

## **Regulation of advertising in audio-visual media services: the impact on consumer protection, investments, innovation and competition**

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### **Abstract**

Europe's member states are in the process of implementing the 2007 Audio-visual media services Directive. This report addresses two implementation issues: the definition of non-linear services and the rules with respect to product placement. The definition of non-linear services (on-demand services) and the demarcation from linear services (television broadcasting) is relevant because a set of quantitative rules applies to linear services only. This concerns quantitative rules on advertising and European content. The second implementation issue - the regulation of product placement - is linked to responsibility and editorial independence, and the protection of programme makers and consumers. Member states can introduce a set of rules to ensure that product placement does not affect the responsibility and editorial independence of media service providers. For each implementation issue, two policy options have been formulated. An impact assessment method was used to assess the impact of each policy option on consumer protection, investments, innovation and competition. This approach reflects that media regulation can take into account several policy objectives.

### **1. Introduction**

The media landscape has seen drastic changes since the introduction of the Television Without Frontiers Directive (TWF) in 1989. Digital technologies have stimulated the convergence of technologies, services and markets such as television, internet access, internet services and telephony. The TWF Directive was not designed with these kinds of developments in mind. The directive applies to 'traditional TV broadcasting' via cable, satellite and terrestrial platforms but not to very similar services that are provided via internet. Convergence raised serious questions on the effectiveness of the TWF Directive in protecting consumers, stimulating the competitiveness of the European audio-visual industry, a level playing field and the single European market. The urgency to modernise the directive was increased by (unharmonised) national initiatives. Individual member states of the EU have introduced national solutions to address convergence, e.g. light regulation for on-demand services and self-regulation for specific types of internet services. National initiatives may distort the level playing field (between different platforms and between firms that are based in different countries) and can increase legal certainty and reduce competitiveness for European players.

In 2003 the EC started the process towards a new directive that is 'convergence proof.' The first draft of the Audio-Visual Media Service Directive (AVMS Directive) was presented in December 2005.<sup>1</sup> After several revisions, the final version has been approved by the European Parliament in November 2007.<sup>2</sup>

One of the most important changes from the TWF Directive is that the AVMS Directive no longer differentiates between services based on distribution platforms (cable, mobile, internet, etc.). This platform-neutral approach should allow traditional broadcasting services (that were regulated, e.g. with respect to advertising) to compete with similar services on the internet (that were not regulated). This level playing field objective is linked to the objective of consumer protection. Because different platforms can support the same type of services, it doesn't make sense to only protect consumers that use traditional platforms.

From now on, the distinctive feature to determine the rules that apply to audio-visual media services, is whether the service is considered linear (television broadcast) or non-linear (on-demand). Linear services will be regulated more strictly than non-linear services. The AVMS Directive has defined a minimal set of qualitative rules that are applicable to both linear and non-linear services. This is expected to provide a basic level of consumer protection. There are additional (quantitative) rules for linear services, e.g. with respect to advertising and European content/products.

Furthermore, the AVMS Directive loosens the rules for specific types of advertising such as product placement. Because product placement will be allowed (with certain restrictions) audio-visual media service providers can increase product placement revenues, to compensate for declining revenues from spot-advertising (commercial breaks between programmes and within programmes). Spot-advertising is the main source of revenues for many media players. It is expected that spot-advertising will become less effective and important due to time shifting and video-on-demand (Leurdijk et al., 2006).

To stimulate the competitiveness of Europe's audio-visual industry, the AVMS Directive seeks to improve harmonisation and to stimulate the internal market. The AVMS Directive has adopted the Country of Origin principle (CoO). If a firm is based in country A, the rules of country A apply to the firms and its services. This allows media services to provide services across borders, without being hindered by differences between national rules. The Country of Origin principle is not new in the context of media regulation. In 1989 it was added to the TWF Directive to facilitate satellite services that are distributed to the entire European market. However, this time the impact of the CoO principle will be much bigger. Audio-visual

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<sup>1</sup> EC (2005a) Proposal for a Directive of the European Parliament and of The Council amending Council Directive 89/552/EEC on the coordination of certain provisions laid down by law, regulation or administrative action in member states concerning the pursuit of television broadcasting activities.

