



Executive Summary

Elektronische Medien

Entwicklung und Regulierungsbedarf

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Purpose of this Report

The media scene is in a state of change, even of upheaval. The telecommunication, broadcasting and internet branches, formerly distinctly separate, are now merging into an entity. Because of the triumph of the internet, services, whether they be based on language, on data or on videos, can now be transmitted in data packets to all technical platforms and into all nets. Terminals of all kinds are potentially multi-functional. Convergence is the word of the day. Publishing houses cooperate in internet with broadcasting companies; cable network operators acquire the rights to the matches of the German Football League and internet search engine operators have Hollywood films on offer. However when three communication branches merge into one, questions must arise as to the nature or scope of future markets. At the moment politicians are trying to predict the future developments of these markets and to identify the prevailing trends, so as to create the appropriate legal provisions where they are needed. The most important task of this report is to support these efforts and plans. The report reveals the complex changes in the media scene and makes recommendations for a viable regulation framework.

The analysis begins with a comprehensive economic inventory, in which the services and terms offered by the firms operating in these branches are described, and the behaviour of the media consumers are analysed. Continuing from here a comprehensive view of the regulation framework existing at the present time is given. It soon becomes clear that the development towards convergence is reflected in those areas where the laws governing media, telecommunication and cartels overlap. In Part Three of the report, possible scenarios of the economic development in this field are presented. The legal regulatory options in Part Four show various possibilities, as to how future developments and new problems arising from these changes could be dealt with by legislative means.

The comprehensive inventory of the German market for electronic media and of its complex regulation framework in Part One and Two of this study has in many parts the function and character of a handbook. Therefore only Part Three, the important economic development scenarios, and Part Four, the recommendation of regulatory options, will be summarised here,

Development Scenarios

Method of Approach

In this report, the economic evaluation of the media sectors offers a viable basis on which to form the legislative specifications and norms of the future. Politicians must orient themselves in their decision-making to the one criteria; which regulatory option generates the highest welfare for the German consumers. Such a criteria is also used by the European Commission as a basis for its measures.

The methodic foundation of the development scenarios is the “more economics based approach” used by the European Commission. Postulated is that consumer welfare, according to the common goals agreed on in the EC contract, is the target to be aimed at. Accordingly the consumer is the centre of attention. However the consumer point of view is not the only one of importance. The assessment itself is an effect-based economic analysis. Therefore market performance is judged to be compatible with the collective rules of competition market performance, if its effect is beneficial to competition. If the results of an action or transaction are prejudicial to competition, it can be assumed that they are also prejudicial to consumer welfare.

New Value-Creation and Regulatory Models

Current developments – digitalisation, convergence, user perspective and new business models – can no longer be represented as a two-dimensional sequential value-creation chain. Therefore in this study a new value-creation and regulatory model has been developed. In these times of convergence the value-creation model evolves as a spiralling, cyclic sequence, determined by formal as well as informal relationships between the various companies. The underlying logic of this model, characterised by reciprocity and no longer sequential, results in a value-creation system, which consists of different levels or **layers**, connected with each other, depending one upon the other, in which different, separate value-creation activities are carried out in a parallel chronology. Derived from evaluative analysis in the scientific world, this value-creation model in the new convergent media world may be defined as a **Business Web**.

Business Webs are defined as groups of companies which, independently of each other, produce value-creative components which enhance and complement each other. The market successes of the companies are interlinked with each other, since the consumer obtains the integral problem solutions, but he only obtains this through a system product which was generated within the whole value-creation net, and which had to gain market acceptance over competing products. In a Business Web two strategic roles can be established: (1) the **Shaper** who controls the core or central subsystems, in which the information flow of the value-creation systems are concentrated, and who determines the strategic development of the Business Web through the coordination of other subsystems on a meta-level (for example, with the help of information on interface standards); and (2) the **Adapter**, who creates the complementary products. These roles can be differentiated according to the degree of internalisation between Shaper and Adapter, and according to the duration of the relationship.

