STIMULATING SCREEN PRODUCTION INVESTMENT

Analysing the impact of key policies on the audiovisual sector

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Netflix works with a variety of players - including partners from the creative industry, governments and international organisations - to better understand how the entertainment sector can thrive and support the economy overall by sharing knowledge, experiences and lessons learned. As part of that work, this study has been developed by Frontier Economics for Netflix.

EXECUTIVE SUMMARY

There is a long history of governments intervening in audiovisual (AV) markets to promote the supply of "local content", using a variety of policy tools and with a number of different policy objectives, from economic to cultural. Governments can choose to limit the supply of foreign content or require minimum levels of investment. However, there is so far limited empirical evidence of the impact of these policies, particularly on their impact on levels of investment in TV content. From a strictly economic perspective, and although those are not interchangeable policy tools, production incentives play an increasingly valuable role in encouraging additional investment in local films and TV series.

This report finds:

- The case for any policy intervention needs to be examined carefully in the context of a broader ecosystem. Introducing new measures should require a thorough impact assessment to evaluate the need for intervention and to fully understand any distortionary impacts to the audiovisual market.

- Applying restrictive policies in the hope that they increase the creation of content (in terms of volume and/or investment) can in fact lead to the opposite outcome.

- If policy makers wish to increase local screen production activity, they should consider automatic production incentives for both domestic and international productions, since they are associated with higher levels of long-term investment.

There are two distinct rationales for policy interventions to increase screen production investment

There are many public policy objectives for measures aimed at increasing investment in locally produced TV series and films, but the two most important ones are cultural and economic.

Cultural motivations relate to the desire for greater levels of investment in, and consumption of "local content".[1] Economic motivations relate to the desire to grow the local production sector (including where broadcasters face obligations to invest in return for rights to use spectrum to transmit their services), or to compensate for economic features that limit the ability of the production sector to compete.

Based on a review of broadcast content quotas used across OECD countries and analysis of policy measures applied to on-demand services in over 80 countries or territories, the study finds that restrictive policies such as local content (or language) quotas and financial

1 While there is not standard definition, "local content" can mean: content that is produced locally; content that uses local production inputs such as cast, crew, infrastructure or intellectual property (IP); content in the local language(s); or content that is culturally specific to the location.

obligations are often used to increase investment in local content. Specifically, 26 of the countries examined have quotas in place and 13 have financial obligations.[2]

Local content (or language) quotas (i.e. rules that require minimum levels of "local content") on suppliers of AV content (broadcasters, Video on Demand (VOD)[3] services, cinemas) limit the availability of non-local content. They thereby support the local content production sector, and indirectly aim to influence consumption of such content.

Financial obligations require affected firms in the AV sector to either invest directly in local content (investment obligations) or to pay a levy or hypothecated tax (i.e. a tax used to fund a specific purpose) that is used to increase the investment in local content production.

An alternative approach to strict restrictions and obligations which encourages investment in local content is to offer production incentives. Automatic production incentives lower the cost of production and enable producers who undertake qualifying expenditure to receive a contribution to that investment. According to Olsberg SPI's Global Incentives Index, automatic production incentives encouraging inward investment have been used in over 60 countries (with many countries offering region specific policies) to "*attract high-value inward investment, strengthen local production sectors and build skills, employment and infrastructure in a future-facing global industry with ongoing growth prospects*".[4] In addition to inward investment incentive programmes, some territories also have domestic incentive programmes designed to increase the value and volume of locally produced content. Selective support (i.e. subsidies provided on a discretionary basis) also lowers the cost of investment, though its discretionary nature means that it is a less secure and predictable source of project finance.

Findings from the review of existing research

There is a wide body of literature highlighting the impact of policy interventions in the AV sector. This study reviewed 22 papers and books published between 1997 and 2023. Many of these studies have highlighted that while policy interventions have often been successful in meeting their stated objectives, they have also resulted in unintended consequences. For example:

- In some cases, content quotas will increase the volume of local content that is available, but also will increase costs and prices, reduce quality, and may increase piracy.

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2 Catalogue quotas are in place for VOD services in the following countries: Austria, Belgium, Bulgaria, China, Colombia, Croatia, Czechia, Denmark, Finland, France, Germany, Greece, Hungary, Indonesia, Ireland, Italy, Luxembourg, Netherlands, Norway, Poland, Portugal, Romania, Slovakia, Spain, Sweden, and the United Kingdom; financial obligations are in place for VOD services in the following countries: Belgium, Croatia, Czechia, Denmark, France, Germany, Greece, Italy, Poland, Portugal, Romania, Slovakia, and Spain.

3 Note that VOD services can be provided on a subscription basis, an advertising funded basis or a hybrid advertising and subscription basis. For the purpose of this report we use the term VOD throughout the report as a shorthand for commercial VOD services that offer professionally produced content.

4 Global Incentives Index 2023, Oct 2023.

- Financial obligations (i.e. financial obligations to promote the production of locally produced content) may increase investment in AV content but can discourage entry or expansion, increase production costs and consumer prices; and in the EU, financial obligations have led to a fragmented regulatory framework, running counter to the ambition of a single European AV market.

- Both automatic production incentives and selective support can effectively channel public contribution to investment and therefore increase content production. However, they have different outcomes. Selective support is more likely to distort investment decisions, whereas automatic production incentives offer clearer, more transparent and more predictable additional financing.

Restrictive policies can lower investment in local content, and incentive policies can increase screen production investment

Econometric analysis conducted for this report measured the extent to which restrictive policies (in particular local content quotas) and incentive policies (especially automatic production incentives that focus on inward investment) can influence broadcasters' investment in local content production. This analysis only evaluates the economic outcomes of these policy measures, and does not consider whether they achieve their cultural goals.

The research found that once other factors which can influence investment are taken into account the following conclusions can be drawn.

- **Higher levels of restrictive policies in the sector will reduce investment.** Sector-level restrictions are estimated and compared using an index created by the OECD (the Services Trade Restrictiveness Index). Restrictive policies will impose additional costs, which will affect or distort the motivation to produce. Ultimately these costs can negatively affect outcomes. The analysis found that restrictions equivalent to the implementation of content quotas would, all else equal, reduce investment in local content by 8.2%.

- **Production incentive programmes lead to higher levels of local investment in content, and more generous programmes lead to higher levels of investment than less generous programmes**. Implementing a basic production investment programme would increase the level of investment by broadcasters in local content by 6.5%. Increasing the generosity of the programme will further increase the level of production.

Three country case studies illustrate different approaches to supporting investment

To complement the quantitative analysis, the study looked at recent experiences of three countries which have taken different approaches to encouraging investment in their local AV sectors.

- **France –** has implemented obligations on VOD services, though in excess of the minimum requirements set out in the Audio Visual Media Services (AVMS) Directive. It also offers production incentives to international and national productions and selective support to domestic productions. Although it is still relatively early to assess the impact of the AVMS Directive reforms, there is some evidence to suggest that some of the unintended consequences highlighted above are emerging, with local regulator ARCOM noting that investment obligations have played a role in price inflation caused by streamers' investments, resulting in "*tensions over the availability of talent (creative & technical) and film studios*".[5]

- **Spain –** while having also implemented the AVMS Directive, its requirements (in terms of local content quotas and financial obligations) are lower than in France. Spain has also adopted an ambitious and outward looking plan to make the country an AV hub, building on its strengths as a country with strong incentives for international and domestic productions, a highly skilled workforce, attractive shooting locations, and a supportive regulatory and recently strengthened incentive framework.[6] Over the period 2014-2019, AV sector revenues in Spain have grown at double the rate of other European countries[7] and they are expected to continue growing at 5.1% until 2026, above the global average rate.[8]

- **Colombia –** has a similar sized domestic population to France and Spain but a lower level of country income. However it has chosen a different approach to boost investment in content. It has set a goal to become an AV production hub within Latin America. To achieve this it has not applied any local content quotas or financial obligations on VOD providers. Instead it has focused on implementing production incentives to boost investment in the audiovisual sector. These incentives were found to have created more than 20,000 jobs in 2022.[9]

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5 ARCOM (2023), *Economic analysis of the French audiovisual industry - main trends and focus on the costs of high-end fiction in France*: https://www.arcom.fr/sites/default/files/2023-04/Presentation%20economic%20analysis%20of%20the%20french%20audiovisual%20industry_0.pdf.

6 https://spainaudiovisualhub.mineco.gob.es/en/spain-audiovisual-hub

7 U.S. Chamber of Commerce in Spain (2022), *Assessment of the Spanish audio-visual sector and its regulation*: https://spainaudiovisualhub.mineco.gob.es/content/dam/seteleco-hub-audiovisual/resources/pdf/Evaluaci%C3%B3n%20del%20sector%20audiovisual%20espa%C3%B1ol%20y%20su%20contexto%20regulador.pdf.

8 PwC (2022), *Entertainment and Media Outlook 2022-2026, Spain*: https://www.pwc.es/es/entretenimiento-medios/assets/global-entertainment-media-outlook-2022-2026-spain.pdf.

9 *Impactos del incentivo CINA en la industria audiovisual colombiana*: https://locationcolombia.com/wp-content/uploads/2023/03/econometria-2.pdf.

Conclusions

As governments around the world consider how to regulate new forms of content distribution (such as VOD) they need to consider whether, and if so how, to set policy to promote investment in screen production.

The findings of this report suggest that the distortionary effects associated with quotas, financial obligations and selective support[10] should be kept in mind when designing interventions aimed at increasing investment.

The analysis provides strong evidence on how different policy choices impact screen production activity.

- First, the case for any intervention needs to be examined carefully. Policy makers that are considering introducing new measures should undertake a thorough impact assessment to evaluate the need for intervention in a broader ecosystem and fully understand any potential distortionary impacts. Providers that distribute content (broadcaster TV or VOD services) have a strong incentive to invest in new local content to differentiate their services, and create an attractive proposition for their viewers. In this context, regulatory intervention may not be necessary.

- Second, econometric analysis shows that applying restrictive policies (in particular local content quotas or financial obligations) in the hope that they increase creation of content can in fact lead to the opposite outcome. Quotas impose costs for content suppliers such as broadcasters and VOD services. Furthermore, they can distort decisions to create and supply content. These costs can mean that countries that have more restrictive policies are associated with *lower levels* of investment in content production. Financial obligations impose costs on suppliers and hence users, and the EU's fragmented regulatory framework on financial obligations distorts incentives to invest.

- Third, if policy makers wish to increase screen production activity locally, they should consider automatic production incentive policies, since they are associated with increased investment. Automatic production incentives are less distortive than selective support and provide a more stable and predictable economic environment in which producers can invest in content. This in turn strengthens the local AV sector by developing capacity, workforce skills, and strengthening local vendors.

While it is still too early to understand the full impact of policy interventions applied to VOD services on motivations to invest in screen production locally, the experiences of both Spain and Colombia show how providing flexibility and reducing costly obligations will support investment.

10 See sections 2.2.1 and section 3.2 for more in depth discussion

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1 Introduction

Restrictive policies, such as local content quotas and financial obligations, have been used by policy makers to influence the amount of local content that is produced. Local content quotas are commonly applied to broadcast and AV services as a way of ensuring that they contain an appropriate volume of local content. Some countries have also introduced financial obligations (such as investment obligations or levies).

With the emergence of VOD services over the last fifteen years, regulation has been applied to VOD providers.[11] In some cases regulation and obligations that had been applied to linear services for decades were "ported" across to new VOD services.

Alongside restrictions, many countries rely on domestic production incentives or selective support to support investment in local content production. Governments adopt such incentives to stimulate the domestic AV industry and provide cultural benefits alongside economic gains. Inward investment incentives further boost the local ecosystem[12] and increase the economic activities in the local screen sector. Despite the growing adoption of policy interventions designed to increase investment in local content as well as to stimulate overall screen production, there has been relatively little empirical evidence of the impact of such policies. Against this backdrop, this report aims to address this evidence gap in understanding the policy outcomes of such interventions.

1.1 Structure of this report

The remainder of the report is structured as follows.

- Section 2 briefly considers the objectives of restrictive policies and incentive programmes in the AV sector. It describes the most commonly used policy interventions aimed at increasing investment in local content by VODs.
- Section 3 highlights the potential impacts of these different measures, including potential unintended consequences of restrictions and incentives, based on a review of the academic literature.
- Section 4 provides a quantitative assessment of the potential impact of restrictive policies and incentives, drawing on data from 27 countries over the period 2018-2022.
- Section 5 provides evidence from the case studies to complement the findings from the econometric analysis.
- Section 6 sets out conclusions.

11 In the EU the AVMSD 2018 applied regulation to VOD services. Beyond the EU, other countries are implementing VOD specific regulation.

12 The local production ecosystem includes a combination of the workforce (cast and crew capacity), infrastructure, film friendliness of a territory (how conducive it is for business).

