Italian Presidency of the Council of the European Union

International Conference

AUDIOVISUAL MARKET AND REGULATION: **AN INDUSTRY AT A CROSSROADS**

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Auditorium Parco della Musica – Teatro Studio Gianni Borgna
Viale Pietro De Coubertin 30 –Rome

REPORT

Foreword

On October 23-24th, 2014, the Italian Presidency of the Council of the European Union hosted the international conference named «*Audiovisual Market and Regulation: An Industry at a Crossroads*». The event has been organized by the Directorate-General for Cinema of the Italian Ministry of Cultural Heritage and Activities and Tourism and co-funded by the Creative Europe Programme of the European Union.

The Conference was aimed at encouraging a debate on a possible updating of the European regulatory framework concerning the audiovisual media services, which should take into due consideration the new media context. The debate has focused on the evolution of technological and economic context, on the role of the new players, as well as on the present and future business models and a possible review of public funding criteria.

The final outcome of the Conference is reported in this document, to be submitted to the Council of Education, Youth, Culture and Sport Ministers of the European Union (EYCS) to be held on 25 November 2014in Brussels. The document is intended to identify critical areas and to suggest updates and innovations to current regulations. The report will hopefully be also useful to detect opportunities offered by the current European regulatory system.

Two Sessions and a Follow-Up

The Conference included two Sessions (both held on October 23rd) and a Follow-Up and Open Debate (October 24th). The first Session was named «*New Business Models in a Changing Audiovisual Market*», and the second one was titled «*Public Support and Regulation Framework*». This report summarizes the outcome of the Conference as a whole.

Session 1: New Business Models in a Changing Audiovisual Market

This session was composed of a single panel on market evolution, as well as its new perimeter, as the outcome of the recent technological transformations and of consumption models in the digital single market. The analysis focused on how the digitisation process and the convergence of distribution platforms are providing a new framework to the entire value chain and to the development of new business models. Key topics:

1. main trends of the audiovisual market;
2. new business models: production, distribution, marketplace;
3. demand-driven strategies and new consumption models;
4. access to finance.

The starting point of the debate concerned the pros and cons of digitisation. We can summarize the pros in three points: a) new alternative production formats, b) new and alternative release and marketing strategies, c) larger consumption of audiovisual products. On the other side, we have some relevant drawbacks: a) audiovisual piracy, b) decreasing in theatrical attendance, c) fierce competition among products, platforms and between traditional and new players.

Keeping in mind the new business environment, the two market sides of demand and supply must be taken into account. The demand side concerns public and customers needs and their attitude, whereas the supply side relates to business and market sustainability. Both sides face a dynamic audiovisual worldwide market, whose main trends in the last five years (2009-2013) can be summarized as follows:

- EU market share down from 20,7% to 15,4%;
- US market share up from 59% to 68,8%;
- strong growth of four leading US Internet players;
- decline of physical home video market;
- consistent revenues from VOD market in the EU, in particular through digital subscription.

One important issue refers to the availability of data, and relates to the "lack of transparency" of the "new audiovisual markets", a frequent complaint along the entire conference. As a consequence, it is difficult to assess the actual situation and therefore the understanding of the real market dynamics and its trends.

Where the actual figures are available, it is important to observe a number of facts, related to the circulation of European works:

- we face in each European territory a dual economy: local films vs. US films, with scarce circulation of EU films;
- there is a progressive saturation of theatrical screens: in France, 400 movies released in 1996, 600 in 2013; in UK, 35 % movies released on less than 10 prints;
- the availability of movies in the various territories is uneven: 650 releases in UK, 200 in Sweden; 650 releases in Milan, 350 in Catania.

The above data emphasize the importance of new technologies of release, in a growing, global economy. There are €509 billion at stake: this is, according to the Motion Picture Association of America, the contribution of the EU core copyright intensive industries. This figure should be added to the 7 million jobs generated each year, although there have been 6 billion illegal downloading of films last year. The new distribution platforms absorb a large amount of bandwidth. In UK and Ireland, Netflix is the second-largest source of Internet traffic during peak evening hours; in North America Netflix's streaming service accounts for 34% of primetime Internet bandwidth usage.

On the demand side, the key words linked to the new digital world are: audience engagement; opportunities, quality of content, diversification, experimentation; complementarity, coexistence (symbiotic relationship); balancing between innovation and continuity; building communities, mixing media, intellectual property valorisation.

In particular, audience engagement becomes more and more important. Do we still know nothing about the audience? New technologies, through their algorithms, give easy access to the preferences of any single customer, but this information is available only to the big players. In other words– again – a lack of transparency (metadata) is evident concerning on demand audiovisual services and platforms vs. Big Data managed by global players. Customers, on their side, face both unlimited supply of product together with the illusion of choice.