These developments in the value-creative chain have given rise to an adaptive, parallel development of the **regulatory** market model. The paradigm shift to a **Layer Regulatory Model** is also perceivable on the international market. This Layer Regulatory Model is grounded on the assumption that in a future IP based world there will, for example, in communication no longer be a differentiation between speech, data or video, fixed or mobile networks, or in services between local, regional or international levels, and that instead these services will be assimilated into the several grades of the **Layer Model**. This model differentiates between the two layers 1) **Content Generation**, 2) **Content Processing**, Service Provider and Network Operator. The two layers of Service Provider and Network Operator are then attached to the third layer, 3) **Content Distribution**. Reception of the content through the user completes this model, whereby the 4) **Content Presentation** which is necessary for this reception is effected through the appropriate terminals. If we use this Layer Regulatory Model as a basis, we can identify a string of **problem areas**, which will be relevant in the future terms of competition, and which can be evaluated from the perspective of economic competition in five scenarios.

Scenarios for Media Development

° Scenario 1 - Content Generation and Processing: The future Structure of the Media Organisation and electronic Press

In the first scenario, the problem areas of the electronic press are dealt with. The problem areas depicted show clearly that it is difficult to create a competitive environment comparable to that of the print press, when we take into consideration the existing regulatory conditions and the developments which are becoming apparent. The press is demanding the creation of an Identical-Level-Playing-Field for the print press and the electronic press. The unequal starting positions of the players create **tension**: Publishing houses market contents financed through advertising. On the other side, the public service broadcasting companies, which can create ad-free information sites financed by rates and fees, are now entering the market. Also coming into the market are the big, financially powerful **search engines from the USA**, which in the fashion of a news-broker provide the consumer with newest articles of the online press, sorted according to the topics covered.

One of the most important questions which must be considered in this context is that of a **transposition of the ethical principles of journalism into the online world**. There is a danger that these ethical principles will lose their meaning or become less important in the online press editions. This cannot be in the interests of the German citizen. Because in the online sector the relative advantages in competition are anything but homogeneous, under certain circumstances it will be necessary to **construct proactive framework requirements** in order to remedy this.

An extension of the print press self-regulation to all online providers or the inclusion of the electronic press into the broadcasting regulations could be considered. From the point of view of the consumer it would be more advantageous to **extend the print press self-regulation to all online providers**.

° Scenario 2 for Content Generation and Processing

In the second scenario the development possibilities of the public service broadcasting companies will be discussed. Two options are open: the public service broadcasting companies develop into multimedia companies in response to changing consumer preferences, or they persist with their current offers. According to the more economics based approach, we will first consider whether a **market failure in television** is probable. It has been ascertained that the supply of television services financed through advertising does not result in an optimal market performance. We therefore assume market failure. The economic reasons for this assumption are given in detail. This market failure persists on into the internet. There the characteristics of market failure can be observed as well, in part even intensified. If the public service broadcasting companies transfer the content they offer into the internet, this can only be regarded as a positive move from the economic point of view. These contents were created to counteract the **market failure of broadcasting** and they can be used and re-used at will (even if only by a small number of consumers). Such a distribution implies a positive effect for the community and for the individual. However we are still of the opinion that, even taking the new web-based offers into consideration and applying the Long Tail Theory, we must assume a market failure for broadcasting. **Public service broadcasting companies have the option to expand their activities and mutate more and more to multimedia companies. From the consumer point of view this can only be viewed as positive.** In the eyes of the legislator, the deciding factor is the consumer point of view which is expressed by the **evaluation of consumer welfare** according to the more economics based approach. Therefore the economic analysis is an argument for putting the contents of public service broadcasting companies into the online sector as well, so that they can reach the consumer wherever he wishes to make use of them.