2 The rationale for policies to stimulate screen production investment

Intervention in AV markets to promote local content is common. While there is no fixed definition of "local content", for the purposes of this report it is defined broadly to include content that is produced locally; content that uses local production inputs such as cast, crew, infrastructure or intellectual property (IP); content in the local language(s); or content that is culturally specific to the location. This section describes the objectives of policies that promote local content production. It also recounts the most commonly observed policies that have been implemented as a way of stimulating investment in locally produced content, based on desk research[13] on restrictive policies implemented in over 60 countries. It draws on Olsberg SPI's Global Incentives Index 2023, which lists automatic production incentives related to encouraging inward investment[14] (note: in some instances, these programmes are also applicable to domestic production) that have been used in over 60 countries, as well as other published sources.

2.1 Objectives of policies that promote local content production

There are many public policy objectives underpinning policies which aim to increase the production and consumption of "local content", but the underlying rationale usually relates to cultural and economic objectives. Policy makers realise that cultural content reflects and strengthens national and regional identities, and it plays a role in promoting civic engagement.[15] Cultural goods such as film and TV are widely recognised as having a "public good" dimension that can have a positive social impact in a number of ways including (Pager, 2011):

- establishing and maintaining a sense of national identity and social cohesion: "*Cultural protection becomes an exercise in nation-building*";
- providing a space for the public to identify and reflect upon issues relevant to their community, "*culture as a pre-political space for public discourse that helps set agendas, clarify values, and highlight areas of consensus or conflict"*; and
- preserving heritage and cultural diversity among viewers (which may include reducing the influence of foreign culture).

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13 The research included resources such as Olsberg SPI's Global Incentives Index 2023, European Audiovisual Observatory, and regulator websites.

14 In addition to US and Canadian State and Provincial programmes, and the Australian Producer Offset.

15 See for example: European Commission (2023) *Culture and democracy, the evidence. How citizens' participation in cultural activities enhances civic engagement, democracy and social cohesion : lessons from international research*. https://culture.ec.europa.eu/news/new-report-participation-in-cultural-activities-strengthens-democracy-and-social-cohesion

All distributors of content (broadcasters and VOD providers for example) have strong incentives to invest in content that appeals to and resonates with local audiences. Viewers have heterogeneous preferences for different types of content, and distributors will assemble bundles of content that appeal to the different tastes of their target customers. However, it has long been argued that a preference for content that has "cultural proximity"[16] to the viewer's own culture is an important preference (among many) that might influence choice of service. Therefore, offering high quality local content is one way that distributors can differentiate their services from rivals. Proponents of policy interventions in the AV sector (such as quotas, financial obligations, selective support and production incentives) argue that absent such interventions these positive outcomes may be underprovided. Hence governments intervene in order to promote the socially desirable level of investment in local content consistent with the supply of these "public goods".

The second group of objectives are economic in nature. The cultural sector is an important part of the economy: globally cultural sector accounts for 3.1 percent of global gross domestic product (GDP), it provides 6.2 per cent of all employment,[17] and is expected to grow by 40% by 2030.[18] Policy is designed to support the sector or mitigate market failures. Some AV markets have small populations, nascent markets, or country specific characteristics that lead to higher costs (Komorowski, Lordache, Kostovska, Tintel, & Raats, 2021) which may make it difficult for their content production sectors to compete internationally. Governments whose sectors have these features may intervene to ensure that their markets can compete with content imported from other countries which may benefit from more favourable conditions such as: large internal markets; an existing endowment of strong sector capacity; or easy access to well-developed financial markets from which to raise funds. Screen production activity, including both local and foreign productions, also results in local economic benefits that ripple out beyond the AV industry.[19] Thus setting policy to support production of content can "*attract high-value inward investment, strengthen local production sectors and build skills, employment and infrastructure*".[20]

16 See, for example, *"[cultural proximity is not the only] but a primary factor in orienting cultural demand and consumption, according to the need for and pleasure derived from recognition, familiarity and identity. Among the symbolic material that competes for the public's time and attention, people expect and are pleased to recognize themselves, their own social, individual and collective world, their customs and lifestyles, accents, faces, landscapes and everything else that they perceive as close and familiar."* See Buonanno (2008: 96), *The Age of Television*, as quoted in Cuelenaere (2020).

17 United Nations' Conference on Trade and Development (UNCTAD): https://unctad.org/system/files/official-document/ditctsce2022d1_overview_en.pdf; UNESCO: https://unesdoc.unesco.org/ark:/48223/pf0000380474.

18 Relates to projected growth 2021-2030 in Germany, the UK, France, Italy, Spain, Turkey, Japan, South Korea and Australia. Source: Deloitte's Future of the Creative Economy, https://www2.deloitte.com/content/dam/Deloitte/uk/Documents/technology-media-telecommunications/deloitte-uk-future-creative-economy-report-final.pdf.

19 Inter-American Development Bank, The Economic Impact of the Screen Industries in Latin America: https://publications.iadb.org/en/publications/english/viewer/The-Economic-Impact-of-the-Screen-Industries-Latin-America.pdf.

20 Olsberg SPI (2023) Global Incentives Index 2023: https://static1.squarespace.com/static/5f7708077cf66e15c7de89ee/t/64b92d9e6e68626bfb0d601a/1689857447506/Global+Incentives+Index+May+2023+%28Updated%29.pdf

2.2 Selective financial support and financial incentives

There are a number of different types of incentives and support that lower net costs of production to the sector, thereby encouraging additional production activity. These can be classified as either “selective” programmes that allocate public funding on an ad hoc and selective basis, and “automatic” programmes where incentives can be accessed automatically for qualifying projects.

2.2.1 Selective production support

Selective support is given in the form of grants or repayable loans to producers of content. There are many different types and sources of selective production support. Support can be provided at the national, regional, and/or local levels, and is administered by a screen agency or the local authority. It can cover various stages of production, including development and post-production, distribution, or theatrical release. Additionally, there are some supra-national support programmes, such as those offered by the European Union or Council of Europe (e.g. Eurimage).

Selective support pursues different aims to automatic production incentives in that it is typically given as a result of a process (that is usually competitive) which allocates funding to projects that meet specific criteria, often requiring that projects achieve certain cultural goals (e.g. encouraging younger authors, artistic or high-cultural-value content, specific cooperations (i.e. official co-productions)). These subsidies are frequently part of governments’ cultural budgets, funded by government taxation revenues or from hypothecated taxes or levies that are applied to the sector.

Selective support programmes are defined as “direct” where they are provided to specific projects or as "indirect” where they support the wider sector such as subsidising training or sector infrastructure.

Examples of direct selective support include programmes offered by Screen Ireland which has the power to provide grants, loans and guarantees for the making of films in Ireland. It provides support for development, production and distribution, and also has dedicated support programmes for short films and for female creative talents. Examples of indirect subsidies are directed to developing the infrastructure for the entire film industry, such as studios, cinema schools, or festivals promoting national production. One study found that 78% of subsidies in Korea were indirect, compared with 27% in France.[21]

2.2.2 Automatic production incentives

Automatic production incentives include cash rebates and tax incentives (such as tax credits and tax shelters) which lower the effective costs of a project and thereby support investment.

21 Messerlin, P., 2019. *"Building Consistent Policies on Subsidies in the Film Industry: Institutions and Instruments in France and Korea."* Kritika Kultura

They are "automatic" in that all productions that meet the program's qualifying criteria can access the programme (subject to project or programme caps). In some cases, the qualifying criteria impose some restrictions (e.g. around the depiction of drug use or meeting cultural tests).[22] Production incentives vary not just by the headline rate offered (i.e. the maximum proportion of costs that can be reclaimed), but by the cap on the entire scheme or individual projects, and the allowable costs that can be claimed.

Incentive programmes can be applied specifically to inward investment, to domestically sourced investment, or both. These programmes enable all qualifying productions to lower their costs, without being subject to a quality or success assessment of their screenplay. They provide companies that invest in content with a direct rebate of some of the costs of production, or the ability to offset some of the costs of the investment against their tax liabilities, or indeed to onward sell the tax advantage or receive the net profit directly (Olsberg SPI 2023).

2.3 Financial obligations and restrictive policies

There are a range of restrictive measures which aim to influence production locally. This report focuses on the main measures that affect suppliers, namely local content quotas and financial obligations such as investment obligations applying to broadcasters and VOD services, based on a review of measures implemented in over 60 countries.

2.3.1 Local content quotas

Local content quotas constrain the volume of non-local[23] content that suppliers can provide to consumers. This might relate to broadcast time (for broadcasters), catalogues (for VOD providers), or the number of screens (for theatrical release). Such quotas are in place on VOD providers in EU member states, as well as countries such as China, Colombia, Indonesia, and the UK. Examples include:

- Broadcast quotas in Australia: *"A commercial television broadcasting licensee must ensure that, for each calendar year beginning on or after 1 January 2015, the total number of hours of Australian programs that were transmitted by the licensee: (a) during targeted viewing hours in the year; and (b) otherwise than on the primary commercial television broadcasting service provided by the licensee; is not less than 1,460."*[24] The broadcast quota also includes sub-quotas for drama and documentary on top of the transmission

[22] See for example German Motion Picture Fund GMPF Schedules1-3: https://www.kulturstaatsministerin.de/SharedDocs/Downloads/DE/2023/2023-08-08-gmpf-guidelines-en.pdf?__blob=publicationFile&v=2; or Czech Film Commission Production Incentives Cultural Test https://www.filmcommission.cz/en/production-incentives/.

[23] See footnote 1 for a definition of "local content". Individual countries may have their own specific requirements for qualifying a title as "local".

[24] Broadcasting Services Act, 1992. Broadcasters are required to fulfil a content quota with more or less weight allocated to different types of content such as documentaries, children's content and dramas and productions with different budgets. These quotas are expected to be applied to streaming services also in 2024: https://www.infrastructure.gov.au/sites/default/files/fact-sheet-modernising-australian-content-regulation_1.pdf.

quota (number of hours). The definition of Australian or local content relates to Australian citizens[25] having "creative control", where "creative control" is a test with Australians in key creative roles such as producer, writer or director.

- Local content quotas as applied to linear broadcast services in Europe, for example for signatories to the 1989 European Convention on Transfrontier Television (ECTT) treaty of the Council of Europe agreed that broadcasters should *"reserve[...] for European works a majority proportion of its transmission time"* subject to various qualifications.[26] Similarly Art. 16 of the AudioVisual Media Services Directive (AVMSD) applies in the same way to European Union Member States.[27]

- Local content quotas as applied to VOD services in the EU: *"Member States shall ensure that media service providers of on-demand audiovisual media services under their jurisdiction secure at least a 30% share of European works in their catalogues and ensure prominence of those works."*[28]

- Screen quotas in Korea: *"Operators of movie theaters shall screen Korean motion pictures for not less than the annual running days as prescribed by Presidential Decree."* [Currently at 73 days][29]

2.3.2 Financial obligations

Financial obligations impose requirements to directly invest a certain amount in local content, or to pay a levy which funds investment (often administered by a regulatory or other public body). These obligations can apply to both domestic and foreign services or only domestic services. Countries or regions with such financial obligations in place on VOD providers include Belgium (Flanders region), Belgium (WBF region), Croatia, Czechia, Denmark, France, Germany, Greece, Italy, Poland, Portugal, Romania, Slovakia, Spain. Examples include:

- Direct investment obligation in Italy: *"Providers of on-demand audiovisual media services subject to Italian jurisdiction promote the production of European works and access to*

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25 Note New Zealanders can also qualify as given the Australia-New Zealand Closer Economic Relations (CER) Trade Agreement trade agreement.

26 ECTT Article 10 (1): *"Each transmitting Party shall ensure, where practicable and by appropriate means, that a broadcaster within its jurisdiction reserves for European works a majority proportion of its transmission time, excluding the time appointed to news, sports events, games, advertising, teletext services and tele-shopping. This proportion, having regard to the broadcaster's informational, educational, cultural and entertainment responsibilities to its viewing public, should be achieved progressively, on the basis of suitable criteria."*

27 AVMSD Article 16(1): *"Member States shall ensure, where practicable and by appropriate means, that broadcasters reserve for European works a majority proportion of their transmission time, excluding the time allotted to news, sports events, games, advertising, teletext services and teleshopping. This proportion, having regard to the broadcaster's informational, educational, cultural and entertainment responsibilities to its viewing public, should be achieved progressively, on the basis of suitable criteria."*

28 AVMSD Article 13, 2018

29 Promotion of the Motion Pictures and Video Products Act, Article 40

them by jointly respecting: … b) investment obligations in European audiovisual works produced by independent producers equal to 16 percent of its annual net income in Italy,"[30]

- A levy in Poland to the Polish Film Institute (PISF). *"The entity providing the on-demand audiovisual media service makes a payment to the Institute in the amount of 1.5% of the revenue obtained from fees for access to on-demand audiovisual media services".*[31]

Some countries (e.g. Spain[32], Belgium[33], Greece[34]) offer suppliers a choice to invest directly or contribute to a levy which in turn is used to invest in AV content. Others do not offer a choice and require direct investment in projects or only offer a levy.