<sup>2</sup> EC (2007) Directive 2007/65/EC of The European Parliament and of The Council of 11 December 2007 amending Council Directive 89/552/EEC on the coordination of certain provisions laid down by law, regulation or administrative action in member states concerning the pursuit of television broadcasting activities.

media services that are provided via the internet will be provided by many firms, to many consumers, located in many countries of the European Union.

Individual member states have to implement the AVMS directive in national legislation, within two years. Although the AVMS Directive has specified most issues, member states still have the freedom to define a number of concepts, to give an interpretation and explanation of European definitions, and to add elements that fit the national context. To some extent, this is due to ambiguity in the final text, the European consensus that was required, and the changes in the proposal that were made along the way.

Furthermore, due to ongoing (technological) innovation the AVMS Directive can never be complete and absolutely clear with respect to new developments in audio-visual markets. The technological and market context for the national implementation is different than the context for the first version of the European directive. One example is the preliminary impact assessment of the directive, in which the EC stated that advertising is not important for on-demand services (EC, 2005b). That same year YouTube was founded, and soon after many similar services that relied on advertising revenues were launched.

Because the AVMS Directive provides member states with some freedom for the national implementation, and because the market continues to evolve, it is important to explore the policy options in the national implementation of the AVMS Directive. This will be the main focus of this study. An impact assessment method will be used to structure the analysis. The method allows for effective use of insights from the European debate on the AVMS Directive, and the opinions of Dutch experts and policy makers. The impact of the AVMS Directive has been broadly debated after the publication of the first draft. The issues that were raised by member states are summarised in Hieronymi (2006). Academics have also contributed to the debate. The distinction between linear and non-linear services, for instance, has been questioned by Van Eijk (2007). The much feared consequences for the freedom of speech on the internet ('regulating the internet') have been addressed in the so called Budapest Declaration for Freedom on the Internet, a petition signed by many (mostly Eastern European) scholars in the media field. These and other sources are used in this study. The method is described in Chapter 2. The main objective of the study is to contribute to the discussion on the national implementation of the AVMS Directive, by means of exploring the policy options and the impact. This will be done for two complex implementation issues that are explored relatively seldom.

The first implementation issue is the distinction between linear and non-linear services. As mentioned above, non-linear services have more regulatory freedom than linear services. The definition of non-linear services will therefore have an impact on several media service providers and the AV industry in general. The second implementation issue concerns responsibility and editorial independence, which according to the AVMS Directive, should not be compromised by commercial interests. Still, it is not clear what this

exactly entails, leaving member states with some freedom to define and explain their notion of influencing editorial independence and responsibility.

Before we will move on to these two issues, we will shortly discuss a definition that also evokes interesting discussions. What is the definition of 'audiovisual media services'? The definition has been discussed in many European and national fora. The definition – and the critique – provides the context for the discussion in this paper.

The first draft of the AVMS Directive from December 2005 was criticised for multiple reasons. The most important critique was the ambiguous definition of audio-visual media services (Valcke et al., 2007; Arino, 2007). The discussion was fuelled by the thought - or rather anxiety - that services like YouTube, (personal) blogs, but also magazines and newspapers would have to comply with the AVMS Directive. After a series of alterations, the AVMS Directive signals that these kinds of services will probably not fall under its scope. The definition of AVMS is:

*"a service as defined by Articles 49 and 50 of the Treaty which is under the editorial responsibility of a media service provider and the principal purpose of which is the provision of programmes in order to inform, entertain or educate, to the general public by electronic communications networks within the meaning of Article 2(a) of Directive 2002/21/EC. Such an audiovisual media service is either a television broadcast as defined in point (e) of this Article or an on-demand audiovisual media service as defined in point (g) of this Article; and/or audiovisual commercial communication" (Article 1a).*

The definition refers to Articles 49 and 50 of the Treaty. Article 49 concerns the internal market; Article 50 concerns services that are provided by firms (rather than by governments or citizens). The final version of the directive can't take away uncertainty on the rules that will apply to a range of existing and emerging services. Technology and innovation will allow for online services where the roles of users and media service providers are entwined (e.g. shared responsibility of content production and selection), where commercial and non-commercial interests are blurred, and where the audiovisual element of a service can not be qualified as either high or low (e.g. online magazines).