° Scenario 3 – Content Generation and Processing: Private Free TV Providers

In the third Scenario, the future development of private free TV providers is discussed. The economic analysis leads us to the conclusion, that the market – if we set out from the premise that **a dual broadcasting system is in the interest of the German citizen** – cannot reach any result which would be advantageous to the consumer. The private free TV stations are confronted with a problem whenever they are **threatened with** or subject to **the loss or reduction of their advertising income**. Right such a development is becoming apparent. The business model of private free TV providers is confronted by three major challenges:

° the increasing fragmentation of the consumer market

° the increasing intensity in the competition for advertising clients, combined with a change in the basic economic principles, and

° the participation of investment funds, which could lead to a change in the behaviour of the private provider.

As a result of these challenges, there is a risk that **the public value which is generated by the private free TV provider at present could dwindle**. From the consumer point of view, intervention by the state in the form of **incentives** would be **ad-**

vantageous: the private free TV provider should receive incentives to create public value.

° Scenario 4 - Content Distribution: Vertical Integration of the Access Providers

In **Scenario 4** the vertical integration in content distribution is the central theme. It is preceded by an analysis showing that, presuming technology neutrality **from the point of view of the end-consumer, access networks will switch away from digital cable and digital satellite**. A diversity of transmission routes on the level of the end consumer will tend to discipline the natural monopolies on the preparatory performance level. As well as this, channel simplification, resulting from digitalization, also solves the problem of capacity scarcity. From the economic point of view this means it is **not necessary to take regulatory measures in the form of must-carry-rules for transmission routes**, as long as they have an adequate programme capacity at their disposal.

Afterwards we consider whether the discussion centred around net neutrality is (already) opportune in Germany. In this context we discuss a possible shift in the power balance in favour of the content provider, a shift which could be linked to the demand for a **must-offer** ruling.

The scenario itself covers the theme of **vertical integration**. In accordance with basic economic principles, we describe the advantages which arise out of vertical integration. This evaluation can change if **market power** concentrates itself **on one of the marketing steps**. In such a situation a vertical integration can lead to behaviour restrictive to competition. This type of vertical integration would have to be **investigated as an individual and isolated case**.

° Scenario 5 – Content presentation: Regulation of the last Metre

The problem areas described in Scenario five with regard to content presentation make it clear that under certain conditions the market can develop in a way that threatens competition. From an economic point of view, the problem areas of content presentation, which could be defined as “bottlenecks on the last metre”, can be very problematic. Experience shows that the probability of a development of such market conditions is pretty high as well. When we evaluate the options, from **the consumer point of view, a guarantee of interoperability and compatibility, as well as non-confidential standards and licensing**, would be the **best solution**.

The economic analysis is orientated towards future development and is more far-reaching than the judicial analysis. It is a matter of experience that the legal system adapts itself in the course of time: in the end legal specifications orient themselves towards the wishes and the values of society.

Regulatory Options and Recommendations

Methodological Approach

Based on the economic and judicial inventory as well as the economic development scenarios, regulatory options are discussed and evaluated in the fourth part of the study. The account orientates itself towards the Layer Model developed from the economic perspective. In addition the five scenarios of the development of the media scene are discussed. The judicial analysis however must take into account the framework of European and constitutional law. In this case the objective of consumer welfare no longer stands alone as the central concern of the regulatory decision-making. Even more important are the objectives of the **diversity of opinion** and the **protection of competition**. Partially the study proposes ready-formulated regulatory recommendations which are meant to demonstrate how the economic necessities can be addressed, while taking the the verdicts of the Federal Constitutional court and the guidelines of the European subsidy laws into consideration at the same time.

Guidelines for Content Generation and Content Processing

The future Forms of Media Law and Electronic Press

In the future forms of media law a graduated content regulation is appropriate. Therefore the Länder should continue to expand the existing graduated content regulation which has already been established in the Interstate Treaty on Broadcasting. The telemedia however should only partially be included in this contract and the regulations should be more relaxed in their case. The embodiment of these graduated regulations should be orientated towards the new guidelines for audio-visual media services. This presupposes a differentiation between **(classic) broadcasting, broadcasting-similar telemedia**, which qualify for the graduated, more relaxed regulation in the Interstate Treaty on Broadcasting, and **other Telemedia**, which are excluded from the application area of the Interstate Treaty on Broadcasting. Other telemedia particularly includes the electronic press, which should be regulated by press laws, especially with regard to the laws on self-monitoring. Finally the model for self-regulation, established in the State Treaty on Youth Protection in Media, should be retained, since it has obviously proved its worth.