The focus is on the audience; as a consequence, we see sophisticated demand driven strategies. This leads to the necessity of **creating "bridges" (connections) with young generations, building "interest based communities"** (e.g. Opera, Sci-Fi, Documentaries, etc.) – also by mixing media, adoption of new strategies to create value and reach audience and, necessarily, to bet on quality and diversification. We are witnessing the rise of cross-media products and new opportunities for filmmakers and local producers, and now producers need to structure their budgets in accordance to the specific release strategies. The competition among the new platforms is based on four key success factors: 1. branding; 2. convenience; 3. price; 4.collateral services.

The disruption of the "old" production business model will affect the competition among products, not only in terms of films and TV content, but including also, for example, the video-games industry. In fact, the new competitive arena is populated by new, innovative products, and includes the competition among different platforms: **we will need more cross-market analysis to assess the commercial potential of new releases**. The key question is: how much are audiences ready to pay for an extra value ?

The theatrical sector is suffering a decrease in attendance, and digitisation can be seen as a way to balance the limited circulation of European films, although the territory-by-territory release strategy remains problematic: positive with the blockbuster movies, lethal for independent, low budget, local films. One of the issues related to content access is the problem of the release windows. Some experiments have been conducted and the first results appear to be in favour of the shortening, towards a day-and-date **release on different**

platforms, although new and wider experimentations must be done to confirm the earlier findings.

In this fast changing world, every day brings us new business models and, for example, there are today new ways of collaboration among distribution platforms and the advertising sector to test innovative strategies. The approach, once again, is user-centred: Amazon e-commerce platform becomes a proactive player in production and distribution (Amazon Studios) in order to deal with users demand, providing the maximum freedom of choice with increasingly competitive pricing strategies. The so-called "Over-The-Top" (OTT) are leading the change, not without controversies.

What happens to the "old" industry? The development of the new on demand services is not considered in contrast with traditional broadcasting systems; in fact, those systems, boosted by the new consumption models, are testing non-linear stand-alone supply models (e.g. CBS, HBO in US; Infinity, Sky Online in Italy). **Actually, the competition between traditional and new players appears to be more a complementary relationship than a true competition; however, the evolution of this relationship must be monitored. It becomes fundamental, on the competitive ground, the role of policy makers and regulators in terms of level playing field**.

On the financial side, in a world in which public money availability is progressively shrinking, the **access to private finance is definitely a priority. From this point of view, the promotion of guarantee funds at national and EU level becomes a must.** Of course, this could lead to the need to consider financial intermediaries constraints.

The changes in the traditional value chain, with new players and new platforms, need a **rethinking of the pricing models**. To assess a fair distribution of the value created by the audiovisual works, transparency becomes essential, one more time, to avoid any inefficient allocation of resources and/or any rent seeking situation.

Another financial source, somewhat alternative, is the crowd funding, although we must be aware that it cannot work the same way for all products.

The main challenges for policy makers can be summarized in four questions, related to the sustainability of the new business models:

- may we experience shadow pricing models and unfair exploitation of author rights?
- May we experience strong price competition among OTT players, which will lead to mergers and high market concentration?
- May we experience OTT players facing the same advertising crisis broadcaster have already experienced?
- Which role for governments and EU to face these risks?

Session 2: Public Support and Regulation Framework

The second session focused on public support adaptation to the new market shape, including the issue of complementarity between EU and national/regional support policies. Therefore the discussion has been about the update of supranational, national and regional regulatory frameworks, according to the new business models and the economic impact of new entrants in the market.

The main points covered in session 2can be grouped in three areas:

1. production and remuneration of audiovisual content;
2. financing of audiovisual content;
3. regulatory needs and possible perspective.

The starting point of the whole discussion has been centred on «Cultural Values and Economic Goals», which represent the dual aspect (Culture vs. Economics) of the audiovisual industry. The cultural exception principle and the most important international treaties have been recalled, emphasizing the effort of the EU in **fostering cultural diversity** via new rules (e.g., Regulation no. 1295/2013, establishing the Creative Europe Programme 2014-2020). A great support to European citizenship is (should be) played by Public Broadcasters, whose role remains pivotal in the industry, through the right balancing between production and circulation of cultural content and the economic sustainability of their mission.

