but a lower proportion in the ‘other’ category, which includes internet sales and telecoms, claim to understand the law (37%).
- 4.3 In comparison, the understanding of non-UK copyright law is weak. Only 19% of digital SMEs agree that they understood it, compared to 61 per cent who do not understand it. Most likely to understand it are the disruptively innovative (27%), and the biggest companies in terms of turnover (57% of those with sales of over £5 million), but there are no significant differences by sub-sector.
- 4.4 For those that are not confident about understanding UK copyright, 57% say they don't need to know about it, whilst 18% have never looked into it before, and 11% say it is somebody else's job to know about it. One in five of these people say that the law is too complex.
- 4.5 However, according to the qualitative evidence from digital firms affected by current copyright laws, and VCs that specialise in investing in this type of firm, the UK copyright regime is perceived as particularly difficult to understand. By comparison, the US regime is seen as more punitive *when a breach is made*, but gives firms more clarity about how to avoid a breach in the law, and makes it easier to avoid doing so.



- 4.6 The Digital Millennium Copyright Act (DMCA) in the USA has a set of rules as to what has to be paid, and how other people's content can be used. It also works on the principle that, if any interested party objects to material posted online, the digital firm responsible (in this context, the 'publisher') agrees to take it down immediately – and, if they do this, no breach is considered to have occurred. This compares with the UK, where there is the possibility that, no matter how quickly the digital firm removes the offending material, they may still be held in breach of copyright. Some of the firms and VCs affected by copyright argued that a DCMA-style approach should be adopted in the UK.



## 5 Views on copyright law

### Views on UK copyright law

5.1 Respondents were asked the extent to which they agreed or disagreed with a number of statements concerning UK copyright law.

<b>Table 4: Views on UK Copyright Laws</b>				
Base = All Digital SMEs (n = 300)		<b>Agree</b>	<b>Disagree</b>	<b>NET</b>
The current UK copyright laws are a fair way of protecting the rights and interests of creative content originators	%	66	10	+56
If anything, the copyright laws in the UK should be more stringent	%	22	33	-11
The current UK copyright laws are a barrier to my business innovating	%	7	72	-65
My business does not perform as well as it could because of the current UK copyright laws	%	5	74	-69
I have considered moving my business overseas because of UK copyright laws	%	4	88	-84

5.2 The majority of digital SMEs are broadly in favour of UK copyright laws. Two thirds agree that the current UK copyright laws are a fair way or protecting the rights and interest of creative content originators, and only 10% disagree. Most likely to agree are the disruptive innovators (81%) and media distribution companies (78%). Least likely to agree are the incremental innovators (63%).

5.3 In the qualitative interviews, the digital firms affected by copyright law, and the VCs that invest in these firms, question whether the current regime is the best way of protecting these rights. Whilst they recognise the need of the content creators to be paid, they argue that:

- The strictness of current UK copyright laws often prevents materials being used at all, even if it were ultimately to benefit the content creator if they were to be used, as it would promote their work to an audience that might ultimately pay them. For example, a musician might be given publicity and thus sales on the basis of their music being used in video content online, but the cost of the rights to use the music means it is not featured. A similar example was given of people in rural areas downloading parts of films using Torrent, in order to gauge whether or not to make the trip to the nearest cinema to watch the film in full. Currently, whenever made aware of this, their Internet Service Provider was having to cut the internet connections of these users until they had removed the downloading software from their PCs;



- The current copyright laws are, in the view of one VC, set up to protect the rights and the revenues of the 'middle men', when this business model is out of date in an era in which the content creator and the audience can interact without them. Arguably, the content creator could generate more income if the copyright regime recognised that revenue opportunities lie in making it easier for their content to be made available to their potential audience;
  - The current copyright laws assume that the content creator wishes their work to be copyrighted indefinitely, when it would be less inhibiting for digital entrepreneurs if copyright were to lapse by default after a certain period, and content creators/owners could decide to extend their copyright if they wanted to do so;
  - Even if you do not wish to completely restrict use of your own business's material by others, or prevent your employees from re-using their own ideas in a new context, the copyright laws are very 'black and white': something is either copyrighted or it is not;
  - Paradoxically, there are areas in which the complexity of the current regime, and the lack of copyright knowledge amongst content creators, also cause content creators to fail to copyright their work entirely (e.g. when uploading music to MySpace or video content to YouTube);
  - The academic research-sharing site Mendeley makes the point that, in their case, the content creators and the users of their site are often the same group of people.
- 5.4 One in five (22%) actually think the UK copyright laws should be more stringent, although a third disagree with this. The media distribution businesses are the most likely to agree (33%, net agree -1%), while the incremental innovators are the least likely to agree (7% agree, net agree -35%).
- 5.5 Only a minority of those surveyed are against the current laws, with 7% thinking that copyright laws are a barrier to their business innovating, 5% thinking their business does not perform as well as it could because of the current laws, and 4% considering moving their business overseas because of the laws. When grossed up, this equates to approximately 2,350 companies in the UK that are considering moving their businesses overseas.

#### Views of VCs on UK copyright laws

- 5.6 The VCs have a similar view to the digital SMEs that are considering relocation. They argue that the UK copyright regime is perceived as particularly opaque, and as the kinds of digital firms they invest in operate in the online domain, these firms can be run from anywhere. Therefore there is a risk that the UK copyright regime will make the UK unappealing for both investors and new businesses, thus encouraging them to move elsewhere. Ultimately, this could have a negative impact on the competitiveness of 'UK PLC'. The UK is compared unfavourably with:
- The US: two of the entrepreneurs interviewed qualitatively claim they are considering moving to the US because the US copyright regime gives firms based there a 'massive advantage'.
  - China: this is mentioned as a territory in which copyright is less strict and thus enables its technology entrepreneurs to be far more competitive:

*"The result is they can act faster and are better capitalised; they can show the content they need to show."  
(Specialist VC, White Bear Yard)*



- 5.7 One digital entrepreneur argues that the UK copyright regime is the reason that the games industry has fared better than other creative technology sectors in the UK:

*[The UK copyright regime] completely stifles innovation, destroys value creation. It's not accidental that gaming is the one industry where things have worked in the UK – because there's no IP involved, but if you need to use someone else's intellectual property it's almost impossible here.” (Technology entrepreneur)*

#### Views on changing UK copyright law to having a 'fair use' rule

- 5.8 Digital SMEs were asked whether they were favourable or unfavourable to the following:

*“In the USA there are 'fair use' rules covering the circumstances in which copyrighted materials may be used without the rights-holder's express permission for any of a number of purposes, including commentary, criticism, news reporting, research, teaching, library archiving and scholarship. To what extent are you in favour or against having a provision in UK copyright law similar to the USA one on fair use?”*

- 5.9 The majority of digital SMEs (63%) are in favour of this provision, with only 13% being against it.