The Mandate of Public service broadcasting companies

In the light of Germany's acceptance of the specifications of the European commission with regard to state subsidies, the mandate of public service broadcasting companies must be defined more clearly and precisely. This does not refer to the general programme functioning, which in the opinion of the Commission has already been codified with sufficient exactitude in § 11 Para.1 Clause 2, Para.2,3,4 RStV.

With regard however to the additional digital TV programme and to the telemedia, its mandate must be defined more precisely in many respects, not only on the point of legal procedure but also of substantive law. For the additional digital range, the mandate must be further substantiated by a strict concentration on information, education and culture through **exemplary programme categories**. In addition to that the state treaty must contain an obligation for the public service broadcasting companies sta-

tions to develop a programme concept in reference to these programme categories in future times. In the state treaty the function of telemedia for public service broadcasting companies must be limited to offering journalistic and editorial material. Furthermore the future state treaty must provide criteria as to the purpose which these offers are to serve. For example, these criteria would include enabling all sections of the population to play a part in our information society; creating adequate access to its offers for minorities; familiarising the public with the uses and advantages of the new digital offers; providing reliable and trustworthy orientation guides in the new digital services; promoting media competence and supporting broadcasting programmes as far as the continuous changes in media make this appropriate. Finally the State Treaty or the ordinances and regulations of the broadcasting stations must contain an exemplary list of telemedia which regularly put into practice the mandate of public service broadcasting companies or which do not, in accordance with Germany's assurances. In order to implement this requirement, an altered § 11 can be incorporated into the State Treaty on Broadcasting.

For new or modified additional digital channels as well as for new or modified telemedia offers, a test method which could be termed the **Three-Step Test**, has been introduced as the appropriate legal procedure. For additional digital television programmes, this test is, through an amendment of § 19 RStV, no longer obligatory if transparency has been ensured by an itemised list of all broadcasting programmes transmitted by the public service broadcasting companies. In this case however, the introduction of a new broadcasting programme or a significant change to an already existing programme is only possible when the State Treaty is altered with an appropriate addendum. If the Länder choose this policy, the test procedure need only be applied in the field of telemedia. If successful, the proceeding ends in a renewed inspection and verification by the Länder in their function as legal supervisory body. It is up to the legislators of the State Treaty to determine the criteria as to when such a procedure be implemented and as to the general pattern of procedure. The public service broadcasting companies should then concretise these criteria in their statutes and regulations. As to the question whether the offer is new or simply altered, the extent to which this offer affects consumer and market participant is decisive.

To implement the Three-Step Test, a process involving extensive activity in the field of search, finding and examination is necessary, a process which the internal members of the company's supervisory committee would hardly be capable of without expert help. Therefore we recommend that, at the very least, **experts should be consulted** to consider the market-relevant repercussions and to make allowances for these repercussions in the decisions taken by the broadcasting commission. An **alternative** would be set up an **advisory expert committee**, which would assess the market-relevant repercussions of a new or an altered project within the Three-Step Test, especially at the second step. This expert committee would function as advisory organ for all broadcasting and television councils, which are then obliged to take into consideration the committee's assessment of the market-relevant repercussions in the decisions they make. It is the business of the television or broadcasting council to assess the medial interests and to take into consideration all points of view. In addition the broadcasting council should be obliged by the State Treaty to give attention to third party opinions before its decision is reached,. To make this possible, it is necessary to publish a description of the proposed project and to provide for an **appropriate period of time in which these opinions can be put forward**. After the project in planning has passed the three-step test , the State treaty must stipulate

that it then be laid before the **Judicial Supervisory Body (Rechtsaufsicht)**, together with the self-monitoring agreements and the explanatory statements. The Judicial Supervisory Body then checks whether the project, together with the self-monitoring agreement, is consistent with the legal mandate, and comes to a decision. A statement of the self-monitoring agreements and the decision of the judicial supervisory body is then published in the official press of the Länder.