Another fundamental issue, related to the regulation of the industry, concerns the remuneration of authors and, consequently, the incentive to creation. According to the authors' view, there are specific challenges in connection with their remuneration: a complex and long contractual chain, which prevents their remuneration flowing back to them; the need to **develop new mechanisms to allow audiovisual authors to be rewarded for the success of their works**; the proposal to implement a system of collection of the remuneration for the use of their works at the final distributor level, to lighten the burden on producers.

There is not industry without funding. The production companies rely on public support, co-production, pre-sales (from broadcasters and distributors) and private investors. **A growing source of funding across Europe (and the rest of the world, indeed) consists of the numerous fiscal incentive schemes supporting film and audiovisual production.** There are three main instruments: 1.tax shelters: investments as a means to reduce tax liabilities for high tax-paying companies (Belgium, France, Ireland); 2. rebates: an amount of the qualifying production costs is refunded by a State budget (Germany); 3. tax credits: similar to rebates, but can result either in a reduction of tax liabilities or, if no tax liability is due, in a cash payment (France, Italy, UK). Unfortunately, an accurate analysis of fiscal incentives is difficult, due to the lack of comparable data, therefore making the benefits of the incentive difficult to prove. The exam of available data shows a significantly higher production activity in those countries which have incentives, which determine positive effects in the short term, but in the long term need to be coupled with other measures, such as investments in infrastructures, skills, etc. The tax shelter has the advantage to provide cash flow during production; however there has been some movement away from a tax shelter model, because it is less transparent and has historically seen abuse.

More efficacy and efficiency is definitely an issue. From this point of view, once again the role of Public broadcasters is central: the success of TV series produced by them is a driving force, both in terms of funding and editorial input.
At the same time, although many OTT players do not fund the production of content, some of them are just starting to invest in production of content and this may create, for the future, an unequal treatment between players operating according to different models: "strongly distribution oriented", "strongly production oriented" and "cross production and distribution oriented". In fact, the level playing field is a much-disputed point in the industry. The question is: «**Do Audio Visual Media Service (AVMS) providers and OTT Internet services offer similar services under different regulation**»? The differences are quite evident (Table 1)

Table 1

	AVMS	OTT[1]
Editorial responsibility	Yes	Ex post liability
Advertising limits	Yes	No
European content quotas	Yes	No
Etc.		

A speaker proposed, with regard to VOD services, that the liability should rest on "gatekeepers" (i.e., operators providing access to content).

Emerging issues and future actions

In general, do we need brand new rules for a new landscape? The ongoing discussion covers a number of key matters: 1. the "**country of origin principle**" in the new audiovisual ecosystem (although according to the Commission, the aim of the Directive to create a single market has been achieved thanks to such principle); 2. the EU **content quotas** (More relaxed rules for linear services? Full **harmonization or flexibility** (more stringent rules for VOD?) 3. **release windows:** still valid? 4. Avoid **unnecessary burden of regulation**.

It is important to note that the questions on territorial and material scope of the Directive are also discussed within ERGA, the European Regulators Group for Audiovisual Media Services, which, as we know, brings together heads or high level representatives of national independent regulatory bodies in the field of audiovisual services, to advise the Commission on the implementation of the EU's Audiovisual Media Services Directive (AVMSD).

[1]Reference is made not to all OTT players, but only to those who do not fall within the scope of the AVMS Directive.

The main challenges for policy makers can be summarized in six points:

1. the management of data is the key of success: transparency issues cannot be postponed;
2. the differences in the implementation of the AVMSD among Member States should be reduced to a minimum, if not cancelled;
3. a decision about the regulation of those OTT services not already under the scope of application of existing rules must be taken, to level the playing field;
4. fighting illegal downloading and streaming with both education and deterrence;
5. forms of cooperation among players based in different Member States should be enhanced;
6. the production of works with strong chance of international distribution should be favoured.

Participants

The Conference got the participation of:

- the main players of the sector (Amazon, YouTube, and BSkyB);
- the representatives of the main European and International institutions and associations in the field;
- representing the institutions: DG EAC and DG Connect of the EU Commission, EU Parliament;
- representing the associations in the field: ACT (Association of Commercial Television), Cine-regio, Digitaleurope, EBU (European Broadcasting Union), European Producers Club, ERGA (European Regulators Group for Audiovisual Media Service), MPAA (Motion Picture Association of America), SAA (Society of Audiovisual Authors), as well as European Audiovisual Observatory, academics and leading experts in the field.

The position of the Italian industry was depicted by the representatives of the main firms and associations in the field.

Italian institutions were represented by Mr. Dario Franceschini, Minister of Cultural Heritage and Activities and Tourism, and Mr. Antonello Giacomelli, Undersecretary of Ministry of Economic Development.