**Table 5: Favourability towards having a provision in UK copyright law similar to the USA one on fair use – by sub-sector**

Base = All Digital SMEs	All	Software	Other Digital Technology	Media distribution
n=	300	99	106	63
	%	%	%	%
Strongly in favour	32	35	39	29
Slightly in favour	31	28	31	29
Neither in favour nor against	19	18	18	18
Slightly against	7	9	5	5
Strongly against	6	9	<b>2</b>	<b>14</b>
Don't know	5	2	5	4
TOTAL IN FAVOUR	63	63	70	59
TOTAL AGAINST	13	17	<b>7</b>	19
NET (In favour minus against)	+50	+45	<b>+62</b>	+40

Figures in bold are statistically significant between all digital SMEs and the sub-group

- 5.10 The other digital technology SMEs are the most in favour of this amendment (net favourable +62%). Those in media distribution are the most likely to be strongly against, but even so this group demonstrated positive favourability to the provision overall.
- 5.11 The incrementally innovative are the most likely to be in favour (net favourable +67%), the disruptively innovative the least (+43% net favourable), but even they are more likely to be in favour than against.
- 5.12 In the qualitative interviews, some digital entrepreneurs and VCs argue that adoption of fair use would help the situation in the UK. By permitting excerpts of works (e.g. pieces of music, art collections) to be shown, more interesting and innovative content could be created.



- 5.13 However, there is a question about whether simple emulation of the US model is enough. One VC claims that the US 'fair use' exceptions also suffer from a degree of ambiguity regarding how many users material can be shared amongst, whilst still being covered by fair use exceptions.
- 5.14 The academic research-sharing site Mendeley suggests that, if 'fair use' were adopted in the UK, it would assist their business. However, they also make the point that, to date, in both the US and the UK, DMCA has been the more relevant legal concept in guiding their approach to copyright matters<sup>5</sup>.

#### Overall preference for revising UK copyright laws

- 5.15 When given a choice – should the UK copyright law be changed or not – respondents are almost equally split between opposing any changes (29%), supporting a revision (30%), whilst 34% cannot agree totally with either statement.

<b>Table 6: Preference for revising copyright laws – by sub-sector</b>				
Base = All Digital SMEs	All	Software	Other Digital Technology	Media Distributors
n=	300	99	106	63
	%	%	%	%
I would oppose any change in the copyright laws, they do a good job of managing IP	29	32	25	37
I would support a revision of copyright laws, they currently obstruct people doing business	30	31	34	30
Neither of these	34	32	36	<b>21</b>
Don't know	7	5	6	<b>12</b>
Figures in bold are statistically significant between all digital SMEs and the sub-group				

- 5.16 There are no significant differences in opinion between sub-sectors. Those most likely to favour a revision to the copyright laws are those with turnovers of £250k + (54%). Those most likely to oppose changes to the copyright laws are the disruptively innovative (47%), whereas only 15% of the incrementally innovative agree that there should be no changes.

<sup>5</sup> I.e. the principle that, if any interested party objects to material posted online, the digital firm responsible (in this context, the 'publisher') agrees to take it down immediately – and, if they do this, no copyright breach is considered to have occurred.



## Views on the Government's proposed changes to IP laws

*"In November 2010 the Prime Minister David Cameron announced that the Government would be reviewing its IP laws, including copyright laws, with the objective of making them fit for the internet age. To what extent do you agree or disagree with the following statements about this."*

<b>Table 7: Views on Government's proposed changes to IP laws</b>				
Base = All Digital SMEs (n = 300)		<b>Agree</b>	<b>Disagree</b>	<b>NET</b>
I think it is very important to the success of the British economy	%	58	17	+41
I think it may be helpful but is unlikely to have much impact on the British economy one way or the other	%	51	21	+29
I think it should not be a Government priority	%	45	41	+4
Any revision to the existing copyright laws will create uncertainty	%	35	33	+2
Any revision to the existing copyright laws will make it more difficult for businesses that rely on copyright to get investment	%	20	34	-14
I think the review is a waste of time and resources	%	25	52	-27

- 5.17 The majority of digital SMEs (58%) consider a review of the copyright laws very important to the success of the British economy. Most likely to agree are the disruptively innovative (71%). Forty-five per cent think the review should not be a Government priority, whilst a quarter think the review is a waste of time and resources. The three categories are not mutually exclusive and respondents may have agreed to more than one of these.
- 5.18 Just over half (51%) of all digital SMEs think the review is unlikely to have much impact on the British economy one way or the other, with this view being most common among the smaller turnover businesses (54% of those with up to £250k turnover).
- 5.19 Respondents are evenly split between agreeing and disagreeing that a revision to the current laws will create uncertainty (35% agreeing, 33% disagreeing). The media distribution SMEs are most likely to agree with this sentiment (49%) and the other digital technology SMEs the least likely to agree (27%). Only one in five agreed that any revision would make it more difficult for businesses that rely on copyright to get investment. Again, the media distribution SMEs are the most likely to agree (36%), and the other digital technology companies the least likely (13%).



### Suggestions for changing UK copyright laws

5.20 A number of suggestions for further modification of the law are made (in the qualitative interviews) by digital entrepreneurs and VCs:

- Simplification and clarification of copyright law, with changes being made internationally in recognition of the fact that digital start-ups tend to operate internationally from the beginning;
- Considering adopting a Digital Millennium Copyright Act (DMCA) style approach, in which, if any interested party objects to material posted online, and the digital firm responsible agrees to take it down immediately, no copyright breach is considered to have occurred;
- A 'grace period' for new start-ups, to avoid them being destroyed by enforcement of copyright laws during their early 'copyright naive' phase;
- Copyright laws offering 'stepped' levels of copyright protection, to allow businesses more flexibility to decide how long they want their material to be protected for; and under what circumstances they are happy for their material to be used;
- Setting up a repository of 'orphan works', i.e. content for which the copyright owner is unknown. This would allow owners/creators to register as the owner of 'orphan works, thus creating revenue for content creators/owners and broadening the range of material that is available to be used by entrepreneurs.





## 6 Views on the Digital Economy Act

### Awareness and understanding of the Digital Economy Act

- 6.1 Only a quarter of digital SMEs had heard of the Digital Economy Act before being interviewed for this survey. Awareness is greater the larger the business, but there are no significant differences according to the level of innovation or sub-sector.

<b>Table 8: Awareness and understanding of the Digital Economy Act – by size</b>				
Base = All Digital SMEs	<b>All</b>	<b>No employees</b>	<b>Micros (1-9)</b>	<b>Small/ Medium (10-249)</b>
n=	300	82	151	64
	%	%	%	%
Good understanding of the act	2	1	3	<b>5</b>
A general idea of what it is about	5	3	9	7
Vague idea of what it is about	7	6	<b>13</b>	12
Heard of it, know very little	6	6	7	6
Heard of it, know nothing	5	6	3	5
Never heard of it	75	77	<b>64</b>	<b>66</b>
<b>TOTAL HEARD OF IT</b>	25	23	<b>36</b>	<b>34</b>
<b>TOTAL UNDERSTAND IT WELL (good understanding/general idea)</b>	6	5	<b>12</b>	<b>12</b>
Figures in bold are statistically significant between all digital SMEs and the sub-groups				

- 6.2 Overall, only 2% of digital SMEs claim they have a good understanding of the act, with a further 5% claiming they have a general idea of what it is about. Combined, this means that 6%<sup>6</sup> of digital SMEs understand the Act well. The larger SMEs are more likely to understand it than the sole traders, but there are no significant differences in the understanding according to sub-sector or levels of innovation.