Furthermore, it can be mentioned that one of the main objectives of the AVMS Directive is to protect consumers, with a special eye on youth. Services such as YouTube and online video games are extremely popular amongst young people. Video games - that provide highly immersive experiences - have adopted advertising in their 'game worlds'. It is likely that this type of services does not fall under the definition of audio-visual media services. This is not to say that this type of online services is not regulated at all. For example, firms that provide these services have to comply with the Unfair Commercial Practices Directive

(adapted in 2007) and the Directive on electronic commerce (2000). For example, the Directive on electronic commerce requires that providers of information society services (such as e-commerce and on-demand online services) must ensure that commercial information shall be clearly identifiable as such (Article 6a). The relevance of YouTube and online games for youth, and the relevance of other directives, illustrate the limitations of the AVMS Directive and the relevance of other European and national policies for the objectives that are mentioned in the AVMS Directive.

As mentioned above, Chapter 2 describes the impact assessment method, the steps that were taken, and the rationale behind them. In Chapter 3 we will address the first implementation issue: the distinction between linear and non-linear services. In Chapter 4 we will address the second implementation issue: responsibility and editorial independence. Both Chapter three and four will conclude with possible trade-offs. A specific policy option may provide both positive and negative impact. Chapter five presents the conclusions and policy recommendations.

## 2. Impact assessment method

In the context of OECD studies and EU policy making, impact assessment refers to the analysis of policy (options) on economic, social and environmental developments (OECD, 2001; EC, 2002). Policy is defined broadly, to include policy instruments such as regulation and self-regulation of products and markets, subsidies, coordination, etc. Impact assessment has become more important in EU policy making. A recent study by the Centre for European Policy Studies analyses the reasons behind this process (such as more political and public demand for accountability, evidence based policy and the need to explain the added value of EU policy), the methods that are used, the benefits and the problems (Renda, 2006). The study also mentions that impact assessment at the EU level is influenced by the rise of impact assessment and regulatory impact assessment in Europe's member states such as the UK and The Netherlands.

The rise of impact assessment is 'horizontal' in that it covers a range of policy domains and sectors. However, tradition and progress in impact assessment methods is stronger in policy domains such as environmental policy, infrastructure policy and R&D policy. Most relevant for this study – on the impact of advertising regulation - are the impact assessment methods that are developed for R&D policy and that are adapted for innovation in general.<sup>3</sup> Innovation here refers to all elements of the innovation process

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<sup>3</sup> Several handbooks provide an overview of methods to assess the impact of R&D policy/programmes. Three examples are: Fahrenkrog, G., Polt, W., Rojo, R., Tubke, A & K. Zincker (2002). *RTD Evaluation Toolbox. Assessing the Socio-Economic Impact of RTD-Policies*. IPTS report prepared by Joanneum Research and IPTS. Institute for Prospective Technological Studies (JRC-EC); Ruegg, R. & I. Feller (2003). *A Toolkit for Evaluating Public R&D Investment. Model, Methods and Findings from ATP's First Decade*. Prepared for Economic Assessment Office, Advanced Technology Program, National Institute of

and innovation system, not just technology and R&D (e.g. diffusion, adoption, incremental innovation, product innovation, services innovation and process innovation, by suppliers and users such as firms and universities).

The challenge for impact assessment studies is to actually link specific policies to specific types of impact. Are there causal or plausible links between specific policies (policy instruments or a set of policy instruments) and specific types of impact (such as investments, innovation, participation, growth)? Two main concepts are attribution and additionality. If a study would focus on a specific type of impact (e.g. innovation) the question is whether this impact can be 'attributed' to policy (and which policies) or to other factors. If a study would focus on one specific policy (e.g. a policy option or a programme that is evaluated) the question is whether policy leads to 'additional' developments (e.g. more or less investments and innovation than would be the case in the absence of policy). Does policy change the behaviour of firms, users and other targets and stakeholders, and hence the pace and direction of developments? In the context of R&D policy, the concept of 'behavioural additionality' is used to stress that policy can have impact 'via' the impact on incentives and behaviour of firms and other stakeholders.<sup>4</sup>

The method that was used in this study has a focus on the *mechanisms* via which policy options (for the regulation of advertising for audio-visual services) can have impact. The method is more about understanding than measuring. One of the comments of the Dutch Court of Auditors (*Rekenkamer*) on evaluation and impact reports by Dutch ministries is that the link between policy and impact should be assessed more thoroughly. Statistics on developments such as innovation plus a description of relevant policy do not suffice to claim that innovation increased *because of policy*. This comment was shared by the Dutch Cabinet.<sup>5</sup>