30 Article 55 2 b, LEGISLATIVE DECREE 25 March 2024, n. 50

31 Article 15, Cinematography Act

32 For example, *"the obligation provided for in the first section may be fulfilled through the direct participation in the production of the works, through the acquisition of the rights exploitation of the same and/or through the contribution to the Protection Fund for Cinematography whose management corresponds to the Institute of Cinematography and the Arts Audiovisuals in accordance with article 19.3 of Law 55/2007, of December 28, on Cinema, or by contributing to the Fund for the Promotion of Cinematography and Audiovisuals in co-official languages other than Spanish included in article 36 of said Law."* General Law on Audiovisual Communication Article 117 (4): https://www.boe.es/eli/es/l/2022/07/07/13.

33 *"Article 157 (2) Private non-linear television broadcasters shall participate in the production of Flemish audiovisual works, either in the form of a financial contribution to the production or co-production of Flemish audiovisual works, or in the form of an equivalent financial contribution to the Flanders Audiovisueel Fond, established by the Flemish Government Decree of 13 April 1999, authorising the Flemish Government to accede to and cooperate with the establishment of the non-profit association Vlaams Audiovisueel Fonds."* Media Decree: https://www.ejustice.just.fgov.be/cgi/article_body.pl?language=nl&caller=summary&pub_date=14-04-03&numac=2014035376.

34 *"On-demand media service providers established in another Member State, if specifically target audience within Greece, must contribute an annual amount equal to one and a half percent (1.5%) of their turnover to their activity in Greece, either a) for the production of Greek audiovisual works, or b) for the purchase of rights to Greek audiovisual works that have not yet been released, or c) by paying this amount to a special account of the National Center for Audiovisual Media and Communication SA (E.K.O.M.E.), established by law 4339/2015 (A΄ 133) for the support of Greek producers."* Article 17, Law 4779/2021: (2): https://www.kodiko.gr/nomothesia/document/672722/nomos-4779-2021.

3 The impact of policy interventions in the AV sector

3.1 Introduction

While the introduction of content quotas and financial obligations could result in an increase in local screen production, it could also have potential unintended consequences, leading to increased costs and less trade in AV services.[35]

This section reviews the available literature on the impact of the different policy interventions. It particularly focuses on 22 academic publications and publicly available reports which consider the impact that content quotas, financial obligations, automatic incentives and selective support have on local screen production and the AV industry. It draws on research undertaken by Frontier Economics for Motion Picture Association (MPA) examining the economic impact of VOD services.[36]

3.2 Selective production support

Selective support plays an important role in funding many TV and film projects. The rationale for selective subsidies is that they can support investment in culturally specific content that might not otherwise be funded and can support the production sector by ensuring that producers retain access to rights. For example, Eskilsson (2022) articulated the rationale for public selective funding of film as achieving four objectives:

"• film as an unquestionable form of art and culture that requires public support; • the public funder as guarantor that the content has a strong cultural reference and is of cultural significance to the territory – including issues of cultural identity, cultural heritage, people/environments/stories that are founded in the territory and to some extent the language; • the public funder as guarantor for artistic and creative freedom and control; • the public funder as guarantor for the ownership staying in […] the specific territory"

Thus, selective production support sits alongside automatic incentives to support investment in content, with selective production support having a more specific role in protecting local culture and supporting local producers, and in particular often smaller, independent producers.[37]

However, while selective funding supports investment, and helps achieve cultural goals, some studies suggest that its application can have greater scope to distort incentives to produce content when compared with automatic incentives.

35 Trade in AV services includes the cross border licensing of content; cross border flows in investment of content and international production of content.

36 See for example: Frontier Economics (2021) The Economic Impact of VOD in Korea: https://www.mpa-apac.org/wp-content/uploads/2021/05/KR-Frontier-The-Economic-Impact-of-VOD-in-Korea-30.04.pdf.

37 Independent producers can be defined as producers that are not owned by a broadcaster / distributor.

- **The inherent uncertainty in the "selective" provision, and its discretionary nature, means that selective support has less of an incentivising impact than automatic incentives.** While each individual country has its own rules and eligibility criteria, selective support often takes the form of competitive grants for a limited pot of money. Awards are judged on subjective as well as objective criteria. In practice this means that only a small proportion of potentially eligible projects actually receive funding and projects apply to many different sources of funding. This ultimately adds costs to projects wishing to finance production, and increases the level of risk (compared with automatic incentives), as producers have to apply to multiple bodies, in time-consuming processes, sometimes across multiple countries, with uncertain outcomes, to assemble sufficient project funding. Pager (2011) contrasted the differences between costly financing in the EU and "one stop shops" that provide certainty for film financing. "*Hollywood studios provide one-stop-shop solutions for financing, production, and distribution,* [whereas when applying for selective support] *aspiring European filmmakers must navigate an increasingly Kafkaesque maze in which applying for funding consumes more time than making the actual movies*." A 2022 survey of European producers (Eskilsson, 2022) noted that "*big changes in the ecosystem have made the fragmented financing model unattractive to creatives and production companies alike. The predictability offered by one-stop/two-stop financing is irresistible."*

- **Selective support can be complex, costly and adds risk for producers.** Selective support is provided by a wide range of existing public institutions and film agencies,[38] each with its own set of rules and competitive application processes. Eskilsson (2022) found that the many overlapping country specific programmes were complex and costly for producers to navigate. He noted that "*the fragmented, territory-based financing model of the old world has become far too complicated and time-consuming. … the fragmented, territory-based, model that is already hard to use, will become even more unworkable in the future. The fragmented financing model could also be acting as a cost driver and be counter-productive in terms of sustainability requirements."* The author reported that while these programmes were viable in the pre-VOD era, the added risk and time that they impose inevitably mean that some projects cannot be greenlighted.

- **Selective subsidies lead to "industry capture".** The selecting committees are composed of a handful of representatives of the industry who will naturally tend to award subsidies to content that aligns with their values. Pager (2011) highlighted the potential for 'industry capture' amongst the institutions that administer subsidy programmes. "*Culturally selective subsidies require extensive bureaucracies to establish criteria, procedures, and personnel to sort through competing applications and identify worthy recipients. … Committee members often lack either the time or the skills to properly evaluate scripts and therefore depend above all on direct acquaintance with the applicant or personal recommendations. In many cases, awards go to those with the strongest lobby rather than the best ideas."* Similarly, a study on subsidies provided in Italy (Teti,

[38] Occasionally other organisations such as broadcasters distribute subsidy.

Tomasi, & Barchitta, 2019) notes that *“Compounding its other flaws, state patronage has spawned red-tape and inefficiency. At best, the ‘bureaucratization of culture’ serves as a dampener on innovation. At worst, patronage invites bureaucratic meddling,* [or] *industry capture”.*

- **Selective subsidies can reduce cultural dynamism and innovation.** The awarding committees will be wary of committing to innovative projects, and can potentially limit representation from minority groups. Pager (2011) notes that "*even where committee members act with the best of intentions, the results can skew in undesirable directions. Committee members often bring conflicting artistic and ideological agendas. The need to balance these diverging visions, as well as an intrinsic conservatism, leads decisions to gravitate toward bland, consensus picks. Committee members are mainly concerned to know that the project has the right 'cultural' feel to it, and is not likely to ruffle any important feathers."*

- **Selective subsidies have not supported the relative appeal of domestic content compared with foreign content.** A study of French subsidies (Messerlin & Vanderschelden, 2018) found that while the level of subsidy (note this also included production incentives) to French films had increased in the period 1995 to 2014 the share of cinema admissions accounted for by French films had not changed; and the share of French films on TV had declined by 20% over the period. The author concluded that the subsidy regime had increased the *volume* of films, though had not boosted the attractiveness of those films either on average or in aggregate. Lee G. (2010) examined the impact of subsidies on the market share of domestic films and found them to be of little importance. Gambaro (2022) found that increased subsidies have generated a greater number of films produced with a lower average budget. Italy has seen success in the development of series, but this is not because of policy but “*as a result of changing balances in the global market*”. The author cautions against introducing such policies or other interventionist measures, arguing that their inherent complexity makes them “*cumbersome*” and can have counterproductive and distortionary impacts.

- **Selective subsidies blunt incentives to create attractive content.** Messerlin & Parc (2017) contrast the use of subsidies in France, a country which has intensively used them as a policy tool for the film industry, and Korea, which has historically had very low subsidies. The authors argue that subsidies can reduce the private sector’s motivation to invest and innovate. As noted above, they distort the producers’ incentives away from creating content that will reach a wide audience, towards meeting the tastes and values of the awarding committee. Their paper concludes that “*a film industry without significant government subsidies can prosper better <u>in the long term</u> than a heavily subsidized one. This is an important lesson for countries that want to develop their film industry and to promote their culture by designing effective film policies.”*

- **Project specific (i.e. “direct”) subsidies are less effective in the long term at generating value compared to “indirect” subsidies (i.e. subsidies to support the whole sector).** Messerlin (2019) examined the economic impacts of different subsidy regimes on France and Korea's AV industry. 78% of Korea's subsidies were indirect (i.e. aimed at supporting infrastructure, skills and capacity) and 22% were direct, while in France, 59% of subsidies were direct (i.e. aimed at specific projects) and 41% indirect.[39] The author concluded that the scale and use of *direct* subsidies in France made them less effective than the *indirect* subsidies preferred in Korea.[40] Messerlin explains that indirect subsidies can create large and widespread benefits through the provision of key infrastructure (studios, human capital, etc.) that the private sector may not adequately supply. These types of subsidies are industry-wide; everyone can enjoy them. Direct subsidies are riskier and more distortive due to their specific targeting; they may subsidise unsuccessful or unpopular productions and can remove producers' commercial incentives.

- **High subsidies mean that filmmakers respond less to audience demand and instead depend on government largesse to fund their projects.** While the purpose of selective subsidies is to support cultural investment that would not otherwise occur, some studies suggest that they can excessively influence production to the detriment of audience needs. A study on subsidies provided in Italy (Teti, Tomasi, & Barchitta, 2019) which compared the performance of subsidised and non-subsidised films found that subsidies that were dispensed for productions judged to be of "national cultural interest" in the period 1995-2003. It concluded that the subsidies to support national cultural interest were neither *"an efficient nor effective instrument for generating consumer well-being"* and thus did not achieve cultural objectives. The author noted that producers that met the selective criteria had lower incentives to produce content that was appealing to audiences. The market as a result "*becomes distorted in that the cultural establishment, and not audiences at the box office*", drive the output. Pager (2011) notes that the "*front-loaded funding removes the incentive of producers to even try for box office success. Independent filmmakers earn their living by taking a cut from the pre-financing packages they assemble. With little or no "skin in the game," they remain relatively indifferent to the fate of the end products."*

- **Selective subsidies contribute to a fragmented market structure.** Pager (2011) claims that the selective subsidies elevates the importance of producers and directors over other players in the industry in the financing of production. The result is a fragmented industry dominated by independents yielding a high volume of relatively low-budget productions.

- **Selective subsidies lead to inward looking content focused on national markets.** Pager (2011) notes that selective subsidies can inhibit incentives to produce content that is valued by audiences as inevitably producers looking for funding, shape their projects to the perceived tastes of the awarding committees. The paper comments that it "*is widely*

[39] Automatic subsidies are made available to film producers to draw upon based on the success of their previous production. This risks reinforcing older companies, stifling the emergence of new firms with new ideas.

[40] Selective subsidies instead allocate funds to projects that show promise based on certain criteria. This approach carries risks, as many targeted projects may not be successful.

recognized that state funders exert a conservative influence on questions of taste and morality and favor projects with overtly national themes (such as historical dramas)."

3.3 Automatic production incentives

Automatic production incentives are now commonplace, with more than 60 countries offering national screen production incentives aimed at attracting inward investment, and more than 100 different programmes around the world. Automatic production incentives offer clear, transparent and predictable additional project financing that minimises distortions to the creative process.

There are numerous examples of research demonstrating **the positive impact that automatic production incentives (e.g., cash rebates, tax credits or tax shelters) have on local screen production**.

- A 2014 econometric study for the European Audiovisual Observatory on the effectiveness of eight EU fiscal incentive programmes found almost all the programmes delivered a greater return to the government in tax revenues than they cost to operate, whilst also providing trickle-down benefits to the broader economy.[41] The analysis suggested that there had been strong job growth in response to the introduction of a production incentive.

- A study in the UK found that screen sectors in receipt of tax relief attracted significant amounts of inward investment, which supported high employment. The study found that each £1 of Film Tax Relief returned £8.30 to the UK economy, and each £1 of High End TV Tax Relief returned £6.44 to the UK economy.[42]

- In a 2023 study, EY determined that in France between 2019 and 2021, tax credit programmes generated a combined €3.3bn of domestic spend. It further noted that raising the rate of the domestic cinema tax credit from 20% to 30% in 2016 increased additional spending in France in the following five years by €373m at a tax expenditure of €189m. The study also found that each Euro of tax expenditure contributed €6.40 of investment in France, which in turn generated €2.88 of social contribution and tax. For the domestic audiovisual tax credit, the figure for each euro of tax expenditure was €7.60, which in turn generated €3.77 of social contribution and tax.[43]

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41 European Audiovisual Observatory, *Impact analysis of fiscal incentive schemes supporting film and audiovisual production in Europe*: https://rm.coe.int/impact-analysis-of-fiscal-incentive-schemes-supporting-film-and-audiov/16808e4506.