In addition to this, taking into consideration Germany's assurances in the negotiations over subsidies, it must be assured that in future State Broadcasting Treaties **purely commercial activities**, such as advertising, sponsoring and merchandising, will only be carried out by legally autonomous subsidiaries, i.e. that there will be a **separation between public mandate and purely commercial activities**. In addition the regulations should stipulate that such activities may only be carried out under market conditions and that they be kept apart from the other activities through separate financial accounting. In addition new regulations regarding investment are planned, orientated on § 36 SWR-State Treaty. Finally guidelines which correspond to those in § 30 ZDF-State Treaty should be adopted, providing for a standardised right of inspection of all subsidiaries by the audit courts.

Based on the decision of the First Senate of the Federal Constitutional Court, dated 11. September 2007, an obligation exists to examine whether, and if so, to what extent, advertising and sponsoring are still being permitted in public service broadcasting companies. The Länder should fulfil this obligation. A short term possibility would be to **forbid (on the air) sponsoring by public service broadcasting companies**. **On the middle term** the Länder should aim for a **funding only from fees and licences**. However the fees which would be necessary after such a renunciation of sponsoring and advertising would have to be ascertained in a procedure, in which the state has neither voice nor influence. So far the KEF has calculated that giving up the revenues from sponsoring would result in an 18 cent increase in monthly licence fees per subscriber, and those from advertising an increase of 1,24 Euro.

What the Law requires from Private Broadcasting Companies

The retention for the most part of the status quo, together with a system of incentives, could be advised as a realistic and appropriate option. However, a remuneration from the state for the implementation of private programmes with public value is a form of incentive which is unacceptable. It is already judicially possible to **include the media-relevant markets into the laws safeguarding plurality in broadcasting more effectively**. If we take into consideration the media convergence which is becoming more and more apparent, it would also be advisable to do so. Communication and cooperation between those different institutions controlling the media market should be enhanced by a judicial regulation of procedure.

Specifications for Content Distribution

Must-Carry Regulations for privileged Content-Offers

The must-carry regulations have only recently been extensively updated by the Tenth Amendment to the Broadcasting State Treaty. Therefore there is no need at the pre-

sent to change them. The evaluation planned for 2011 will show whether or not the existing regime should be changed. At that time the question as whether additional securities are necessary for basic packages will also be decided.

Transmission Entitlement with Regard to Monopolistic Network Operators

A separate transmission entitlement for content providers to be enforced against network operators does not appear necessary in media law at the moment. It would be better to wait and see whether the transmission entitlement derived from § 42 Abs. 1, 4 Satz 3 TKG can cope with the emerging threats to diversity and fair competition. In this field the Federal Network Agency (Bundesnetzagentur) as well as the State Media Authorities (Landesmedienanstalten) should develop **effective procedures of coordination, including appropriate division of labour**, which should take as example the procedure developed as a response to §§ 48 ff. TKG, 52c RStV (network surveillance instead of uniform regulation).

Content Access

At the moment a must-offer ruling, which enables access to media contents for all consumers under identical conditions and at identical prices, must be rejected. A sector-specific limitation of exclusive marketing of premium content does not seem to be necessary in these days. In this case the **provisions of the antitrust laws** are sufficient.

Content access will play a central role in task of protecting diversity and fair competition in the coming years. We recommend however to keep this field under constant observation, so as to identify possible deficits and to decide on future legislative and political procedures to remedy them.

Net Neutrality

A **comprehensive regulation of the problem** of net neutrality, as it is very vocally demanded in the USA, is **at the moment unnecessary**. The potential threat to the goals of competition and diversity has not yet been adequately sounded.

The fact that the European Commission wishes to ensure an increased transparency in their recommendations of TK-Review is to be welcomed. Furthermore it wants to set specification for the quality of services to reduce discrimination in this field even further.

