
29 Fixed book price

Marja Appelman

'Books are different.' This is a statement that was first used in support of a fixed book price agreement in the United Kingdom in 1962 (Barker and Davies, 1966). Books are one of the few products in our Western market economy for which the use of fixed prices, better known as resale price maintenance, is widely known. Defenders of fixed book prices emphasize that books are not merely economic products, but also a vehicle of culture. Economic characteristics of books include the cost structure, with high fixed costs and low marginal costs, as well as the fact that a book is an experience good (which can only be valued after consumption). Moreover, books are different in the way that each book has many close, but no perfect substitutes, which makes the market for books a case of monopolistic competition. These characteristics do not, however, apply uniquely to books. Why, then, do so many European countries know fixed book prices?

This chapter will show that fixed book prices could be an effective way to improve the production of a great number of quality books and the availability of books through an extensive network of booksellers. It is, however, an instrument that entails major disadvantages concerning the restriction of competition and of innovation (Internet). Moreover, there is no guarantee that publishers and booksellers will use the instrument in favour of cultural goals.

The effectiveness of the fixed book prices

The use of fixed book prices for books is widely known in the European Union: in 2002, ten out of fifteen countries use this instrument (EIM, 2001). Only Belgium, Finland, Ireland, Sweden and the United Kingdom have free book prices. Outside the European Union fixed book prices are rare. Systems of fixed book prices generally include all types of books, given a few exceptions for schoolbooks.

Governments of all the European countries have one or more cultural objectives, such as the promotion of reading or the production of a great deal of quality literature. To this purpose, subsidies are being granted to authors, publishers, booksellers and libraries. In countries using fixed book prices on top of the subsidies, the government also aims to have an extensive network of booksellers. Below I show that fixed book prices can indeed contribute to these policy goals.

Resale price maintenance

The effects of fixed book prices can be explained using the theory of resale price maintenance. The theory relates to a contract in which a producer keeps the right to determine the price at which the retailer sells the product (Mathewson and Winter, 1998). Under a system of fixed book prices a publisher determines the price at which all booksellers sell a book title to consumers. Resale price maintenance removes the possibility for booksellers to compete on prices, but price competition is still possible between different publishers and between different book titles. Although the expression 'fixed book price' suggests otherwise, it is important to know that the instrument sets minimum prices.

A publisher can use resale price maintenance to influence the retail margin of booksellers. This is possible because the publisher determines not only the price at which he sells the book to the bookseller, but also the price at which the bookseller sells it to consumers. The retail margin is protected because of the absence of price competition between booksellers. Resale price maintenance does not equalize the retail margin for all booksellers, because the price for which the publisher sells his books to the bookseller is still the result of negotiations between these two parties.

Use by publishers

Publishers can use the retail margin of booksellers as an instrument to increase sales. The higher the retail margin for a book title (read: the higher the marginal revenues of sales), the more attractive it becomes for booksellers to offer this title to consumers. Therefore the number of retailers who are willing to offer the book title to consumers will increase as the retail margin rises. Overstreet (1983) points out that this theory only holds when booksellers differ in their profitability, but the book market seems to meet this condition (Appelman and Van den Broek, 2002). In addition to this, Deneckere *et al.* (1996, 1997) show that publishers can use the retail margin as an instrument to promote the sales of larger amounts of a book title to booksellers in the case of uncertain consumer demand. Finally, in certain conditions, the use of resale price maintenance protects the margin of publishers, which increases their possibilities of financing the losses on unsuccessful book titles (cross-subsidies). The disadvantage of this is that it decreases the incentive for publishers to innovate and improve the profitability of their choice of manuscripts (Appelman and Van den Broek, 2002).

Use by booksellers

A favourable effect of resale price maintenance for booksellers is that they can use the protected retail margin on the high sales of best-sellers to

finance the losses on slow-moving books in stock (cross-subsidies). But this has the disadvantage – as with publishers – that it reduces the incentive of booksellers to improve the profitability of their choice of book titles in stock. Inefficient booksellers can also benefit from resale price maintenance because it protects them from price competition. The protection of inefficient booksellers may be positive from a cultural point of view, but the drawback of this is that innovation and overall efficiency are harmed when more efficient booksellers cannot use price competition to increase market share. International comparison shows, for instance, that book sales by Internet and alternative retail channels (such as supermarkets) are lower in countries with fixed book prices than in other countries (EIM, 2001). Finally, it will be a disadvantage for booksellers not to be free to lower the price of book titles for which there is little consumer demand. This reduces their willingness to keep those books in stock and can set prices of slow-moving books above market equilibrium.

Additional effects

In addition to the disadvantages of fixed book prices mentioned in general theory, namely inefficiency and higher prices, research in the Netherlands points out a few other disadvantages of the instrument (Appelman and Van den Broek, 2002). The first disadvantage is the lack of focus of the instrument as a means of reaching cultural objectives. It is used for almost all book titles, whereas the cultural political need for the instrument is often limited to unprofitable quality books. A second disadvantage of the instrument is that market players are not committed to using the revenues from higher margins for the benefit of cultural objectives. There seem to be quite a few publishers and booksellers in the market that hardly contribute to the cultural objectives, but concentrate on commercially interesting best-sellers instead. Finally, systems of fixed book price are often not restricted to resale price maintenance, but include other arrangements that result in an unnecessary additional restriction of competition.