42 BFI, *How screen sector tax reliefs power economic growth across the UK*, 2017-2019: https://static1.squarespace.com/static/5f7708077cf66e15c7de89ee/t/61b7aa232d2d7d68cbe9cc85/1639426599505/screen-business-full-report-2021-12.pdf.

43 CNC, *Évaluation de l'impact des crédits d'impôt relevant du CNC de 2017 à 2021, "Entre 2017 et 2021, chaque euro de dépense fiscale associée au CIA contribuait à localiser 7,60 € de dépenses en France, dont 2,85 €de recettes fiscales et sociales et 0,92 € de recettes fiscales uniquement, soit un niveau proche de l'autofinancement via les recettes fiscales."* https://www.cnc.fr/documents/36995/1872922/EY_CNC_Impact+cr%C3%A9dit+d%27impot_Rapport_Juillet+2023_.pdf/1b54eb3f-16d5-bdad-9c28-dedf71ec6e12?t=1700236638129.

- An analysis of the US state of Georgia's tax credit incentive found that for each $1 investment of tax credit, the state's economy benefited by $6.30. 94% of respondents to a survey for the study stated that the production enabled by the tax credit was additional, meaning that they would not have undertaken the investment absent the credit.[44]

- Research for Screen Ireland found that Ireland's tax credit had supported production expenditure of over €500mn in 2021, of which 82% can be attributed to the tax credit.[45] The "additionality rate" (i.e. the incremental investment caused by the tax credit) was even higher for inward investment productions, with 89% of incoming production expenditure attributable to the incentive.

Some studies have not found evidence that incentives bring benefits to the wider economy.

- A study on the US state of Georgia (Bradbury, 2019) found that although film tax credits increased the film industry's presence in Georgia, the return on investment appears to be small, and film production incentives were not associated with state-wide economic growth.[46]

- Button (2019) considered the case for state film incentives causing an increase in content production by looking at US data related to film industry employment, wages, filming locations, and spillovers in related industries. The author used econometrics to determine that US states that adopted incentive policies have seen an increase in TV series production relative to those that did not. The author did not find a meaningful relationship for film however, or for broader economic activity, meaning employment and wages. The study concluded that the impact of tax incentives on outcomes is "mixed" in that they can increase the level of productions but not necessarily grow the film industry locally. However, the results should be interpreted with care since the analysis was conducted under the assumption that location of filming is unrestricted and can easily move. In practice, many factors mean that location is not sensitive to incentives given specific

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44 GSE Coalition, *Economic Impact Study of Georgia's Entertainment Industry Tax Credit*: https://www.gsecoalition.com/_files/ugd/18ed45_c5ca9791ffde4f36a4ac705491f56538.pdf.

45 Section 481 of the Taxes Consolidation Act 1997 is a payable tax credit to incentivise film, television, animation, and creative documentary ("Screen") production in Ireland. Screen Ireland *First Report on Cultural Impact of Section 481 Tax Incentive for the Creative Screen Industry*, published by Fís Éireann/Screen Ireland: https://www.screenireland.ie/news/first-report-on-cultural-impact-of-section-481-tax-incentive-for-the-creative-screen-industry-published-by-fis-eireann-screen-ireland.

46 Another US study (Tannenwald (2010): https://www.cbpp.org/sites/default/files/atoms/files/11-17-10sfp.pdf) STATE FILM SUBSIDIES: NOT MUCH BANG FOR TOO MANY BUCKS) claimed *that "the only independent, in-depth empirical study to date that properly evaluates a film subsidy was undertaken by the Massachusetts Department of Revenue in 2008 finding that … every dollar of state tax revenue lost because of the film tax credit generated less than 69 cents in income for the Commonwealth's resident"*. However, a subsequent study by the same Massachusetts government agency found the film tax credit programme resulted in $85.5mn in net new spending in the Massachusetts economy during the calendar year 2017. Over the calendar year 2006 to 2017 period, the film incentive programme resulted in $615.5mn in net new spending in the Massachusetts economy. Massachusetts Department of Revenue (2022): https://www.mass.gov/doc/dor-report-on-the-impact-of-massachusetts-film-industry-tax-incentives-through-calendar-year-2017/download#:~:text=approximately%20%2487.4%20million%20in%20tax,from%20142%20productions%20in%2020161.&text=In%202017%2C%2014%20feature%20films,generated%20%2425.5%20million%20in%20credits.

location requirements; or supply of local infrastructure and quality and depth of crews and talent base.

Some studies noted that **in the presence of capacity constraints production incentives can lead to cost inflation**. A 2014 study for the European Audiovisual Observatory found that production incentives can lead to cost pressures in countries where supply is not able to respond to increased demand in the short term.[47] The report uses Ireland as an example. There, government intervention was necessary to provide sufficient studio space following the success of its production incentive programme in attracting investment.

Over the longer term, production incentives provide a stable and predictable economic environment in which producers can invest in long term assets (such as studio space, skills). The incentive programmes in the UK and France were found to help "*sustain growth, building the confidence needed for future investment in skills and infrastructure capacity, which is essential for the long term health of the sector*."[48] A report by the Quebec Film and Television Council provides evidence of such a virtuous cycle of investment.[49] Production volume in the visual FX industry in Quebec rose from C$139mn in 2014 to C$622mn in 2019. The report also highlights the region's "*competitive tax incentive programs*", the "*quality of its infrastructure*" and the "*industry's ability to export its products to foreign markets*" as supporting investment.

3.4 Impact of local content quotas

Local content quotas can apply to both linear broadcasters and VOD services. They are designed to ration the volume of "foreign" content which is supplied, and thereby influence the consumption of local content. However, quotas have a number of distorting effects.

- **Quotas increase costs and prices.** Cost inflation can arise for three reasons. First, local content quotas oblige suppliers to switch away from less costly imports to more costly local production.[50] Second, they may also create cost inflation if the capacity of local production markets cannot increase supply to meet demand. Third, they increase administrative monitoring and costs to affected suppliers.

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47 European Audiovisual Observatory (2014), *Impact analysis of fiscal incentive schemes supporting film and audiovisual production in Europe*: https://rm.coe.int/impact-analysis-of-fiscal-incentive-schemes-supporting-film-and-audiov/16808e4506

48 Ibid.

49 Quebec Film and Television Council *Annual Report 2021-2022*: https://www.bctq.ca/wp-content/uploads/2022/10/QFTC-Annual-Report-2021-2022.pdf.

50 The intuition is that they require suppliers to switch away from their preferred content to higher cost (or lower quality) domestic content. The increased demand for domestic content will all else equal push up costs. For a general discussion of the impact of Local Content Requirements (LCR) see: Stone, S., J. Messent and D. Flaig (2015-05-01), *"Emerging Policy Issues: Localisation Barriers to Trade*", OECD Trade Policy Papers, No. 180, OECD Publishing, Paris: http://dx.doi.org/10.1787/5js1m6v5qd5j-en.

- **Quotas do not necessarily lead to increased demand for local content.** Parc (2017) found that screen quotas led to lower customer turnout on days that Korean movies were being screened. Anderson, Swimmer, & Suen (1997) and Crampes & Hollander (2008) found that broadcast quotas drove down TV ratings. Lee & Bae (2004) found that screen quotas are not a significant predictor of domestic films' share of gross box office revenues. Parc J. (2017) concludes that import quotas were ineffective in boosting domestic Korean film production. In some circumstances quotas can have the unintended effect of supporting foreign content. Parc, Messerlin & Kim (2022) describe a "paradox" relating to the imposition of screen quotas on foreign films. As a result, *"a limited number of Hollywood films in China have been able to attract large audiences and even exert a strong influence upon society*".

- **Quotas can reduce quality.** Suppliers will adjust their strategy to meet the quotas, with corresponding impact on the quality of services offered to consumers. Parc J. (2017) found that quotas led to lower quality Korean films being made, with limited export potential. Broughton Micova (2013) found that broadcast quotas led to increased repeats and the reciprocal re-broadcast of broadcasters' programming in order to cheaply meet the quota. It found that broadcasters resort to "*cheap to produce, largely in-house production*".

- **Quotas may increase piracy.** In current AV markets where consumers have unlimited choice (including from illegal sources), constraining the supply of certain content (i.e. rationing the use of non-local content) may push consumers towards illegal consumption of copyright infringing content, which in turn further lowers incentives to invest. Parc & Messerlin (2020) note that fast-growing use of virtual private networks places "*more power in the hands of the consumer*", allowing individuals to access content from anywhere despite the existence of geo-restrictions.

- **Quotas do not efficiently support the domestic market**. Parc J. (2017) found that when the screen quota in Korea was *reduced* in 2006 (i.e. restrictions were lifted), there was no noticeable detrimental impact on the domestic market and in fact over the coming years domestic film production went from strength to strength both within Korea and in international markets. Gambaro (2022) found that quotas have been ineffective in Italy with regards to the development of the AV market. Telecom Advisory Services (2020) found that quotas on OTT content are associated with a *reduction* in film production per capita and that markets with more liberal "development" policies experience less of a negative impact on film releases than those with stricter protectionist policies.[51] Frontier Economics research for MPA found that restrictive policies reduced exports of audiovisual content partly because producers face less competition.[52]

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51 Telecom Advisory Services, *Quotas or incentives for the development of national audio-visual production: trends and analysis of economic impact*: https://www.teleadvs.com/wp-content/uploads/Quotas-Report.pdf.

52 MPA, *The Economic Impact of Video On-Demand Services in Korea*: https://www.mpa-apac.org/wp-content/uploads/2021/05/KR-Frontier-The-Economic-Impact-of-VOD-in-Korea-30.04.pdf.

- **Quotas that apply to a continent or region (e.g. EU's AVMSD 2018 local content quotas) disproportionately hurt suppliers in smaller countries.** Broughton Micova (2013) notes that smaller countries have lower content budgets and are thus less able to invest in the fixed costs of producing domestic content. This means that they inevitably have to rely more on imported content than larger countries whose big domestic population makes it more economically viable to produce local content.

- **Quotas that apply to a continent or region have not significantly increased trade within the region**. Papp (2020) found that quotas have proven ineffective at ensuring cultural diversity and encouraging the circulation of European works.

3.5 Impact of financial obligations

Financial obligations (to directly invest a certain amount in local content, or to pay a levy which funds investment) are designed to increase investment in local content but could lead to unintended consequences in the AV sector.

- **Financial obligations discourage entry or expansion**. Stout & Colangelo (2023) note that obligations risk distorting investment by non-local firms in a way that discourages entry and encourages exit, thus resulting in less production overall than would have occurred absent obligations.

- **Financial obligations can lead to cost inflation**. Stout & Colangelo (2023) argue that if local content production is overstimulated, countries will simply drive up the prices for local production, while at the same time oversaturating local markets. The authors claim that financial obligations can bid up the price of resources involved in production, leading to fewer local producers being able to compete. Eventually, this makes local production more dependent on fewer firms that can absorb the higher costs. As a result, financial obligations might cause higher costs, but only limited incremental output. According to the European Commission (2023), producers' financial risks have increased in recent years largely as a result of "*increasing costs across the board, and in particular for costs on technical crew and creative talent*".[53] Gambaro (2022) noted that complex sub-quotas or stricter requirements for independent producers have the effect of raising the costs of inputs that have limited supply elasticity.

- **In the EU, the system of financial obligations has led to a fragmented regulatory framework**, discouraging the development of pan-European services. This is exacerbated by policies deliberately designed to promote national production which vary significantly across different EU countries. Italy's AGCOM recently called for "*simpler and*

53 European Commission, *European Media Industry Outlook*: https://data.consilium.europa.eu/doc/document/ST-9621-2023-INIT/en/pdf.

more flexible" rules — stating the regulatory system was "*layered, complex, rigid and not always coherent*".[54]

3.6 Conclusion

There is a large literature on the impact of policy interventions in the AV sector. While these policies may be directed at achieving different outcomes, with some focused on bolstering local content and others aimed at increasing the level of local screen production, policy makers should consider the overall impact of each policy, including any potentially distorting effects on the broader ecosystem.

- Automatic production incentives are least likely to distort outcomes since they operate solely on the supply of content, and are provided in a clear and predictable way that can maximise the incentive property of the policy. They are more simple to administer (compared to selective support), and since they are automatic do not distort creative production decisions.

- Selective support is effective at channelling funding to AV production and thus boosts the supply of local content. However, it is more likely to distort motivation to produce than automatic incentives, it is costly and time consuming to administer, and it is discretionary and inevitably unpredictable and thus has a more limited incentive effect compared with automatic programmes.

- Quotas ration the supply of non-local content. They can adversely affect the quality of content offered and can put pressure on costs and prices, and are relatively ineffective at influencing consumption, particularly in the age of on-demand services.