Structural Specification as opposed to vertical Integration

A structural or functional separation does not seem advisable at the moment. The threat of monopolistic network operators who might employ “Monopole annuities”, and thus clandestinely subsidise their content acquisition, is no longer to be feared if they are subject to remuneration regulations. Additionally the law on telecommunications already offers the possibility of arranging separate accounting. The Federal Network Agency should in this field cooperate very closely with the State Media Authorities (Landesmedienanstalten). Only if these instruments have been proved to be

ineffective, the introduction of a separate media-specific transparency ruling (e.g. with regard to the conditions governing uploads) should be taken into consideration.

Access to Frequencies

In the next few years the use of frequencies, reserved until now for radio services, will be the subject of intense discussion. As the result of international specifications, an alternative use, e.g. by the mobile phone industry, would be feasible at the earliest in 2015. The European Commission is trying to hasten this process by the means of suggestions for using the financial potential of the digital dividends, but whether it will succeed is not clear yet. In the Federal Republic of Germany there is already an intense discussion as to whether and, if so, how far broadcasting – especially in the case of a distribution in an HDTV standard – must at all be dependent on terrestrial transmission. Users of wireless techniques must demonstrate the advantages which can be gained by allotting them the spectrum in question. Decisive in this point will be the question as to whether they can successfully **supply rural regions with broadband internet applications**. The Munich Circle could offer a forum here, to promote the necessary community discussion.

Specifications for Content Presentation

Technical Services relevant for Access

The existing regulatory approach (§§ 48 TKG, 52c RStV) has proved its worth in the eyes of the authorities. This is also true for the coordination procedure between the Federal Internet Agency and the State Media Authorities (Landesmedienanstalten). Instead of the uniform regulatory model, there is an intensive cooperation and division of labour between the two agencies (**interlinked Supervision Model**). The legal security hereby obtained counts more than any pressure towards change. On these grounds the existing access specifications should not be changed by now.

In future it should be assessed whether a review under media law as well as the review under telecommunication law is necessary and, if so, what aspects should be reviewed. Also the effect which the recent extension of the specifications in media law have on all platforms should be set out. Moreover the coordination procedure between different authorities should be thoroughly checked for practical feasibility.

Access to Orientation Aids

In the field of navigators and electronic programme guides, the regulatory approach which has been used so far has proved to be appropriate. The general principle of freedom from discrimination is guaranteed in the State Treaty on Broadcasting. The State Media Authorities (Landesmedienanstalten) have given this substance in the statutes and ordinances of the Joint Position on Digital Access.

Commercially operating internet search engines offering information and orientation already exert an enormous influence on all areas of life. It is the legislator's duty to take the necessary precautions to curtail this excessive influence and to protect the

diversity of information and orientation. At the present it does not really seem advisable to transfer the existing legal precautions for navigators and EPG's into the field of internet search engines though. However, if the consumer comes increasingly dependent on search engines in his selections from the range of broadcasting offers, the legislator should consider the possibility of transferring the regulations also into the field of these orientation assistants. **New directive methods and procedures should be developed if necessary.** It is advisable to investigate just how far the existing obligations to self-monitoring and to transparency can be included into this regulatory concept. Very soon though, the first steps will be taken in the development of a **public-service orientated search engine** for broadcasting offers and for high-quality media offers. It remains however to decide whether this task should be entrusted to the, public service broadcasting companies or to a new (for this task specifically created) Public Service Publisher.

Media Supervision

The creation of a "Federal Media Institution" as one of the highest public authorities, or as an institution of public law, responsible for all electronic media, including broadcasting and other services, as well as telecommunication, is constitutionally out of question; the constitution provides for separated competence in the media field. On the other hand, if the status quo could be gradually and carefully extended by strengthening the central commissions of the State Media Authorities (Landesmedienanstalten), this would be both possible and advisable. For the middle term prospect, the strongest arguments, economic and judicial, are to be found for the creation of a merged state media authority for broadcasting and broadcasting-related telemedia. For the time being, this could be established as a statutory corporation, with its field of action restricted to offers available all over Germany, and respecting the competence of the existing State Media Authorities (Landesmedienanstalten).