<sup>6</sup> Figures do not sum due to rounding.



## Favourability towards the Digital Economy Act

- 6.3 The Digital Economy Act was summarised to respondents, whether they had heard of it before or not, as follows:

*“The Digital Economy Act came into force in April 2010. It established a system which aims to increase the tracking down and suing of online copyright infringers, and in some cases requires Internet Service providers to introduce technical measures such as reducing the quality of, or terminating, those infringers’ internet connections. From what you know or have just heard, are you broadly in favour or against the Act as it currently stands.”*

- 6.4 The majority of digital companies interviewed are in favour of the Act: 28% strongly in favour, and 32% slightly in favour, a combined total of 59%. Only 16% are against the Act. The net favourability was therefore +43%.
- 6.5 Those demonstrating lower than average net favourability are the software SMEs (+32% net favourable), and the incrementally innovative (+16% net), whereas the disruptively innovative were the most likely to be in favour (+55% net). Those in media distribution are both significantly more likely to be strongly in favour of the Act, and significantly more likely to be strongly against it. Perhaps surprisingly, those that hold IP are no more in favour of the Act than those without (59% of both groups in favour).

Table 9: Favourability towards the Digital Economy Act – by sub-sector				
Base = All Digital SMEs	All	Software	Other Digital Technology	Media Distribution
n=	300	99	106	63
	%	%	%	%
Strongly in favour	28	23	23	<b>46</b>
Slightly in favour	32	29	36	<b>21</b>
Neither in favour nor against	17	18	17	7
Slightly against	6	<b>10</b>	6	1
Strongly against	10	10	9	<b>17</b>
Don't know	8	9	8	8
TOTAL IN FAVOUR	59	52	59	67
TOTAL AGAINST	16	20	15	18
NET (In favour minus against)	+43	<b>+32</b>	+43	+49
Figures in bold are statistically significant between all digital SMEs and the sub-group				

- 6.6 Favourability levels do vary according to knowledge of the Act. Those who have no understanding of the Act, or have never heard of it, are more likely than average to think they should be in favour of it (net favourability +49%). On the other hand, those who understand it very well are almost as likely to be favourable as unfavourable (43% favourable, 36% unfavourable, +7% net favourable.) Therefore, the conclusion is that the more one knows about the Act, the less likely one is to be in favour.
- 6.7 The reasons given in the quantitative survey for being in favour of the Act largely relate to the need to protect copyright generally, rather than the Act in particular:



*"I think measures should be taken against infringement. We are keen to protect our own IP and I think others should be afforded the same rights." (Web developer, 50-99 employees)*

*"Because if I spent my time and money over years building my website I'd be annoyed if someone could just come and copy and paste my information." (Telecommunications company, 1-5 employees)*

*"Online piracy is a crime and I believe that the concept of fair use and utilising someone else's copyright if paid for is reasonable, as opposed to stealing it. Copyright allows film makers to make a valid point in their work." (Film distributor, 6-9 employees)*

*"Because people treat digital copyright as being different from physical copyright. Why should you get a piece of software for free when I have invested so much money on developing it, and a competitor can steal the idea and make money without that investment. My business would fold." (IT consultancy)*

*"If somebody nicks my stuff, I want them caught. I'm not sure who pays the cost of prosecuting or catching them – if it's down to me to catch them, where will I find the funding from?" (Educational software publisher, 1-5 employees)*

*"Because from what you have said, without the Act someone can copy my information over the internet, so it affords protection for businesses like mine." (IT consultant, no employees)*

*"I think that when people create things like digital online, or if we use pictures on our website, then we should pay for that which we use, and there should be some enforcing of this. In this country the problem is that a lot of things are offshore and developed in other countries that we cannot control. We can spend time and effort trying to look at that, but it will be costly in terms of enforcing, and too much law is not good either." (IT support, 1-5 employees)*

- 6.8 The reasons for being against the Act relate to freedom of information, the impracticality of the terms of the Act, and the terms of the Act being too harsh:

*"It's a waste of time and money, I don't think it would work. ISPs would have to spend money on equipment." (Internet services, 1-5 employees)*

*"I'm committed to open source, I don't think the government has any way of shutting it and it's very simple to go around it." (Web-based software developer, 1-5 employees)*

*"It's a sledgehammer to crack a nut. It's only the music industry where the problems lie, and it could be responsible for lousing up the whole e-commerce of the UK. The government need to wake up to the fact that they are being pressurised by lobbyists." (E-commerce project management, 1-5 employees)*

*"There would be a monopoly on certain products or services that are already quite difficult to acquire, and although I don't condone the use of pirated or illegal material I feel that it would still have a detrimental effect on small businesses. The companies that are chasing this are the ones with the most money, they aren't really changing anything, they're just owning everything." (Data management, 1-5 employees)*

*"It's attacking the wrong people. If people are downloading illegally you track them down and deal with them, but tracking IP is a different issue – the ISPs become like policemen, just to protect the movie or entertainment industry. I don't think that's right, there's too much infringement on my rights to freedom of information." (Software developer, no employees)*



*“The additional cost of implementing counter measures and controls by ISPs and service providers of all sorts would result in unwarranted increased cost, which would be passed on to customers and users, with very little to no benefit for the majority of users or customers.” (Technology consultancy, 6-9 employees)*

*“I think requiring ISPs to be responsible for other peoples’ action is inappropriate. I’m not satisfied that there is enough of a review on this process. I’m wary of anything that damages the network mentality principle and I’m wary of unequal access to the internet.” (Computer consultant and trainer, no employees)*

*“Because the freedom of the internet is a greater force for good than small-scale losses due to piracy.” (Software development, 1-5 employees)*

*“The Act is very wide ranging, very biased to small groups of people and does not consider the general public. Big music companies are trying to protect their business models and therefore they are not being fair to smaller businesses.” (Satellite TV broadcaster, 100-249 employees)*

### Qualitative views on the Digital Economy Act

6.9 In the qualitative interviews the digital entrepreneurs and VCs thought that the Act was being set up to protect outdated business models, particularly in the music industry, without any recognition of the needs of digital start-ups or of how the Internet is used within communities. They argue that, in seeking to prevent large-scale copying and dissemination of material, copyright law will also crack down on digital sharing on a small scale that used to occur informally without any penalty, e.g.:

- People within a community lending each other books or sharing photos (once digitalised, and shared digitally, the fear is that these materials will be held in potential breach of copyright);
- Academics discussing research papers (once a paper is put online for discussion a copy has in effect been made on the website server, thus creating a potential copyright breach).

*“Strict copyright law that was made in the 70s doesn’t really apply in an age where everything digital is actually copied anyway. If I give you a piece of paper, I don’t still have the piece of paper but in digital, I give you a piece of material but I still have it as well so even by accessing a website you are technically breaking the rules.” (Technology entrepreneur, A-Frame)*



## 7 Impact of UK copyright laws

### Impact of not being able to use copyrighted material

- 7.1 Of those digital SMEs that needed to change a product in order to avoid using copyrighted material, nearly three-quarters (74%) had to spend time or money finding other material that could be used. This was less likely to be the case for those that decided not to pursue a product (8%).