- Financial obligations are costly for providers, and can lead to cost inflation (i.e. where the obligations have less impact on the volume of content produced, and instead increase the costs of supplying) and barriers to entry.

The academic literature often focuses on qualitative assessment of the different types of policies and there are relatively few studies that quantitatively estimate the impact of these policies. Therefore the following section contributes to the literature by presenting a new quantitative analysis of the impact that automatic incentives and content quotas can have on local screen production.

54 Screen Daily*, The US streamer squeeze: Why Europe is taking on the SVODs*: https://www.screendaily.com/features/the-us-streamer-squeeze-why-europe-is-taking-on-the-svods/5185829. Note that Italy has since updated its regulatory framework. See: *DECRETO LEGISLATIVO, 25* marzo 2024, n. 50: https://www.normattiva.it/uri-res/N2Ls?urn:nir:stato:decreto.legislativo:2024-03-25;50

4 Quantifying the impact of restrictive policies and production incentives on the AV sector

4.1 Introduction

The discussion in the previous section described that while there is a substantial body of evidence highlighting the impacts of policy measures aimed at increasing screen sector activity in a territory , there are relatively few quantitative studies. Those that do exist tend to focus on film rather than TV investment and examine the number of titles rather than focusing on the overall level of investment in titles.

The purpose of this section is therefore to address this evidence gap, by quantifying the impact that different policy measures could have on investment in film and TV production, once other factors that influence investment are taken into account, drawing on quantitative analysis and econometric modelling. The analysis can be used to measure the impact of policies on investment in local content production and estimates the size and statistical significance of this relationship. It uses data from 27 countries (countries where there is comparable data of investment by broadcasters, and measures of policy incentives and restrictive policies).[55]

Policy interventions designed to increase local content production may have cultural motivations, economic motivations, or both. The econometric analysis presented in this section only evaluates economic outcomes of these policy measures and does not point to their interchangeability. Even when considering policies that have primarily cultural goals, policy makers should understand their potential to either stimulate or depress content production locally.

4.2 Modelling the impact of policy interventions on investment

4.2.1 Many factors affect investment in content production

Investment in content production is costly and risky. Success depends on the tastes of consumers. As noted in section 2.1, some studies note that “cultural proximity” to the viewer’s own culture is an important preference (among many) that might influence viewer choice. Hence, for the reasons set out above, distributors may have strong rationale to invest in local content in order to appeal to audience demand and to positively differentiate their services from competitors in important markets for their business.

However, producers will be more likely to invest when costs are minimised and risk is mitigated. Many factors affect the cost and risk of investment including the following:

[55] Countries included are Australia, Belgium, Brazil, Canada, China, Colombia, Czechia, Denmark, Finland, France, Germany, India, Indonesia, Italy, Mexico, Netherlands, New Zealand, Norway, Poland, Portugal, South Africa, Spain, Sweden, Thailand, Türkiye, United Kingdom, and the United States

- **The availability of infrastructure including production and post production facilities**. Large-scale TV and film production requires a high availability of large studio facilities to shoot and undertake special effects. Some countries have an ample supply of such facilities. The costs of screen infrastructure vary depending on country specific factors. Remote locations have higher costs which deter investment, while lower-cost countries enable investment. The ability to attract investment to a country in turn increases the willingness of suppliers to invest in infrastructure – meaning the country is more likely to be viewed as a "hub" for production. Peripherally, a country's infrastructure in the broader sense, such as well-maintained roads, proximity to quality health care and airports, also plays a part in location decisions for production.

- **The depth of skills and capabilities of the crew and cast**. The process for making film or high-quality TV is complex, requiring many different high-skilled workers to interact at different stages of production. Countries that have highly-skilled workforces, across all the relevant trades, have an advantage in attracting investment.

- **The regulatory and policy environment and general "film friendliness" of the territory.** Territories familiar with, and supportive of, production generally have systems in place to reduce barriers to doing business. This can involve facilitation through film commissions, low/no location permit fees, strong collaboration from all tiers of government (local, state, federal) with an empowered film commission etc. Producers face lower costs and risks where there are lower regulatory burdens. Other considerations with respect to "film friendliness" include issues like a country's approach to critical issues such as content review mechanisms and piracy.

- **The availability of production incentives**. As previously mentioned, 60+ countries offer production incentives in recognition of the role they play in developing the local industry and attracting international investment. The industry as a whole directly supports a high value added, export-focused sector with significant scope for skilled employment. It also offers indirect benefits favourable to related sectors such as fashion, music, publishing, tourism[56], or, more broadly, a country's soft power.[57]

This analysis focuses on two specific policies which affect investment decisions: the use of automatic production incentives and the regulatory and policy environment with respect to investment in content.

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56 For example, a recent report by the CNC highlighted the role that film production, and particularly VOD distribution, plays in supporting French tourism. See: https://www.cnc.fr/professionnels/etudes-et-rapports/etudes-prospectives/impact-du-cinema-et-de-la-fiction-tv-sur-le-tourisme-en-france_2097648.

57 There are a number of studies that examine the link between cultural outputs (film and TV) and soft power (i.e. the ability to influence outcomes and opinions by producing attractive content. See for example, Mondo Internazionale (2023) *Screenplaying Soft Power: The Influence Of Cinema On The Global Stage*: https://mondointernazionale.org/focus-allegati/screenplaying-soft-power-the-influence-of-cinema-on-the-global-stage; Modern Diplomacy (2023) *Netflix as a Global Soft Power Multiplier*: https://moderndiplomacy.eu/2023/11/21/netflix-as-a-global-soft-power-multiplier/; and *Cinema and Soft Power Configuring the National and Transnational in Geo-politics,* edited by Stephanie Dennison, Rachel Dwyer (2021): https://edinburghuniversitypress.com/book-cinema-and-soft-power.html.

4.2.2 This analysis focuses on content production investment and associated policy measures

Broadcaster investment in local content production

The analysis in this section assesses the impact of policy interventions on broadcasters' investment in content production. Policies like production incentives do not directly affect content licensing, so this analysis does not consider investment in licensed content.

One of the reasons for focusing this analysis on investment by broadcasters in content is because there is a long history of policy interventions (and particularly restrictive policies such as quotas) applied to broadcast services, whereas policies impacting VOD services are newer.

Data on broadcaster investment in content (excluding investment in sports content, which can be related to cost of acquiring TV rights) in the period 2018-2022 was supplied by Ampere Analysis. The data is expressed on a Profit and Loss ("P&L") basis (i.e. it is consistent with how broadcasters report the data in their financial statements).

Policy variables

For the purposes of this analysis, two policy variables were created to assess the level of use of foreign automatic production incentives, and countries' implementation of restrictive policies (specifically local content quotas). The key policy and investment variables used in the analysis are described below.

Level of restrictive policies

The level of a county's restrictive policies in the broadcasting sector was proxied by the OECD broadcasting Services Trade Restrictiveness Index (STRI). This index provides a consistent way to compare restrictions in the broadcasting sector across countries. The score is based on an assessment by country sector experts to a standard set of questions. The scores are estimated based on 86 measures in the following five pillars:

- restrictions on foreign entry - restriction on the form of investments companies, leadership of companies, content quotas, mergers, copyright law, cross border data;
- restrictions on movement of people;
- other discriminatory measures - discriminatory tax breaks, presence of a cultural test, copyright;
- barriers to competition - government control of broadcasters; and
- regulatory transparency - intellectual property rights.

Local content quotas (falling under the pillar of "restrictions on foreign entry") represent roughly 5.7% of the STRI index (broadcast or airtime quotas for motion pictures, broadcast quotas, and whether the number of foreign channels is limited by quotas).

Automatic production incentives for inward investment

Data on foreign automatic production incentives in 2023 was sourced from Olsberg SPI.[58] As noted, while over 60 countries offer different forms of automatic production incentive, the precise implementation varies significantly by country. In the case of countries with national programmes *and* regional programmes in place, the analysis focuses on the national programme as it is likely to be more representative of the range of incentives available to producers.[59]

The influence of production incentives on broadcaster investment could be as a direct commission of local content,[60] or as part of a co-financing (as many costly High-end TV (HETV) productions are co-productions) or purely inward investment production activity in the case of non-local broadcasters. Many countries with an inward investment incentive programme also have a domestic programme, in recognition of the importance of supporting the sector at the most local level. Moreover, programmes often fully or partially apply to both domestic *and* inward investment.[61]

External factors (such as exchange or inflation rates) notwithstanding, the degree of generosity of a production incentive in a country depends on the following factors:

- the percentage of production costs that could be reclaimed or offset as a cash rebate, tax credit or tax shelter;
- the overall budget of the programme or project caps; and
- the coverage of allowable costs for the purpose of calculating the rate.

Countries were classified in four ways:

- countries with no production incentives (or production incentive limited only to a small area within the country)[62];
- countries with low production incentives, typically <20% of allowable costs;
- countries with medium incentive policies, typically 20-30% rate or a lower percentage but no budget cap; and

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58 Olsberg SPI Global Incentive Index 2023

59 For countries with only state-level programmes (e.g. the US), the analysis averaged state incentive rates weighted by states with highest production. Canada instead has provincial incentive programmes, so the analysis looks at the typical rate available to a producer in some of the most popular provinces in Canada. It averages across regional incentive programmes, which are stackable on top of the federal 16% tax credit, to result in an average incentive across British Columbia, Quebec and Ontario. *Please refer to the technical annex for further details.*

60 See footnote 1 for definition of "local content".

61 For example, US programmes apply to both domestic and inward investment; the Australian Screen Production Incentives (ASPI) includes the Producer Offset which is for local production & coproduction and subject to a cultural test; the Location offset for inbound production and post-VFX offset for local and inbound post-VfX work.

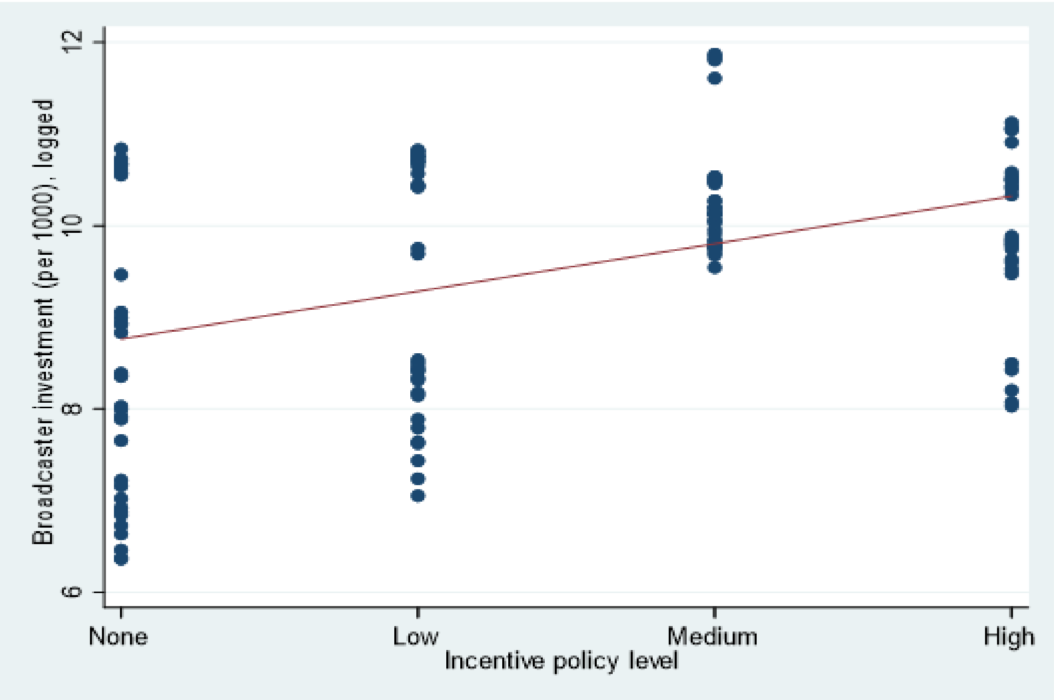
62 For example, though there is an incentive programme in Sao Paulo and Rio, there is no national incentive production programme in Brazil.

- countries with high incentive policies, typically 30% tax rebate with wide coverage and no budget cap.

4.2.3 The relationship between policy measures and broadcaster investment in content

A comparison of the level of investment in content production[63] across different countries and the level of policy incentives or restrictions shows that there is a **positive correlation** between broadcaster investment in content production and production incentives (Figure 1). The vertical axis shows (the logarithm of) broadcaster investment in each country weighted by population size and the horizontal axis shows the four levels of incentive policy (as categorised above). The upwards sloping red line of best fit demonstrates that countries with more generous incentives tend to have higher investment in local content than countries that have less generous or no incentives.