Figure 1 summarises the method and the steps (next page). Within each step, qualitative methods are used. This allows for an explorative and rich analysis, to acknowledge that policy is one of many factors (nothing more and nothing less), that several policies can play a role (the policy mix), that different mechanisms may be relevant, that different types of actors may respond differently to policy, and that different types of impact can be relevant (related to the objectives of policy as well as side-effects). In other studies, the method could be implemented in a more quantitative way (e.g. when the topic, the policy domain, the relevant types of impact (e.g. focus on one type of impact) and existing data allow for a more targeted and quantitative method). Furthermore, the explorative method could be a good way to

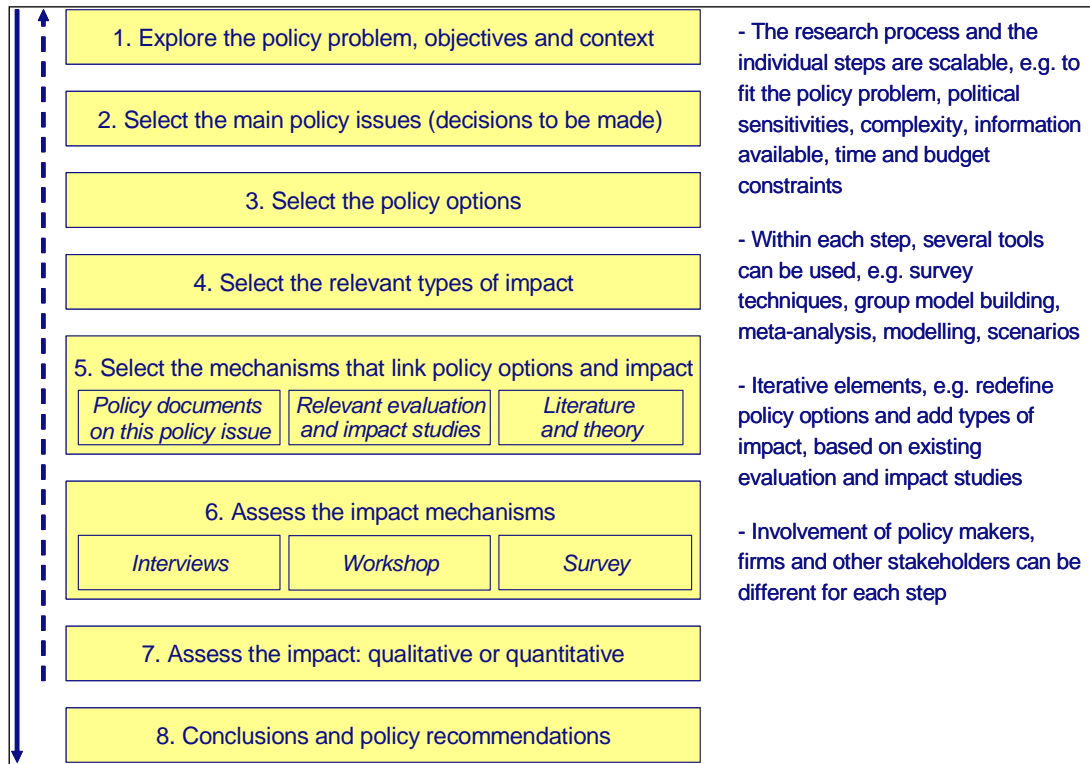
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Standards and Technology, US Department of Commerce; and Polt. W. and N. Vonortas (2006). *IST Evaluation and Monitoring*. Report for the EC;. Methods to assess the impact of innovation policy are described in: Arnold, E. and Guy, K. (1999). *Technology diffusion programmes and the challenges for evaluation*. Study / book chapter prepared for the OECD; OECD (2005). *Innovation Policy and Performance. A cross-country comparison*; and Louis Lengrand & Associates, PREST, ANRT and Reidev (2006). *Smart Innovation: A practical Guide to Evaluating Innovation Programmes*. Report for the EC.

<sup>4</sup> OECD (2006). *Government R&D Funding and Company Behaviour. Measuring Behavioural Additionality*.