Table 10: Impact of not using copyrighted material		
Base = All Digital SMEs who have changed a product in order to avoid using copyrighted material/decided not to pursue a product or opportunity because of possible copyright infringement	Changed a Product	Decided not to pursue a product
n=	47	66
	%	%
Restricted the sales that might have otherwise been gained	10	24
Caused financial problems for the business	3	9
Had to spend time or money finding other material that could be used	<b>74</b>	<b>8</b>
No real impact on the business	<b>24</b>	<b>51</b>
Other	9	12
Don't know	1	1
Figures in bold are statistically significant findings between the two groups		

- 7.2 Restricted sales occurred for one in ten of those who needed to change a product to avoid a copyright conflict, and for one in four of those that decided not to pursue a product.
- 7.3 Relatively few had financial problems as a result of needing to change a product (3%), or not pursuing a product (9%).
- 7.4 Needing to change a product was more likely to have an impact than not pursuing it. The need to change a product had no real impact on the business for a quarter where this occurred, but there was no impact for half of those that decided not to pursue a product.

### Avoidance of copyrighted materials

- 7.5 In the qualitative interviews, the entrepreneurs and VCs commented that, in addition to the time costs involved in trying to understand the copyright regime internationally, the current lack of clarity could lead firms to decide not to try to understand all the detail of copyright law, but instead to give a wide berth to 'grey areas' in copyright, i.e. in which they might run into difficulties. This was perceived to hamper innovation, as firms avoid pursuing ideas that might lead to copyright problems.



7.6 There were instances in the qualitative interviews of digital firms talking about abandoning business ideas altogether due to concerns about copyright, for instance:

- A system of sharing data between blogs, abandoned because there was no way of accurately determining what was and wasn't copyrighted material;
- A file sharing service for academic papers, not pursued due to copyright laws – in the meantime, a US competitor scribd.com, that fulfils this role, has taken off (but has now itself been hit by a class action for copyright):
- A music industry 'sandbox', in which software developers could be given materials to develop new formats and new tools for the music consumer, prevented due to copyright issues;
- An application to share music via Facebook, turned down for investment due to likelihood of copyright problems;
- Online mix tapes of music being impossible to licence.

#### Investment in digital firms

7.7 The VCs also claim that the current copyright regime has a detrimental impact on their ability to invest in digital technology firms. They have to be particularly careful that the firm they are considering investing in genuinely has ownership of its assets/content – this often involves giving careful scrutiny to contracts with employees, suppliers and sub-contractors.

7.8 The VCs argue that this is a 'binary' situation: if a business is likely to run into copyright issues, rather than offering investment on less favourable terms, they will not invest at all. At best, the firm will be told to go away and resolve their copyright issues. The VC will only consider investing if they are able to achieve this.

7.9 Firms that are content 'creators' rather than 'curators' therefore tend to be more appealing as investment propositions, as it is easier to establish that they own the rights and can maintain the value of their assets. There are specific examples of difficulties with 'curating' others' content:

- Music and video content can be licensed on such terms that they are unaffordable for a new business. Alternatively, the firm can buy into a music/video library, which makes it more affordable (e.g. £100k per annum), but which restricts the scope of what can be used, thus inhibiting innovation. Some claim that music is now becoming increasingly difficult to licence and many of the collective rights are no longer available to buy into;
- Art that is still within copyright/by a living artist can be enormously time-consuming due to the need to clear every single image individually with the artist, sometimes via their gallery (however, much art is now out of copyright/already in the public domain).

7.10 To put this into context, one specialist VC estimates that he is presented with around 1,000 new business ideas a year, 50-100 of these will typically involve copyright, and 90% of those involving copyright are turned down due to the likelihood of experiencing copyright problems.



- 7.11 However, a generalist VC, who invests in digital start-ups as well as other businesses, goes against the grain of some of the views of these specialist VCs. The generalist VC would not necessarily support a weakening of copyright laws, as it would make it harder to defend the rights of the firms they have invested in (and thus harder to maintain their value). In common with the other VCs and firms, they would, however, support a *clarification* of the copyright regime, as currently it can be unclear as to whether a start-up is at risk of infringing copyright (and, in such circumstances, in common with the other VCs, they tend not to invest).
- 7.12 One of the technology entrepreneurs also holds the view that the current copyright regime presents few problems to his business. However, there is again some consistency with other entrepreneurs, in that they feel that copyright is an international rather than a UK-specific issue.

#### Usage of lawyers

- 7.13 Seven per cent of all SMEs, and 13% of digital SMEs have ever used a lawyer to deal with copyright issues. For SMEs generally this appears to be mainly to protect copyright, with 37% of manufacturing SMEs having used lawyers; for digital SMEs this was more likely among content creators, with 27% of software publishers having ever used a lawyer, and 22% of media distribution SMEs, compared to just 10% of other digital technology SMEs. Larger companies were much more likely to use lawyers than smaller ones.
- 7.14 For SMEs generally the average amount spent on lawyers per year is higher than it is for digital SMEs – a mean average of £10,675, compared to £5,205. A high proportion of digital SMEs spend nothing or a minimal amount on lawyers (32% of those using them), and this is particularly so for media distribution SMEs (59%). Forty-two per cent of the smaller turnover SMEs that use lawyers (i.e. those with less than £250k turnover) only pay a minimal amount. The reason for this discrepancy is likely to be because digital SMEs that use lawyers for copyright purposes are more likely to do this in order to use content created by others, than SMEs generally who are more likely to do this to protect their own IP, which costs more to do.

**Table 11: Average amount of money spent each year on lawyers to deal with copyright**

Base = All SMEs/Digital SMEs who have ever used lawyers to deal with copyright	All SMEs	Digital SMEs
n=	42	48
	%	%
Nothing/a minimal amount	13	32
Less than £500	10	19
£500 - £2499	13	19
£2500- £9999	5	3
£10,000 - £49,999	25	10
£50,000 or more	*	1
Don't know/refused	33	16
Mean average	£10,675	£5,205
Figures in bold are statistically significant findings between the two groups		
* = a figure which is more than 0%, but less than 0.5%		

- 7.15 A point made in the qualitative interviews with firms affected by copyright law was that, as well as costs associated with the use of lawyers, another type of direct cost associated with copyright law is that of insuring



the business against breaches in copyright law. Taken together, the cost of legal fees and insurance was estimated at around £50k to £100k per year for one entrepreneur interviewed.