Figure 1 Correlation of broadcasters' investment in content production per capita against production incentives



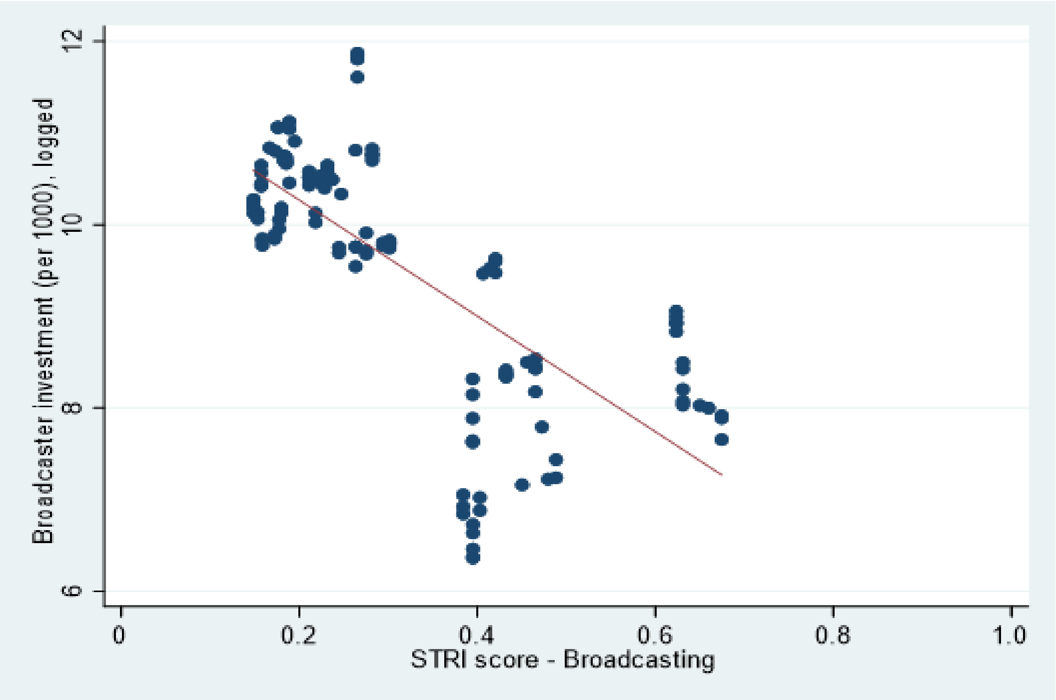
Source: Frontier Economics; Broadcaster investment sourced from Ampere Analysis. Incentive policy level data sourced from Olsberg SPI's Global Incentives Index and operator website.

Note: The vertical axis is logged broadcaster investment in content production (i.e. excluding licensed content) in 27 countries across 2018-2022; the horizontal axis shows production incentives. Broadcaster investment is logged to normalise the data and reduce the variability of investment levels across countries to make it easier to visually depict. Countries' production incentives are scored none, low, medium, high.

[63] Data on investment in content production is sourced from Ampere Analysis (Ampere Analysis uses the term "investment in original content"). It relates to content commissioned or directly invested in (as a co-production for example) and excludes investment in licensed content.

There is a **negative correlation** between broadcaster investment in content (excluding licensed) and restrictive policies as shown in Figure 2 below. The vertical axis shows the logarithm of broadcaster investment weighted by population size and the horizontal axis shows the STRI Broadcasting score. The downwards sloping red line shows that countries with tougher restrictions tend to have lower investment than countries that have less stringent restrictions or no restrictions.

Figure 2 Correlation of broadcaster content investment per capita against STRI



Source: *Frontier Economics; Broadcaster investment sourced from Ampere Analysis. STRI sourced from OECD*

Note: *The vertical axis is logged broadcaster content investment (excluding licensed) in 27 countries across 2018-2022; the horizontal axis shows restrictions, modelled using the STRI Broadcasting score. Broadcaster investment is logged to normalise the data and reduce the variability of investment levels across countries to make it easier to visually depict. The STRI takes values between 0 (least restrictive) and 1 (most restrictive).*

However, while Figure 1 and Figure 2 are useful in indicating that there is correlation, they do not take into account the impact that other factors have in driving investment or the risk that the relationships observed are not causal. Econometric modelling described below can be used to address these concerns.

4.3 Description of the econometric model

The econometric modelling focuses on isolating the impact of policy on investment in local content by broadcasters. The econometric analysis draws on data from a variety of publicly available data sources over the period 2018-22 and covers 27 countries with a good mix of different policy interventions.

The model assumes that broadcaster investment in local content is determined by:

- Policy variables (as set out above)
- Other factors affecting investment:[64]
  - The level of country income proxied by GDP per capita. Consumers in higher-income countries may be more willing to subscribe to VOD services, or subscribe to higher (more expensive) tiers or providers of these services, and hence these countries may be more attractive markets to invest in.
  - The population size. Countries with larger populations can spread the high fixed costs of content production across more subscribers or viewers.
  - Spanish language.[65] Countries whose language is widely spoken around the world may have higher investment as the content can be exploited in the original language to a much wider potential customer base.
  - The proportion of sector revenue that is derived from public licence fees or taxes. Countries with high levels of public financing for broadcasting may affect investment by broadcasters. Public investment may:
    - increase overall levels of investment in content and/or raise the level of quality of content in a country.
    - “crowd out” private sector investment (if it limits incentives to invest); or
    - “crowd in” investment if it makes such investment more profitable (for example if the value of TV advertising is higher in countries with public broadcasters; or public investment creates a more diverse and sustainable AV ecosystem).

There may also be other country specific factors which cannot easily be measured - such as the availability of sector infrastructure or skills or the level of selective support available. Some factors (like infrastructure or skills) will be correlated with GDP. Furthermore, the omission of these factors (like selective support) will not invalidate the results.

64 In addition to these explanatory variables the model also included a dummy variable for the US since the scale of production in the US was an outlier compared with other data.

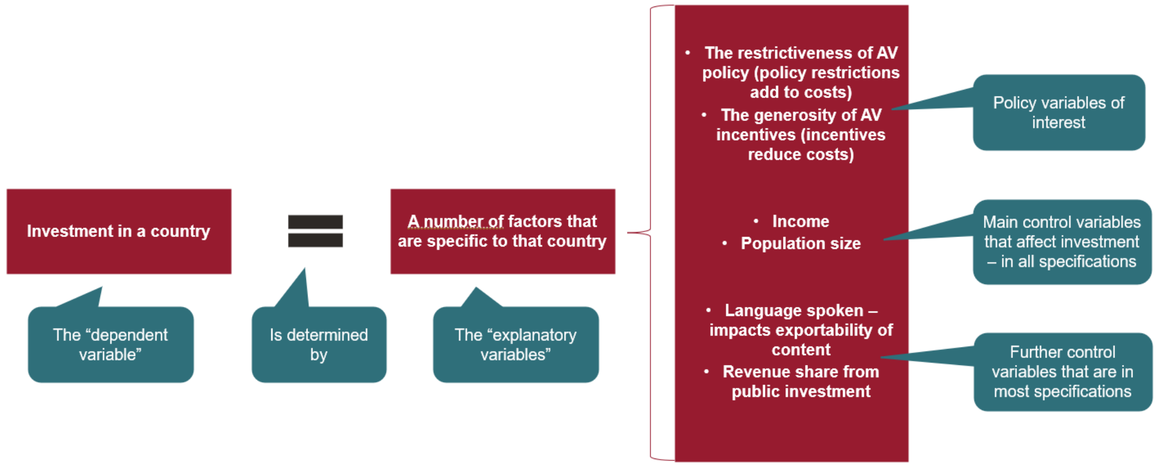
65 Note that the modelling also considered other widely spoken languages as alternative explanatory variables.

4.4 Overview of the model

The analysis is based on multivariate analysis which is good at detecting broad patterns across large datasets. The model assesses the drivers of variation in investment in content across time and across markets.[66]

Figure 3 illustrates the model overview.

Figure 3 Model overview



Source: Frontier Economics

4.5 Results and commentary

Once factors such as the level of GDP per capita; population; the share of revenue accounted for by public licence fees; whether the content is from the US;[67] and whether the content is Spanish language;[68] are controlled for, the following relationship holds.

Production incentives

On average, the increase in a country's level of production incentive by one level (from no incentive to low incentive; or low incentive to medium incentive etc.) causes investment in

66 Further details of the econometric analysis is available in the technical annex.

67 The level of investment in the US is somewhat of an outlier compared to other countries on an absolute level and on a per capita basis. Therefore a "dummy variable" for the US is used to control for the high level of investment observed in the US when estimating the coefficients on the policy variables. The technical annex shows the impact of excluding the dummy variable when estimating coefficients.

68 In the chosen specification dummies for languages which are widely spoken (i.e. by a majority of the population) in multiple countries.

local content by broadcasters to increase by 6.5%. This is a very strong statistical relationship (significant at the 5% level). Thus increasing the generosity of the programme will further increase the level of production, though in practice there are likely to be limits to the scope of incentives to increase investment such as supply constraints or the ability of the production ecosystem to meet demand.[69]

Restrictive policies

On average, each percentage point increase in the STRI score (i.e. by increasing restrictive policies) would reduce investment by 1.46%.

This implies that, given the application of broadcast quotas represents 5.65% of STRI index,[70] countries with broadcast quotas would have ~8.2% less investment in local content than those that do not have quotas (i.e. $-1.46 * 5.65 = 8.2$). This is a very strong statistical relationship (significant at the 1% level).

4.6 Investment by global VOD providers

While the results presented above describe the relationship between local content policy and investment by broadcasters, investment by global VOD providers is similarly affected by production incentives and restrictive policies. However, the relatively recent entry of global VODs, and the rapid growth in investment by global VODs around the world mean that it is difficult to estimate the size of the relationship using a similar econometric analysis as described above.

Simple correlation charts show a similar pattern. Investment in content by global streamers across ~50 countries in 2018-2022 appears correlated with both the level of restrictive policies and incentives.[71]

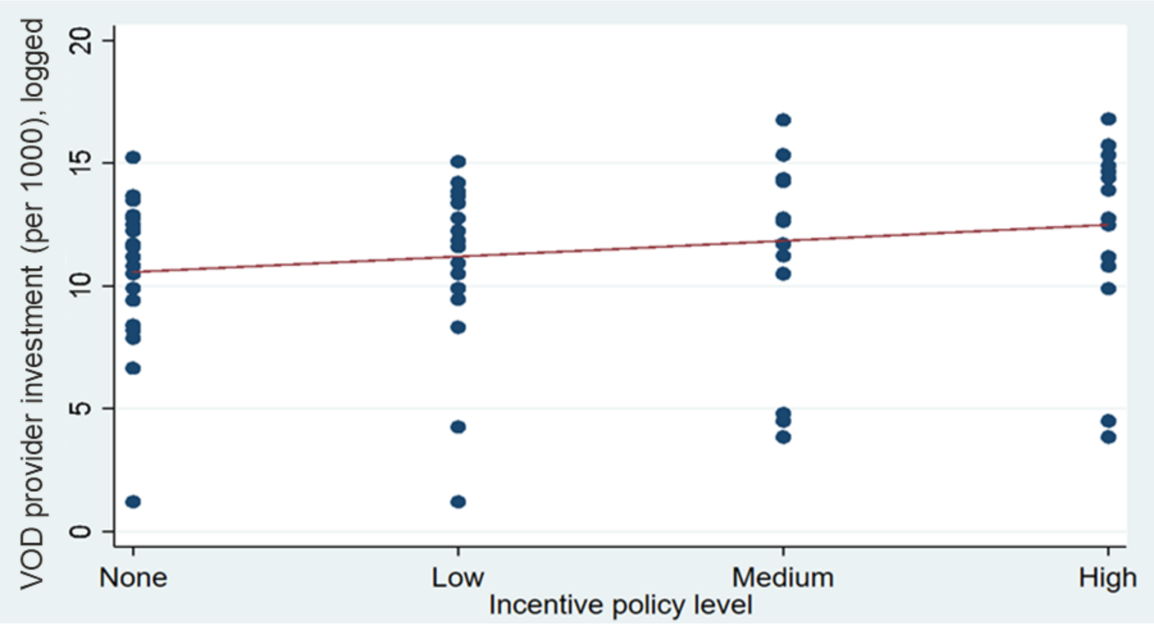
Figure 4 shows a positive relationship between investment by global VOD in content production (logged and expressed on a per capita basis) and the level of incentive policy. This relationship is similar to the analysis using broadcaster investment.

69 The local production ecosystem includes a combination of the workforce (cast and crew capacity), infrastructure, film friendliness of a territory (how conducive it is for business), as well as incentives.

70 Section 4.2.2 notes that there are three types of quotas which contribute to scores in the STRI index. This implies that countries with all three quotas in place (such as France) will have an STRI score of 5.65 percentage points higher than a country that does not have any quotas (such as the US).

71 Note that whilst scatter plots are a useful introductory way to explore the relationship between the dependent and independent variables, correlation does not reflect causality as it fails to consider the control variables that would have been used in the regression models.