Debates about fixed book prices

Publishers and booksellers can use fixed book prices to offer a large volume of books through an extensive network of booksellers. In this regard the instrument effectively contributes to this cultural objective of governments. But there are also important drawbacks. Fixed book prices are not restricted to quality books and quality booksellers, nor does the instrument obligate publishers and booksellers to use it in favour of culture and/or of consumers. Moreover, the agreement has important disadvantages concerning efficiency, innovation and prices.

Because of the mixed effects, the use of fixed book prices is often a topic

of debate, with changes in policy as a result. Belgium, the United Kingdom, Ireland, Sweden, Finland and Australia used to have private agreements on fixed book prices, but abandoned them. France did have a short period without fixed book prices, but restored the instrument. At the beginning of the twentieth-first century, Belgium and Ireland also contemplated bringing it back into use. Since the 1980s, the fixed book prices in France, Spain, Austria, Greece, Luxembourg, Denmark, Italy and Portugal turned from private agreements into laws. In most cases this was to escape from increasingly tight competition policy: the European Commission (2000) considers resale price maintenance to be a hardcore restriction under the Block Exemption Regulation. The European Commission has forbidden fixed book price agreements that affected inter-state trade, that is, the agreements between Austria and Germany and between the Netherlands and Flanders.

In Germany and the Netherlands, the fixed book prices are arranged by a private agreement. The private agreement in Germany (and until its abandonment also in the United Kingdom) differs from the fixed book price in other countries. While most countries have collective resale price maintenance (established either by law or privately), Germany has individual resale price maintenance.¹ In practice, publishers use resale price maintenance for almost all books, so that the effects of the two forms of resale price maintenance are almost the same.

The future of the fixed book prices

The attractiveness of fixed book prices lies in the fact that it enables market players to contribute to the cultural political objectives without any red tape or the risk of government failures. The negative aspects of the instrument relate to the restriction on competition – resulting in higher prices and reduced incentives for efficiency and innovation – and the uncertainty over whether publishers and booksellers will use the instrument in favour of cultural goals.

Considering current technological developments in the book market, the question arises whether in the future there will still be a need for policy instruments such as fixed book prices to reach cultural goals. For instance, the Internet is an efficient additional way to make books available to consumers and may reduce the need for an extensive network of booksellers. It could therefore be undesirable that fixed book prices reduce the possibilities of the Internet obtaining market share (see above). The reduction of the costs of printing books (especially the technique of printing on demand) and the possibilities of electronic books reduce the costs of publishing and might improve the profitability of (quality) books. Considering these developments, fixed book prices might become unnecessary and undesirable.

Alternative government interventions

If a government does not want to rely on technological developments to reach its cultural political objectives, but does not want to restrict competition with fixed book prices either, it has the option to use subsidies. Subsidies come in many forms: focusing on authors, publishers, booksellers and/or consumers. Countries such as Sweden and Finland use several types at a time. A fruitful option, not used in any country yet, would be to grant subsidies to booksellers who have a certain number of quality books available for consumers. Such an instrument could guarantee an extensive network of booksellers and the availability of quality books. Indirectly, those subsidies could increase the incentive to publish quality books. An alternative idea is to divide subsidies by means of a 'cultural contest' in which all market players are invited to participate. Market players who show that they are able to contribute to the availability of quality books qualify for a subsidy. This idea is known in other cultural sectors (for example, the performing arts in the Netherlands), but not in the book market. A negative aspect of all types of subsidy is the red tape it involves, although a clever design of the subsidy may limit this disadvantage. Other alternative instruments seen in countries without fixed book prices include lower (or zero) Value Added Tax on books (for example in the United Kingdom).

All the above-mentioned instruments to reach concrete cultural political objectives have advantages and disadvantages. Which alternative is best depends on the importance a government attaches to competition, avoiding red tape or having guaranteed cultural results. Regardless of these considerations, it is desirable to evaluate the need for policy instruments periodically, taking into account the favourable technological developments in the book market.

Note

1. With individual price maintenance a publisher can decide for every book whether he wants to use resale price maintenance or not. As a result, booksellers have the possibility to compete on prices for some books and have fixed prices for others. This has the advantage that some price competition between booksellers will remain. A disadvantage of individual resale price maintenance is its limitations for booksellers to contribute to cultural political objectives: the possibilities for cross-subsidies by booksellers for unprofitable books are limited, because publishers might not use resale price maintenance for potential best-sellers.

See also:

Chapter 51: Publishing.

References

Appelman, M.D. and A. van den Broek (2002), *Boek en markt: effectiviteit en efficiëncie van de vaste boekenprijs*, The Hague: CPB/SCP.

- Barker, R.E. and G.R. Davies (1966), *Books are different: an account of the defence of the Net book agreement before the Restrictive Practices Court in 1962*, London: Macmillan.
- Deneckere, R., H.P. Marvel and J. Peck (1996), 'Demand Uncertainty, Inventories, and Resale Price Maintenance', *Quarterly Journal of Economics*, III (3), 885–913.
- Deneckere, R. H.P. Marvel and J. Peck (1997), 'Demand Uncertainty and Price Maintenance: Markdowns as Destructive Competition', *American Economic Review*, 87 (4).
- EIM (2001), *De vaste boekenprijs; een internationale quick scan*, Zoetermeer: EIM.
- European Commission (2000), *Guidelines on Vertical Restraints*, Brussels: European Commission.
- Mathewson, F. and R. Winter (1998), 'The Law and Economics of Resale Price Maintenance', *Review of Industrial Organisation*, 13 (1–2), 57–84.
- Overstreet, T.R. (1983), *Resale Price Maintenance: Economic Theories and Empirical Evidence*, Washington, DC: Federal Trade Commission.