- 7.16 The qualitative interviews also point towards hidden costs that have a detrimental impact on the businesses affected. Many of the entrepreneurs are unable to afford legal help with copyright and are therefore dealing with copyright issues themselves – resulting in a time cost. The digital entrepreneurs affected by copyright law and the VCs spend a long time figuring out what the implications of copyright law are, which distracts them from what they believe they should be focusing on, i.e. building their business.
- 7.17 The point is also made that the current lack of clarity in copyright laws discriminates against smaller businesses, as the larger and better resourced businesses are better able to fight their cases than the smaller entrepreneurs.
- 7.18 The UK law is also defined in a ‘qualitative manner’, using terms such as ‘substantial’ that can only be gauged on a case-by-case basis by a human being. One technology entrepreneur (the online news portal, NewsNow) argues that this inhibits businesses (like search engines) that employ computer systems to assess whether content can be used without breaching copyright, as computers can make quantitative judgements but cannot weigh up the merits of an individual case in a qualitative manner.
- 7.19 Generally the UK copyright laws are considered to be unclear:

*“Even though our largest user base is in the US and we are DMCA compliant, we are uncertain if that would protect us if there were a law suit in the UK. We are operating in a sphere of ‘tolerated uncertainty’ of our legal situation – I would like certainty and clarity.” (Technology entrepreneur, Mendeley)*

### Other impacts of the current copyright laws

- 7.20 This highlights an issue with the current copyright regime that is not UK-specific. In the qualitative interviews, the entrepreneurs and VCs note that these kinds of businesses – because they are operating in the online domain – often launch across multiple markets worldwide. The copyright laws are completely different in each part of the world and an entrepreneur will often have to operate within the parameters of all of them if launching a site/online business internationally. Concepts such as ‘fair use’, ‘free speech’ and the ‘right to parody’ are mentioned in a lot of the documentation but apply to the US only (and, even if a site is US-hosted, if it operates internationally it is hard to be certain that this US-specific leeway will apply in practice). This lack of an international copyright regime is perceived to greatly exacerbate the time cost involved in trying to understand it – which entrepreneurs and VCs claim distracts business founders from their core purpose (building the business) and thus restricts business growth.
- 7.21 Another issue that presents a risk to digital entrepreneurs is user-generated content. No matter how meticulous the business is in clearing rights where it’s self-generated content is concerned, there is still a risk of a copyright breach if user-generated content is a key component of a business model, as the business is regarded as the publisher of the content that users upload.





- 7.22 As a case in point, on the Blackburn Rovers fan site, users might copy and paste an entire news story or article from another website or a local newspaper, which is illegal. To tackle this they have vigilant moderators based in different time zones, to monitor posts around the clock. They also have 'alert' buttons to allow users to flag up any potential copyright breaches, and a programme of education of their users to encourage them to post links instead of word-for-word content. In the UK, even if the offending content is taken down a few hours later, this offers no defence. So they perceive this as a major risk to their business. The same applies to images uploaded as users' avatars in chat-rooms, although this is widespread throughout internet chat rooms, and no-one has so far clamped down on this.
- 7.23 Another (anonymous) technology entrepreneur makes users click accept on a statement, saying that they own the copyright or permissions for the material they are uploading. This ensures the user is legally responsible for the user-generated content. If there is a complaint, the site simply removes the material.
- 7.24 The digital entrepreneurs and VCs affected by copyright law claim a potential breach is very risky (relative to other risks when starting a business) as the severity of copyright laws mean one breach could finish a start-up business financially. The risk of a breach is perceived to be higher in the first couple of years of a digital business starting up, as new businesses are often run initially on a non-professional basis, e.g. from a student bedroom, and these nascent firms can initially be very naive about copyright.



## 8 Appendix: Case studies (qualitative summaries)

### Digital SMEs

#### **Martin Rigby, Psonar (psonar.com)**

An internet-based digital music business that provides users with music on-demand for a small fee for each individual play; and allows them to store and access their own music collection wherever they are. The 'pay per play' model of providing music on demand has not been pursued by anyone else before.

He has had issues with copyright law in relation to their service allowing users to store and access their own music collection. In the view of some copyright-holders in the music industry, this is tantamount to making an illegal copy as, in the act of uploading the music they own, the service user is effectively making a copy of it onto the Psonar server. There is a further issue with this, which has commonalities with other firms that deal with user-generated content: Psonar is reliant on the service user only uploading music that they legally own. Psonar relies on European 'safe harbour' laws to be able to continue to offer this service. He would like the UK law to emulate that in the US, where the DMCA and 'fair use' provisions allow users to make back-up copies of copyrighted material to which they have bought the licence as a consumer.

The fact that some copyright-holders in the music industry did not approve of the 'remote storage' element of their business caused them to actively decelerate the growth of this element of their business. However, a positive side-effect of this was that it prompted them to explore other models for generating revenue, which led to the 'pay per play' model: *"that got us motivated to set up the other business, so a barrier became an opportunity."*

#### **Stef Lewandowski, A-Frame (aframe.com)**

Online facility that allows people to make film, TV and other video content collaboratively via the Internet. It allows users to use the site as a means of storing centrally all of the high resolution files (more cheaply than buying an expensive server to store it on). It also acts as a means of indexing all of the video content to make it searchable. The firm describes itself as 'disruptively innovative', i.e. ahead of the game, in the context of a TV/film sector that has, so far, been relatively insulated from major changes in its business model simply due to the size of the files, where video content is involved.

He has had potential issues with copyright in relation to (in effect) user-generated content and orphaned works. When clients are working on (for example) a TV programme via A-Frame, they will upload the content to A-Frame's server. This can sometimes involve the client wanting to use unlicensed material that they have sourced. This means A-Frame has to guard against clients leaving unlicensed material on A-Frame's server (as often, this material is 'orphaned', i.e. it is difficult to establish with whom the rights to this material lie). They also have to be careful about clients leaving their own material on A-Frame's server, as after they've finished work on it the rights to their end product may have been transferred elsewhere (e.g. to the broadcaster who commissioned it).

He also has another issue with the current copyright regime: it costs a prohibitive amount for a small business to take a copyright breach to court, e.g. £20k to pursue a copyright complaint, and £500 to £1,000 for an order to take down copyrighted material. Thus, in their view, the ability to enforce the law, or to use lawyers to ensure that new ventures are properly licensed, tends to exist only for larger businesses, whilst the smaller entrepreneurs can neither defend their own rights, nor set up new ventures involving 'slightly borderline' areas of copyright (*"and slightly borderline is where all the interesting stuff happens"*).



He would like a culture like that in the US, of 'act first, ask permission later', because "*with most new ideas, you have a three month window before someone else thinks of it, so if you want to innovate you just have to do it and worry about the consequences later.*" Their own business benefited greatly from copyright holders being generous with granting them permissions when they were at their 'experimental' stage. He suggests that businesses should be free to experiment with material, and that copyright laws should only kick in when the commercial exploitation of the idea begins.

**Struan Bartlett, NewsNow (newsnow.co.uk)**

An online news portal that provides links to thousands of different online news reports, with constantly updated links. This can be tailored for business-to-business clients who have specific topics of interest that are relevant to their sector.

He has issues with the current copyright regime in that it is a 'grey area' in terms of whether they would be protected if someone chose to duplicate their own 'curation' of news content.

In providing links to news stories, they have to copy each story's headline in order to communicate to the service user what each story is about. It is also a 'grey area' as to whether copying a headline is substantial enough to be covered by copyright – in their view, they do not need to seek permission to do this but, whilst most news sources are pleased to be promoted in this way, a few have objected in the past. These instances have involved the use of lawyers by NewsNow and ultimately resulted in the removal of some news sources from the site, especially from their 'by subscription' business-to-business services. This has closed down the subscription services as an avenue for achieving growth.

The lack of clarity in UK copyright laws also means they have shied away from analysing and indexing the content of articles in full (as to do so involves – in effect – copying the article). This has prevented them offering improved functionality to service users.