Figure 4 Correlation of VOD provider content investment per capita against production incentives

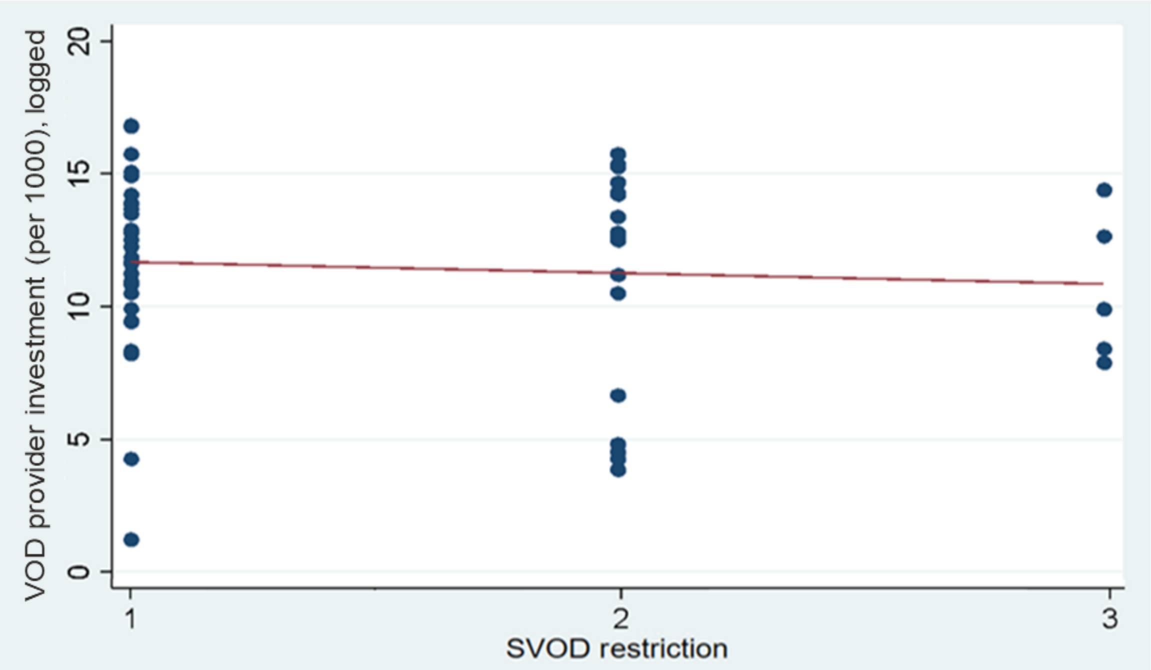


Source: Frontier Economics

Note: The vertical axis is logged "VOD provider investment" (i.e. investment in original content by VOD providers, excluding investment in acquired / licensed content) in 51 countries across 2018-2022 (spend has been summed across years for each country so that each dot represents the total spend of a given country); the horizontal axis shows production incentives. VOD provider investment is logged to normalise the data and reduce the variability of investment levels across countries to make it easier to visually depict. Countries' production incentives are scored none, low, medium, high.

Figure 5 shows a slight negative relationship between weighted VOD content investment and the level of restrictive policy. Once more, this is a similar pattern to the correlation chart using broadcaster investment, (noting that this chart uses a different restriction variable based on the type of content quotas as compared to the broadcaster analysis (as the Broadcaster STRI was not entirely applicable)).

Figure 5 Correlation of VOD provider content investment per capita against the level of VOD restrictions



Source: Frontier Economics

Note: The vertical axis is logged "VOD provider investment" (i.e. investment in original content by VOD providers, excluding investment in acquired / licensed content) in 51 countries across 2018-2022 (spend has been summed across years for each country so that each dot represents the total spend of a given country); the horizontal axis shows production restrictions, namely quotas. VOD provider investment is logged to normalise the data and reduce the variability of investment levels across countries to make it easier to visually depict. A restriction score of 1 refers to countries with no content quota policy, 2 refers to countries with a regional/continental quota in place (e.g. AVMSD 2018 which applies a minimum 30% quota of European Works to qualifying VOD services), and a 3 reflects countries with a country specific quota (e.g. for example France applies a 40% sub-quota for original French language content requirement on VOD services).

5 Findings from the case studies

The previous section examined the economic outcomes of policy interventions and highlighted that, across the countries included in the analysis, restrictive policies generally depress broadcaster investment in content production, while automatic incentives generally raise broadcaster investment even once other key drivers of investment are taken into account. The econometric analysis presented only evaluates economic outcomes of these policy measures.

However, the analysis reports the average impact across many countries. In practice, country specific factors also explain the level of investment (see section 4.2). As well as the specific AV policies, the existing endowment of capabilities, capacities and skills will influence investment; the wider regulatory and policy environment (including the use of selective support) will determine the level of investment. Furthermore, different countries choose to implement restrictive policies and automatic incentives in different ways which can be difficult to capture in quantitative modelling.

The varying approaches taken by countries to regulating VOD investment in local content create an alternative way to assess how policy can affect investment. It is notable that EU countries have taken different approaches to regulating investment by VOD even in the context of the AVMSD 2018 which created a common minimum framework for the application of quotas, though with a degree of flexibility in the approach that can be adopted, especially with regard to the optional introduction of financial obligations. The differences and similarities in regulation illustrate the variation in policies to promote the production of “local content”.

This section draws on case study evidence to complement the quantitative analysis, looking at the approaches that three different countries have taken to promoting investment in locally produced content. In particular, it considers how Spain and France have chosen to implement regulation on VOD services. Both countries are high income countries, within the EU, and have similar sized populations; both are subject to the AVMSD; both have financial obligations to promote production of local content in the sector; and both have relatively high levels of investment in local content.

The section also includes a case study on Colombia, which has a similar sized population to France and Spain, though it is a middle income country. Colombia has chosen not to impose regulation on VOD, though has been successful at attracting investment in local content.

5.1 The implementation of VOD regulation to enable investment in local content - country case studies

5.1.1 VOD regulation to enable investment in local content in France

France has imposed very high investment obligations (the highest in Europe) which constrain how suppliers operate. The restrictions are partly designed to support the theatrical sector meaning that the broadcast and VOD sectors subsidise the theatrical sector through these obligations. In France, services must invest 25% of their revenue into EU film and audiovisual production when they offer annually at least one feature film within 12 months of its release in theatres in France or 20% in other cases. At least 85% of investment must be dedicated to French-language content. In addition, a significant portion of this contribution (three quarters for film production, two thirds for audiovisual production) will support independent production of European works.[72] Furthermore, France has limited the ability of VOD service providers to exploit the Audiovisual works of independent production companies to which it is obligated to invest in. It may acquire rights to exploit the works for no more than six years, of which a maximum of three years may be exclusive rights.[73]

France has set very high local content catalogue quotas for VOD providers that are domiciled in the country. These catalogue quotas go beyond the level set in the 2018 AVMS Directive that sets a floor of 30% quota of the catalogue to be European Works. In the case of France, there is a requirement on VOD services domiciled in the country that at least 60% of the catalogue is European Works and 40% is French language original. Agreements with the regulator can set lower percentages of EU titles (no less than 50%) in exchange for commitment to invest in the production of brand new original French-language audiovisual works produced by independent production companies.[74]

The combination of high local content quotas and investment obligations found in France partly reflects France's longstanding policy (going back to the 1980s) of using the distribution sector (historically mainly broadcast TV channels) to finance the production sector.[75] In return for granting new licences for terrestrial TV services the broadcasters were required to fund independent cinema and TV, for the benefit of the production sector. However, as new distribution services were developed (such as VOD), policies that had applied to broadcasters were "transferred" across to the new sectors.

These policies have supported the production of French content, but have led to a fragmented sector. While there is a small number of large producers (e.g. Banijay, Mediawan, Asacha, JLA Groupe)[76], there is a long tail of smaller independent producers that rely on public support, but lack scale to compete internationally. For example, a 2022 report for the French Senate

72 Decree No. 2021-793 of June 22, 2021 relating to audio media services, section 21 and 22.

73 Decree No. 2021-793 of June 22, 2021 relating to audio media services, section 22.

74 In addition, EU and French titles must be made prominent by means other than the mere mention of the title. This can be by displaying visuals, making trailers available and adding specific sections on the home page, in recommendations to users, in searches initiated by users and in campaigns to promote services.

75 See for example Lavialle (2020), *Industrial trajectory and regulation of the French TV market,* section 1.4.2, and 4.1. *"All broadcasters, including the public ones, were granted free terrestrial licenses in exchange for funding independent cinema and TV producers. Through this funding, the TVs would acquire temporary broadcasting rights for the programmes. The producers flourished in a large ecosystem gathering 700 companies specialized in cinema and 2000 companies focused on TV shows. These producers kept the ownership of the copyrights."*

76 European Commission (2023) *European Media Outlook table 3*: https://ec.europa.eu/newsroom/dae/redirection/document/95874.

found that while the production sector was performing very well overall (with 4,500 producers), only a third of the sector's revenues were generated by the 4,300 smallest producers.[77]

The production obligations and local content quotas have incentivised investment in film by broadcasters. However, these productions are often lower budget films that tend not to find a large audience. It is argued that the reliance on a mix of quotas and investment obligations to fund film production has distorted producers' incentives which has resulted in low value works. One author commented (in the context of describing European production):

"Reliance [by movie producers] on television has proven a mixed blessing. The pre-purchase deals that TV executives dangle distract filmmakers from focusing on theatrical distribution. Moreover, it encourages smaller productions that are unlikely to be theatrically competitive at the box office … Television pours funds into a multiplicity of low-budget productions, … Trading box office for TV has served European film poorly." (Pager, 2011).

This view is borne out by data on French film production. According to the French Film Fund CNC, 159 films were financed by broadcasters and VOD services in 2022 to fulfil their investment obligations, of which 141 are French.[78] According to the same report, 143 French films were produced in total in 2022. This implies that broadcasters contributed to the financing of 99% of the French films produced in 2022. However, in 2022 (first post-Covid year) only eight French films generated more than 1mn admissions in France and 21 films generated between 500,000 and 1mn admissions.[79] This suggests that the vast amount of films produced and funded did not find large audiences and instead were distributed on TV.

By the same token the focus on small productions destined for TV broadcast means that French films have struggled to generate significant revenues in international markets. In 2022, 61 French films generated in excess of 100,000 admissions abroad, down from 76 in 2017.[80] Furthermore, French films saw 31.3mn admissions internationally in 2022, compared to 80.5mn in 2017, though the impact of COVID on domestic admissions will have affected admissions.[81]

In addition, the combination of high investment obligations and high production incentives may have contributed to price inflation in recent years as supply has failed to grow with demand. Production costs for fiction have been particularly affected, with premium 'dramas' having an hourly cost of at least €1.2mn.[82] A 2023 report by ARCOM found that the costs of fiction –

77 SÉNAT SESSION ORDINAIRE DE 2021-2022 No 593 Report by the French Senate

78 https://www.cnc.fr/documents/36995/1872922/La+production+cin%C3%A9matographique+en+2022.pdf/697a20d2-0599-7086-8704-21922a769d35?t=1680089021871

79 *French initiative films; excluding coproductions and films with a majority of non-French funding*: https://fr.wikipedia.org/wiki/Box-office_France_2022.

80 https://en.unifrance.org/news/16769/results-for-french-films-abroad-in-2022, https://en.unifrance.org/news/15143/unifrance-releases-results-for-french-films-abroad-in-2017.

81 Ibid.

82 Arcom (2023), *Study on the economic fabric of the audiovisual production sector* - 7th edition, p.7

especially high-end – have been rapidly increasing since 2018 with a peak in 2020-21, largely driven by crew costs and on-location expenses. ARCOM identified several factors that contribute to high costs (including Covid and the transition to greener production). However, ARCOM also clearly notes that investment obligations (in place since mid-2021) have played a role as streamers' investments resulted in "artificial price hikes".

5.1.2 VOD regulation to enable investment in local content in Spain

Spain has adopted an ambitious and outward-looking plan to make the country an audiovisual hub. As a result, it has built a strong and healthy audiovisual ecosystem. As well as growing domestic production, Spain has positioned itself as an international audiovisual hub which builds on its strengths as a country with a highly skilled workforce, attractive shooting locations, and a supportive regulatory and recently strengthened incentive framework.

In 2022, the Spanish Government implemented a five-year plan to internationalise and promote the AV sector, and the AV Media Services Directive (AVMSD) was transposed into Spanish law. This expanded the scope of existing AV service obligations to new players in the market, including VOD providers.