<sup>5</sup> Tweede Kamer der Staten-Generaal (2005). *Staat van de beleidsinformatie 2005*. Verslag Algemene Rekenkamer en reactie kabinet. Vergaderjaar 2004-2005, 30116. Den Haag: Sdu.

identify the main factors and mechanisms ('to open the black box') and to select the factors and indicators to be used in quantitative methods such as statistics, econometrics, cost-benefit analysis and benchmarking.



**Figure 1:** Impact assessment method

The first step is to explore the policy problem, the policy objectives and the context. Starting with the opportunities of digital audio-visual media (economic, social and cultural), the importance of advertising revenues was acknowledged (e.g. for online services), in relation to several issues in the national implementation of the European Audio-Visual Services Directive. This was discussed between the researchers and the relevant ministries.

The second step is to select the main policy issues. Again, the relevant ministries were involved. We selected two complex and less explored issues, that have to be decided in the national (Dutch) implementation of the European AVMS Directive. The first issue concerns the definitions of (and the demarcation between) linear and non-linear AVMS services. More rules apply to linear services, so it makes

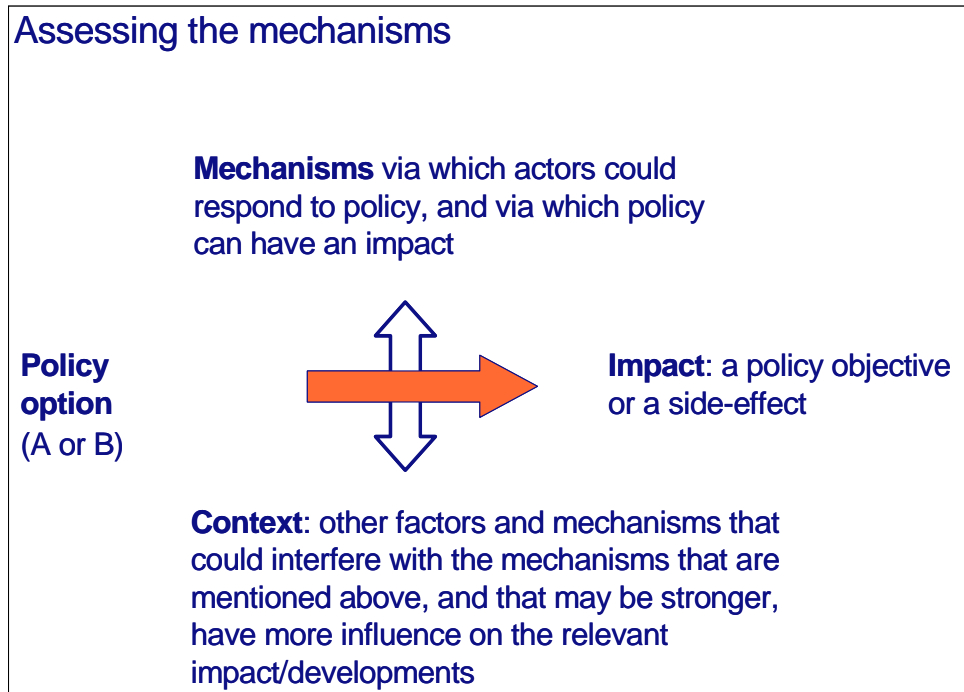
a difference whether services fall within the definition of linear services. The second issue is the definition of responsibility and editorial independence. The definition will influence how a service can be designed and provided so that the firm/provider can live up to the rules. The two issues are introduced and addressed in the next two chapters. It was expected that a third issue, the definition of audio-visual media services, would be discussed in several European and national fora, and that it would be touched upon when discussing the two issues of this study. This was the main reason for not selecting the definition of audio-visual services as the main topic for our study.

The third step is to define the policy options. For each of the two issues, the researchers defined an option that can be labelled as light or minimum intervention and a policy option that is more strict. This allows for a discussion whether and how each of the policy options influences mechanisms, whether this is effective, whether negative side-effects occur, and how other policy instruments can be more relevant for the impact/objectives. How the policy options are defined (e.g. two ends of a continuum, as is done in this study) and the number of options that are defined (e.g. two or three) will of course influence the analysis. For example, one of the comments on impact assessment by the EU is that three policy options are defined, which signals that the middle one is most effective or realistic (Renda, 2006).