He argues that, in a digital age, copyright laws are out of date, as the very act of indexing or viewing content online involves making a copy, which arguably infringes copyright laws. This leaves businesses operating in a 'grey area'. He believes that this lack of clarity leads to inequality before the law: the larger and better resourced businesses are better able to fight their cases than the smaller entrepreneurs:

*"Because of the lack of clarity in the law, it mitigates in favour of the most powerful players in the market – whether they are copyright holders like the large publishers or users of copyright material like the large technology companies – it seems that it is money that dictates who wins a copyright case and not clarity in the law."*

**Glenn Pegden, Blackburn Rovers Football Club Supporters Internet Site (brfcs.co.uk)**

An unofficial fan website and forum set up in 1996 and run as a not-for-profit enterprise, but part funded by donations and merchandising. They have good relations with the official club website and 5600 registered users.

Because of the growth of meta-reporting they report content from other websites and newspapers, but are careful not to lift content word for word. They have a good relationship with local and national papers, and are very careful to seek out permissions for potential copyright clashes. However, they have a problem with user-generated content in their chat rooms

Users might copy and paste an entire news story or article from another website or a local newspaper, which is illegal. To tackle this they have vigilant moderators based in different time zones, to monitor posts around the clock. They also have 'alert' buttons to allow users to flag up any potential copyright breaches, and a programme of education of their users to encourage them to post links instead of word-for-word content. In the



UK, even if the offending content is taken down a few hours later, this offers no defence, which they perceive to be as a major risk to their business.

The same applies to images uploaded as users' avatars in chat-rooms. Although this is widespread throughout internet chat rooms (pictures from The Simpsons etc.), no-one has so far clamped down on this.

They have had issues in the past with publishing the fixtures list on their website. This is copyrighted by the Press Association, and there is a fee chargeable, even for small not-for-profit fan sites. They decided in the end that it was not worth the money, and no longer publish it.

As a software developer in his day job, he is supportive of copyright generally, although believes it is very badly understood. He believes that his fan site goes out of its way to avoid copyright conflicts, but user-generated content is a threat that is difficult to contain.

### **Nico Perez, Mixcloud (mixcloud.com)**

Mixcloud is a website which hosts the music of thousands of radio creators, DJs and stations which can be listened to on demand. It is an access rather than an ownership model: music can be streamed but not downloaded. They are funded by advertising which pays for bandwidth, hosting and royalties to rights' owners. They are looking to launch a premium paid-for subscription-based service in the future.

They spend a lot of time and effort ensuring there are no copyright breaches in their broadcasts. They always seek permission to use content, but concede that in some circumstances this is not always possible (e.g. with 'mashed-up' sampled dance music). Their philosophy is that they are building a legal alternative to their illegal competitor platforms: they respect copyright and want to pay rights holders. This does come at a cost, however. They spend about £10,000 a year in lawyer fees, but reckon this is cheap considering the amount of work they do.

They would like to be able to offer downloading to their users, but the high rates for performance rights payable mean this is impossible. They feel they could have grown quicker as a business had they been able to offer this feature.

In general he feels that copyright restrictions do discourage talented people to start up businesses in the media space, because of the difficulties, costs and confusion over copyright. He also feels that investors steer away from these types of business because of potential complications. Most internet services are born global, and geographical restrictions such as differing copyright laws are a major barrier to innovation.

### **Levi Russell, Zonerider (zonerider.net)**

The software they provide allows private individuals and businesses the ability to share their broadband wi-fi with customers and other users, and get paid for doing so (users of the wi-fi service buy a subscription or use pre-paid vouchers).

They have had some experience of copyright infringement when they first started: their home page was in breach of copyright and they received a letter from lawyers. They dropped the offending images and eventually the matter was let go.

The main concern they have, which is shared by all providers, is the activity conducted in the wi-fi hotspots, which needs to be monitored. Although the current copyright laws do not pose a problem for them currently, he is of the view that big content holders hold the small operators to ransom, and obstruct their growth and development.

*"I know of companies that have stopped, or ideas that have not come to fruition because of copyright. We would have the same problem if patent law was like copyright, and marked in favour of big companies. If this was the case I wouldn't bother trying to compete."*



**Victor Henning, Mendeley (mendeley.com)**

Mendeley is a free reference manager and academic social network that helps to organise scientific and academic research, collaborate with others online, and discover the latest research. At the moment they are not making any money, but in future 'crowd sourcing' will enable them to generate research about research which is marketable. They have VC backing and are still growing, with 750,000 researcher users worldwide.

Copyright is a big issue for them. Individual databases are all copyrighted, e.g. to universities, and copies are not permitted. However, the moment anything is put online and shared it is effectively copied. For Mendeley the content creators and site users are usually the same people, who want research shared so that people can discuss it, but at the same time do not want their copyright infringed. So in this respect the UK copyright laws fail.

Mendeley can at least track usage and send the information back to the publishers, who tend to be favourable to Mendeley as they index publications (therefore effectively acting as search engines and advertising for these publications), but some people in the organisation fear that they might still technically fall foul of the laws.

If 'fair use' were adopted in the UK, it would assist their business. However, they also make the point that, to date, in both the US and the UK, DMCA has been the more relevant legal concept in guiding their approach to copyright matters.

*a "Even though our largest user base is in the US and we are DMCA compliant, we are uncertain if that would protect us if there were a law suit in the UK. We are operating in a sphere of 'tolerated uncertainty' of our legal situation – I would like certainty and clarity." (Technology entrepreneur, Mendeley)*

Mendeley do spend an amount per year on lawyers, about £2000, because of the uncertainty. Although they are a UK company most of their users are in America. They do have a US office for marketing and business development purposes, and have discussed whether it would make more sense to relocate part of their business there because the US is more web friendly.

**Anonymous**

An online magazine that makes money through e-commerce and advertising creates its own content, and therefore has to be very wary of copyright laws, e.g. if using somebody's music for a video. They subscribe to music, video and image libraries rather than going to the source, which is too time consuming and expensive. Even so they spend up to \$100,000 a year for these subscriptions. They use lawyers who they are on good terms with, and pay almost nothing, but recognise that normally they might be expected to pay up to £50k a year for these. They spend a lot of time researching and understanding copyright laws as they apply to them, which is very difficult and frustrating as the laws are so complicated, but they are careful not to break any laws:

*"The risk is so great compared to other risks. If you hire the wrong person you can always fire them. If you upload a load of songs on your videos that you're not allowed to it can financially kill you. It can kill you financially, or in terms of your operation because you need a few people to look into it each time. It takes a lot of man hours for something that isn't actually part of your business, which is particularly difficult right at the beginning when you're trying to get started. Copyright is a very daunting thing for a young company."*

Currently they do not allow user-generated content because of potential breaches of copyright, but would like to do this in the future. Nor are they able to use the very expensive material that they would like to use. They



recognise that content creators are entitled to be paid for use of their content, but still it does prevent them from creating better content themselves.

### **Christine Conder, Wraycom.com**

A charity, in partnership with Lancaster University Special Projects Unit, that promotes ICT – including provision of wi-fi access to a whole rural community of 500 users in 200 homes. If someone doesn't have a PC, they refurbish and provide an old PC in order to get them online; and they also provide an online centre in the village three days a week. They are currently installing a new network feed to provide faster internet access for the community.