In doing so, Spain has taken a slightly different approach to regulation of VOD to promote investment in local content when compared to other countries like France. The Spanish Government has created automatic investment incentives to attract foreign investment (like France); but while it recently implemented AVMSD in relation to VOD services, it has to be done in a balanced way that gives some degree of flexibility in how providers can meet these obligations. Spain implemented a local content quota which was the minimum permissible with the AVMSD floor, i.e. at least 30% of titles must be European Works (lower than France's 60% European Works quota). Spain, like France, has imposed a sub-quota requiring that at least 15% of the catalogue must be European Works in Spanish language (again lower than France's quota of 40% of the catalogue to be in a French language).[83]

Similarly, Spain has taken a different approach to financial obligations. It requires that 5% of annual revenues in Spain are used to support investment of European Works, though it provides flexibility on how providers can meet these requirements. The obligations are applied in a non-discriminatory way to both broadcasters and VOD providers (a 5% investment obligation has been applied to Spanish broadcasters since 2010 and was extended to VOD services in 2022)[84]. The aim is to "*eliminate disproportionate and unnecessary regulatory burdens by making obligations more flexible, reducing administrative burdens, eliminating discrimination and promoting a level playing field between all actors in the audiovisual*

[83] It imposed a further quota on public on-demand television audiovisual media service provider at state level shall in any case reserve a minimum of 6% of the catalogue must be in one regional language, taking into account the population of the region. *Ley 13/2022, de 7 de julio, General de Comunicación Audiovisual* - Art. 116

[84] *Ley 13/2022, de 7 de julio, General de Comunicación Audiovisual*: https://www.boe.es/buscar/act.php?id=BOEA-2022-11311.

sector".[85] VOD providers can choose to invest directly in production, or purchase rights to European Works, or pay into a Film Fund (either the Spanish Cinematography Protection Fund and/or the Cinematography and Audiovisual Promotion Fund). *"At least 70% must be allocated to audiovisual works by independent producers, produced on their own initiative or on commission, in the official language of the Spanish State or in one of the official languages of the Autonomous Communities."*[86] Additionally, at least 40% of the 5% obligation must be allocated to cinematographic films by independent producers in the official language of the Spanish state or languages of Autonomous Communities.[87]

Spain offers generous foreign automatic production incentives. These include a 30% rebate up to €1mn eligible spend and 25% after that.[88]

Spain's plans to become a hub for production have been accompanied by a period of strong sector growth. Between 2014 and 2019, the sector revenues grew at levels (11.4%) double those of other European countries, including Germany (4.2%), France (3.9%) and Italy (2.9%).[89] Currently, Spain ranks 12th in the world in AV industrial revenue, which is expected to continue growing at 5.1% until 2026, above the global mean rate.[90]

However, as with other countries, there is evidence that the boom in demand can lead to a shortage of skilled professionals, albeit that the boom may have peaked, and pressures are declining. In 2021, a study from the Ministry of Digital Transformation found that 38% of companies in the AV sector have challenges finding qualified professionals.[91] As a consequence, some producers have resorted to advance booking of crews for a full year in order to guarantee their availability to film in the capital city. As most of these crews are hired by large production companies, national and independent productions are forced to hire less

85 España Hub Audiovisual de Europa, *Plan de impulso al sector audiovisual*, p. 63: https://portal.mineco.gob.es/RecursosArticulo/mineco/teleco/comun/ficheros/plan-de-impulso-al-sector-audiovisual.pdf.

86 See: https://rm.coe.int/iris-plus-2022en2-financial-obligations-for-vod-services/1680a6889c. *"Of this sub-quota, the provider of the television audiovisual communication service, whether linear or on demand, shall in any case set aside: A minimum of 15% to audiovisual works in the official languages of the Autonomous Communities, taking into account their population weight and reserving at least ten percent for each of them. A minimum of 30% for audiovisual works directed or created exclusively by women."*

87 Ibid.

88 Per production there is a cap of $21.7mn and per series $10.8mn per episode. For Spanish productions and co-productions at least 50% of the deduction base corresponds to expenses incurred in Spanish territory. For foreign productions $1.1mn minimum expenditure in Spain is required for the tax rebate. For animation and post-production, the minimum expenditure required in Spain is $221,000. The applicant production company must be registered in Spain as a producer.

89 U.S. Chamber of Commerce in Spain (2022), *Assessment of the Spanish AV sector and its regulation*: https://spainaudiovisualhub.mineco.gob.es/content/dam/seteleco-hub-audiovisual/resources/pdf/Evaluaci%C3%B3n%20del%20sector%20audiovisual%20espa%C3%B1ol%20y%20su%20contexto%20regulador.pdf.

90 PwC (2022), *Entertainment and Media Outlook 2022-2026, Spain*: https://www.pwc.es/es/entretenimiento-medios/assets/global-entertainment-media-outlook-2022-2026-spain.pdf.

91 Cámara de Comercio de España, *ANÁLISIS DE IMPACTO ECONÓMICO DE LOS SECTORES DE TELECOMUNICACIONES Y DE CONTENIDOS AUDIOVISUALES*: https://www.audiovisual451.com/wp-content/uploads/2021/07/210716_i_camaras.pdf.

experienced staff to meet demand. The high demand is, in turn, feeding inflationary pressures in the sector as the cost of certain skill technicians is driven up.[92]

5.1.3 VOD regulation to enable investment in local content in Colombia

Colombia has designed policies to support the film industry with the aim of making the country an AV production hub within Latin America.[93] As part of this it has adopted an investment friendly approach to regulation of VOD services.

Currently, Colombia is the 4th largest producer of feature films in the region, behind Mexico, Brazil and Argentina. The growth of the sector is seen in the increase in volume of film production: two decades ago, the Colombian cinema sector produced only 10 features films a year, currently this figure is 50 on average.[94] In addition, box office revenue is expected to continue growing at an average of 18% per year until 2026.[95]

The 2012 Film Act[96] aims to stimulate investment along the whole AV industry value chain and to create the enabling conditions for a "*progressive, harmonious and equitable development of national cinematography*" in Colombia.[97] It also intends to showcase the Colombian territory and cultural heritage as elements of AV productions encourage tourism and a positive image to the country.

In the Colombian market there is no quota or investment obligation applied to VOD services. Colombia offers two relatively generous automatic production incentive programs. It offers a 40% cash rebate for film services and 20% for logistics (Fondo Filmico Colombia (FFC)). This operates alongside a 35% tax credit for AV and logistics services (Certificado de Inversión Audiovisual en Colombia (CINA)).[98]

The automatic investment incentives have supported investment in the local audiovisual sector as a whole. According to an assessment of the CINA policy, since its implementation

92 El Confidencial, *La odisea de rodar pelis en Madrid: la ciudad es un caótico plato sin técnicos*: https://www.elconfidencial.com/espana/madrid/2022-04-26/rodajes-madrid-caotico-plato-sin-tecnicos_3411484/.

93 BizLatin Hub (2019), *Film Laws support growth in Colombian's film industry*: https://www.bizlatinhub.com/film-laws-support-growth-colombia-film-industry/.

94 El Tiempo (2017), *Colombia cuarto productor de cine en América Latina*: https://www.eltiempo.com/cultura/cine-y-tv/colombia-es-el-cuarto-productor-de-cine-en-america-latina-108210.

95 PwC, *Global Entertainment & Media Outlook 2023-2017, Colombia*: https://www.pwc.com/co/es/publicaciones/GEMO/2023/gemo2023.pdf.

96 Ley 1556 de 2012, *Por la cual se fomenta el territorio nacional como escenario para el rodaje de obras cinematográficas*: https://www.funcionpublica.gov.co/eva/gestornormativo/norma.php?i=48319#:~:text=Esta%20ley%20tiene%20por%20objeto,el%20desarrollo%20de%20nuestra%20industria.

97 Ley 814 (2003), *Por la cual se dictan normas para el fomento de la actividad cinematográfica en Colombia*: https://www.programaibermedia.com/wp-content/uploads/2013/06/Colombia-Ley-de-Cine-N-814.pdf.

98 The cash rebate applies to services provided by Colombian entities or Colombian nationals that are domiciled or residing in the country. The project must spend a minimum amount equivalent to 1,800 monthly salaries (approximately $450,000). The same applies for the tax incentive. CINA has an average budget cap and is transferrable. The annual budget cap is approximately $2mn for the FFC and $66.4mn for the CINA.

in 2020, around $107mn has funded 67 foreign AV works. These foreign works have achieved a historic foreign investment of almost $323mn. This means that for each $1 associated with CINA, approximately an additional $2 go back into the Colombian economy as foreign investment. This investment has created more than 20,000 jobs in 2022 and offered the opportunity to train and develop skills of local talent. In particular, AV works under the CINA mechanism have allowed Colombian professionals and technicians to be part of international productions which deepen and broaden the sector's skills base.[99]

However, as with other countries, there is evidence that increased demand for AV content has had inflationary pressures and some crew positions have been filled with people without the necessary experience and knowledge. A report on the effects of the investment incentives noted that higher education and further education institutions have been slow at responding to the increasing demand of Colombian workers in the sector, which has resulted in upward pressure on wages.[100]

5.2 Commentary

These case studies illustrate the different approaches to regulating VOD suppliers to support the investment in content. While all three countries have similar goals to promote investment in content and become a "hub" for investment, there are clear differences in approach. France has adopted the most onerous approach with very high local content quotas and very high financial obligations applied to VOD services. Spain has adopted a middle course with local content quotas set at the AVMSD floor (with an additional lower language quota) and lower financial obligations. Colombia has opted not to impose local content quotas or specific financial obligations on VOD services.

France's high investment obligations and high quotas should be seen as contextually specific to its longstanding policy to subsidise production of French theatrical content from content distributors (initially broadcasters, but more recently VOD suppliers). As new technology enabled entry by VOD services, France's policy was transferred to these new suppliers. However, while these policies have contributed to investment in production of local content, there are concerns that the approach distorts incentives away from producing high valued, attractive content, which earns revenues in international markets. Furthermore it has been suggested that the policies encourage a fragmented production sector that, with the exception of a small number of producers, cannot achieve the scale to compete internationally.

Spain and Colombia's approach to incentivising investment in local content appears to rely more on incentive-based policies which potentially have a less distorting impact. They aim to build the scale of the sector by attracting international investment, though place less emphasis on requirements on VODs for that investment to be culturally local.

99 https://locationcolombia.com/wp-content/uploads/2023/03/econometria-2.pdf

100 Idem.

All three countries have found that recent increases in investment in local content partly driven by content investments by VOD providers have led to inflationary pressures. In this context policy makers can act to help secure a viable future supply of skilled professionals to support the sector.

6 Conclusions

As governments around the world consider how to regulate new forms of content distribution (such as VOD), they need to consider whether, and if so how, to set policy to promote investment in local content production.

Government actions to increase production of local content (such as content quotas, financial obligations and selective support) have roots in policies that were applied to broadcasters in the 1980s. These policies were created at a time when markets were liberalising, enabling a degree of competition with national, state owned and funded services. However, scarce terrestrial broadcast spectrum inevitably limited the degree of competition and suppliers to a limited number of national broadcasters. Thus, policies at the time were targeted at the relatively small number of distributors with privileged market access; and technology limitations meant policies such as quotas were reasonably effective at influencing consumption and production.

Since these policies were introduced the context for regulation has clearly changed. In recent years the ability to distribute content over broadband networks has lowered barriers to entry to the benefit of consumers. Compared to the 1980s consumers now enjoy vastly more choice, innovation and high quality AV services. Competition between suppliers, including international competitors, has created the boom in content investment that continues today. However, it is right to ask whether the policies created decades ago are still needed, and if so, are they still the most effective and proportionate ways to incentivise investment in content.

While policy interventions in the AV sector can have both cultural and economic motivations, policy makers should consider the overall impact of any policy on the sector, which can include unintended costs and market distortions.

- Selective support, and associated financial obligations, are effective at channelling funding to production. However, these policies have created a complex bureaucracy which is becoming a barrier to entry in itself and adds to costs and risks of production. It also has inevitably influenced the incentives of producers, and has distorted their incentives to produce content to meet audience demand, leading to a high volume of low cost content aimed at a narrow audience, and a fragmented production sector.

- Content quotas aim to influence the consumption of content by "rationing" non-local content. However, while this may have been effective, to a degree, at influencing consumption of content in the 1980s when choice was limited to a few terrestrial broadcasters, the impact of quotas in the current world of on-demand content is more muted. To the extent that they influence broadcasters, they will tend to distort the programming decisions and lead to lower quality services.

The impact that these costs and distortions have on incentives to invest can be observed in the results of the analysis of economic outcomes presented in section 4, and in the case studies presented in section 5. The analysis presented in this report has the following implications for policy makers.

- First, it may not be necessary to apply restrictive policy to oblige broadcasters to invest in content. All content suppliers have strong incentives to invest in local content in order to meet the tastes of their customers. It is by investment in valuable local content that broadcasters or VOD services are able to differentiate their services and appeal to their audiences.

- Second, econometric analysis demonstrates that countries with more restrictive policies, in particular local content quotas, may see *lower* levels of investment in local content production. This is because onerous restrictions impose costs on commissioners that will ultimately affect their ability and willingness to invest.

- Third, if policy makers wish to promote investment in local content production, they should consider automatic production incentive policies. Automatic incentives are increasingly adopted around the world. They are effective at incentivising production, however, they do so in a way that minimises distortions. They are more targeted at the specific market failure: the high cost and high risk of content production. As incentives are “automatic”, they provide clarity and certainty to investors, on a timely basis, boosting investment.

While it is still too early to understand the impact of restrictive policies applied to VOD services, the experience of both Spain and Colombia suggest that incentive based approaches and a different approach to regulation have been successful in supporting the development of healthy AV ecosystems.

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