She feels that copyright forces people to 'reinvent the wheel', For example, they have a website to promote their project. Ideally they would have taken a website template from another site that they admired, and adapted it – but copyright forces them to start again from scratch, thus creating work for them and – potentially – depriving the creator of the site they admired of kudos as a web designer.

Copyright also, in her view, restricts scope for creativity – for example, in making video content to promote the benefits of ICT, she will have to use non-copyrighted music, rather than the music that would best serve the content being created.

There are also issues with 'orphaned works': she often finds video content that she would like to incorporate into her own films but, having no idea of who it belongs to or how to obtain the rights to use it, she has to give such content a wide berth. In response to her own frustration at not knowing whether or not she can use others' video content, she has taken to putting a disclaimer in her own films, stating that she is happy for her content to be used by others.

As they are the wi-fi provider, they have a responsibility to their users to educate them as to what they can and cannot do – and this too encompasses copyright issues. There has been an instance of users using Limewire or Torrent to illegally download a game (kids who were ignorant of copyright laws) and another of a user illegally 'seeding out' a film to share it with others (adults who were not skilled enough with Torrent to switch off the uploading part of the program). In these instances they disconnect the infringers, educate them and check they have removed the offending download program.

She feels that sometimes instances of copyright infringement are for innocent reasons, e.g. someone sampling a film to check whether they want to go to the cinema to see it (so the download in effect acts as a trailer); or someone making a copy of something they own for someone else, akin to lending it to them.

However, once in the digital domain, what used to happen legally by passing an object around becomes illegal because of the act of making a copy. She feels that the current copyright regime is protecting outdated business models, and fails to recognise how the internet is used in a small community:

*"If I have bought it and want to give it to somebody else, why can't I? People want to share things, and they can if it is an actual book or a CD, [so] why can't you pass on copies of things digitally without it being illegal? This why people use Torrent... My overall views are that the Digital Economy Act is a total disgrace to democracy. I watched all the Parliamentary debates on TV...All their evidence is based on information from the music industry; they haven't listened to the views of ordinary people at all. They don't understand how the internet works on a community level... it protects an obsolete model of business based on the costs of vinyl objects."*



## Anonymous

A social website that is funded by advertising has few problems with copyright. Users generate content, but a disclaimer ensures that the user take legal responsibility for anything they post. If approached by a copyright holder they would immediately take down the disputed content, but this has yet to happen.

Their main experience of copyright law was when they were looking to use a database of a global events listing company. Because of complications with copyright they ended up having to deal with a few different companies instead. There was no huge delay because of this, but it meant they had to do a bit more work. They share the view that is held by others – that copyright laws need to apply globally rather than nationally.

## VCs

### Stefan Glaenzer, White Bear Yard

Venture Capitalists that specialise in investing in entrepreneurs in the digital space, with consumer-facing businesses.

He argues that the current copyright regime is out of date, as it is based on a business model in which copyrighted material existed as physical, rather than digital copies:

*“Take music for example. An average teenager today has an MP3 player on which you can store 50,000 songs. There’s no way that teenager spends £50k to buy music. The copyright law was working with me, when I had a long-player.”*

The copyright laws therefore no longer reflect reality, and are thus difficult to work with in practice, as the way in which the ‘old’ copyright model applies to the real world of today is open to interpretation.

A further problem is that there is no clear international consensus around copyright – the laws differ from territory to territory, which presents major problems for digital firms which typically launch online services in multiple territories from the outset.

He argues that this ambiguity leads businesses to steer clear of ‘grey areas’ in which it is unclear whether or not copyright would be breached, and that this ultimately inhibits innovation, by causing entrepreneurs to play it safe.

As a Venture Capitalist, this ambiguity also presents a problem when he is considering whether or not to invest in a start-up. If there is any doubt as to whether an entrepreneur’s business idea will infringe copyright, he will turn them down. He claims that he is presented with around 1,000 new business ideas a year, that 50-100 of these will typically involve copyright, and that 90% of those involving copyright are turned down due to the likelihood of experiencing copyright problems.

He therefore wants to see a move towards a clear global framework for copyright.



## Anonymous VC

A VC and digital entrepreneur, who has a large worldwide technology and software portfolio, is careful to check out copyright issues before making an investment. If a firm claims it has registered IP, this needs to be thoroughly checked, although it is the responsibility of the firm to do this rather than the VC. If a firm creates then they need to prove the worth of their IP, if they curate they need to prove they have the right to use the material they hold.

This becomes complicated with the creative industries. Digital art collections will need to prove they have the right to show every single work they have. For film and music the copyright terms can be extremely complicated and make it impossible to create a sustainable business model. More often than not, if the copyright arrangements in a business are very complicated, or if the business cannot prove it has the IP it claims it has, or the right to use someone else's IP then the VC will simply walk away. The UK copyright laws are particularly complex in these respects, and this deters investment.

*"I think that some VCs might look at the UK and see it as a less attractive environment in which to place a company because of the laws that exist. They may be better off placing that company in a different country where the laws are more clear cut."*

## Anonymous VC

Another VC and digital entrepreneur has a number of business interests, mainly in the creative industries.

With music you have to seek out other people's copyrighted material. If you want to play music you have to get the rights, either through statutory licences, or through individual negotiations with the rights holders (e.g. the publishers or record labels). The latter is a nightmare: time consuming and difficult, and even if you manage to negotiate a deal for a year the chances are that the cost will increase the following year. In the USA there is the DMCA (Digital Millennium Copyright Act) which has a set of rules as to what has to be paid, and what people can do.

*"Over here with statutory licences you have to negotiate with every label, every MD, every publisher, every year. And if they see that you're doing well, the next year they will come back and screw you for even more. In the end you just won't do it. The difference is, in the US they will have internet radio, and over here in Europe at some point probably not."*

It used to be easier in the UK but the terms of organisations such as PPL and PRS now make digital broadcasting of music economically unworkable. The advantage of US law is that it is much clearer, but it's not in the interests of any rights holder to have the system changed.

*"You would be bonkers to set up a company here (in the UK). For most businesses that involve any content you are much better off being in the States. It completely stifles innovation and destroys value creation. It's not accidental that gaming is the one industry where things have worked in the UK because there's no IP involved, but if you need to use someone else's IP it's almost impossible here. There's no incentive for the copyright owners to change, and there's no mechanism to experiment. Incumbents never want change."*





## 9 Appendix: Sample and business profiles

### Profile of SMEs in the SME Omnibus

9.1 The table below shows the unweighted (actually interviewed) and weighted (to be representative of all enterprises) proportions for the general sample of SMEs.

<b>Table 12: Profiles of SMEs in the SME Omnibus – size, turnover and broad sector</b>			
Base = All SMEs	<b>Unweighted</b>		<b>Weighted</b>
<b>Employment size</b>	<b>n=</b>	<b>%</b>	<b>%</b>
No employees	90	18	75
Micro businesses (1-9 employees)	185	39	21
Small businesses (10-49 employees)	142	28	3
Medium businesses (50-249 businesses)	83	17	1
<b>Annual turnover</b>	<b>n=</b>	<b>%</b>	<b>%</b>
Up to £250,000	50	10	33
£250,001 - £1 million	128	26	23
£1.01 million - £5,000,000	102	20	6
More than £5 million	70	14	8
<b>Broad sector</b>	<b>n=</b>	<b>%</b>	<b>%</b>
Primary/manufacturing/construction	110	22	32
Transport, retail and distribution	159	32	21
Business services	131	26	26
Other services	100	20	20



## Profile of digital SMEs

9.2 The following tables show the unweighted and weighted profiles for the 300 digital SMEs that were interviewed in the quantitative 'boost' survey.

<b>Table 13: Profiles of digital SMEs - sector</b>				
Base = All Digital SMEs		Unweighted		Weighted
2007 SIC	Description	n=	%	%
58.20	<b>Software publishing</b>	<b>99</b>	<b>33</b>	<b>27</b>
	<b>Other Digital Technology</b>	<b>106</b>	<b>35</b>	<b>40</b>
62.02	Computer consultancy activities	27	9	10
62.09	Other information technology and computer service activities	44	15	19
63.10	Data processing, hosting and related activities; web portals	35	12	10
	<b>Media Distribution</b>	<b>63</b>	<b>21</b>	<b>24</b>
59.13	Motion picture, video and television programme distribution activities	26	9	9
63.91	News agency activities	18	6	10
73.10	Advertising	15	5	3
77.22	DVD rental	4	1	1
	<b>Other</b>	<b>32</b>	<b>11</b>	<b>10</b>
47.91	Retail sale via Internet	10	3	3
61.90	Telecommunications activities	22	7	7
	<b>TOTAL</b>	<b>300</b>	<b>100</b>	<b>100</b>



**Table 14: Profiles of digital SMEs – size, turnover and level of innovation**

Base = All Digital SMEs	Unweighted		Weighted
Employment size	n=	%	%
No employees	82	27	76
Micro businesses (1-9 employees)	151	50	19
Small businesses (10-49 employees)	52	17	2
Medium businesses (50-249 businesses)	12	4	*
Annual turnover	n=	%	%
Up to £250,000	161	54	75
£250,001 - £1 million	45	15	7
£1.01 million - £5,000,000	30	10	2
More than £5 million	14	5	2
Level of innovation	n=	%	%
Disruptively innovative (have a product, service or business model that is substantially different from others)	98	33	23
Incrementally innovative (have a product, service or business model that others created, but built upon)	45	15	18
Non-innovative (neither of these)	150	50	57
Don't know/refused	7	2	2



## Characteristics of digital SMEs (sub-sectors)

9.3 The following tables give some more detail of digital SMEs in terms of their characteristics and innovation.

<b>Table 15: Characteristics of digital SMEs – by sub-sector</b>				
Base = All Digital SMEs	<b>All</b>	<b>Software</b>	<b>Other Digital Technology</b>	<b>Media Distribution</b>
n=	300	99	106	63
<b>Sales channels</b>	%	%	%	%
Direct to customers	81	82	82	77
Online e-commerce	24	23	<b>17</b>	31
Subscription/membership service	12	13	14	<b>2</b>
Through agencies	9	12	<b>14</b>	0
Through retailers	7	3	4	<b>15</b>
Hosting other people's adverts	7	<b>1</b>	19	6
Other	6	5	8	8
<b>Age of business</b>	%	%	%	%
Less than 5 years	15	<b>7</b>	17	13
5-10 years old	22	24	21	21
10-15 years old	30	<b>44</b>	32	<b>12</b>
Over 15 years old	33	25	30	<b>54</b>
<b>How founded</b>	%	%	%	%
Entrepreneurial new venture	86	90	<b>91</b>	<b>75</b>
Split from existing business	12	10	9	17
Other/don't know	2	*	*	<b>8</b>
<b>Turnover in the last year</b>	%	%	%	%
Increased	31	33	<b>39</b>	<b>14</b>
Stayed the same	36	40	34	<b>47</b>
Decreased	27	25	24	28
Don't know/refused	7	1	3	<b>12</b>
<b>Turnover in the next year</b>	%	%	%	%
Increase	40	<b>49</b>	43	<b>20</b>
Stay the same	39	31	42	49
Decrease	9	10	9	7
Don't know/refused	11	10	6	<b>24</b>
Figures in bold are statistically significant findings between the two groups * = a figure which is more than 0%, but less than 0.5%				



**Table 16: Characteristics of digital SMEs (innovation) – by sub-sector**

Base = All Digital SMEs	All	Software	Other Digital Technology	Media Distribution
n=	300	99	106	63
<b>Hold IP</b>	%	%	%	%
Yes	19	<b>28</b>	<b>10</b>	26
No	78	72	<b>88</b>	<b>65</b>
Don't know	3	*	2	8
<b>In the process of applying for IP</b>	%	%	%	%
Yes	6	3	6	4
No	93	97	91	96
Don't know	1	*	<b>2</b>	0
<b>Consider themselves to be innovative</b>	%	%	%	%
Yes	61	<b>71</b>	<b>69</b>	<b>41</b>
No	36	28	31	<b>54</b>
Don't know	3	1	0	5
<b>Level of innovation</b>	%	%	%	%
Disruptively innovative (have a product, service or business model that is substantially different from others)	23	<b>30</b>	<b>28</b>	<b>13</b>
Incrementally innovative (have a product, service or business model that others created, but built upon)	18	7	18	10
Non-innovative (neither of these)	57	62	54	<b>74</b>
Don't know/refused	2	1	0	3
<b>View on which innovation is most important</b>	%	%	%	%
Creative industry innovation	10	<b>1</b>	6	<b>29</b>
Digital innovation	12	10	<b>18</b>	3
Both equally	75	<b>88</b>	75	<b>63</b>
Other/don't know	4	1	1	5
Figures in bold are statistically significant findings between the two groups				
* = a figure which is more than 0%, but less than 0.5%				



## Profile of in-depth interview respondents

9.4 The table below profiles the participants in the in-depth interviews:

<b>Table 17: Profiles of in-depth interview participants</b>				
<b>Depth</b>	<b>Type</b>	<b>Activity</b>	<b>Agreed to be named?</b>	<b>Organisation name</b>
1	SME/Entrepreneur	Travel/leisure social network	TBC	
2	SME/Entrepreneur	Video collaboration platform	Yes	A-Frame
3	SME/Entrepreneur	Internet based digital music business	Yes	Psonar
4	SME/Entrepreneur	News portal	Yes	NewsNow Ltd
5	SME/Entrepreneur	Academic research-sharing site	Yes	Mendeley
6	SME/Entrepreneur	ICT charity	TBC	
7	SME/Entrepreneur	Football fan site	Yes	Brfcs.com
8	SME/Entrepreneur	Online video magazine	TBC	
9	SME/Entrepreneur	On demand radio	Yes	MixCloud
10	SME/Entrepreneur	Facility to allow owners of wireless networks to make money from others using them	Yes	Zonerider
11	Venture Capitalist	Specialist VC	Yes	White Bear Yard
12	Venture Capitalist	Specialist VC	No	
13	Venture Capitalist	Specialist VC	No	
14	Venture Capitalist	Generalist VC	Yes	Venrex Investment Management