The fourth step is to decide on the types of impact that are considered relevant and that are addressed in the study. The policy makers involved agreed on the selection of four impact domains: consumer protection, investments, innovation and competition. For each of the domains, more specific impact dimensions were selected, e.g. whether consumers can tell the difference between a commercial message and services/content with a clear responsibility and editorial independence of the provider, and whether service providers will locate, invest and innovate in countries other than the Netherlands.

The fifth step is to select the mechanisms - or the intervention logic - via which the policy options can lead to the relevant types of impact. The list of mechanisms is based on desk research of policy documents on this topic (e.g. the intervention logic in the AVMS Directive), existing evaluation and impact studies (such as impact assessment studies for the EC and Ofcom, the British communications regulator) and literature and theory (such as scientific articles on the AVMS Directive). One of the advantages of the method is that it explicitly builds on existing knowledge. The sources that were used have been mentioned in Chapter one. The mechanisms are selected and structured by the researchers, as will be demonstrated in the next two chapters, and summarised in Figure 2.





**Figure 2:** Assessing the mechanisms

For each type of impact (for each policy option) a set of mechanisms is selected that – individually or as a set – can lead to the type impact to be addressed. This is presented on the top half of the slide. To acknowledge and assess the relevance of other (contextual) factors and mechanisms, a set of ‘other mechanisms’ is presented under the label ‘context’. This is presented on the bottom half of the slide.

The sixth step is to assess the mechanisms. This was done in a workshop with policy makers and experts (for the first issue) and in interviews with policy makers and experts (for the second issue). Because the policy options lean towards different sides of one continuum, the first policy option (e.g. the light / minimum option) was discussed in detail, added by a brief discussion on how the second option would lead to different impact. The next two chapters contain the main slides that were used during the workshop, and that were circulated before the interviews. In a larger study, it would be possible to have both interviews and workshop for one issue, for example to validate the interview results in a workshop. This could be complemented by a survey (e.g. a survey among market participants). Because this study is no formal consultation, and because it concerns a pilot of an impact assessment method, no survey was conducted.

The seventh step is to assess the impact. This is a separate step that could be based on several methods and building blocks, e.g. the results of interviews and a survey. In this study, this seventh step was partly integrated with the sixth step. The workshop included the qualitative assessment for the first case, e.g. whether the policy options would have a small or large, positive or negative impact on consumer protection, investment, innovation and competition. Because the second case was analysed in interviews, the researchers did the overall assessment of impact. The seventh step includes the question whether any trade-offs emerge, when one policy option has both positive and negative impact.

The eighth step is to draw the main conclusions and to provide policy recommendations. This was done by the researchers, based on the workshop and interviews, and validated by the policy makers that were involved in the study.

The next chapter will present the policy options and the analysis for the first issue in the Dutch implementation of the European AVMS Directive. The fourth chapter will address the second issue. Chapter five presents the main conclusions.

### **3. Linear and non-linear audio-visual media services**

#### **3.1. Introduction and policy options**

The answer to the question whether a media service is considered to be linear or non-linear determines the rules that apply to the service. Both types of audio-visual media services have to comply with a minimal set of qualitative rules. The services have to respect human dignity, they may not incite hate or discrimination. There are rules to protect minors. Furthermore, surreptitious and subliminal advertising is prohibited. There are additional rules for linear services. These concern quantitative rules regarding the length and frequency of commercial breaks, and quota for European and independent productions.

The AVMS Directive provides a definition of linear and non-linear services (see below). The definition can not avoid that some existing and emerging services will be hard to categorise as either linear or non-linear. To some extent, the line between linear and non-linear services can be clarified in the national implementation of the European AVMS Directive. The definition in national laws and regulations, but especially the explanation, examples and interpretation will have an influence on how services are categorised, and hence which set of rules applies to a service. As was mentioned above, if a service is considered non-linear, less rules and restrictions apply. In this chapter we will discuss two policy options

for the demarcation between linear and non-linear services, and we will assess the impact on consumer protection, investments, innovation and competition.

The definitions in the AVMS Directive (EC, 2007) are:

- Linear (or: television broadcasting): *'television broadcasting' or 'television broadcast' (i.e. a linear audiovisual media service) means an audiovisual media service provided by a media service provider for simultaneous viewing of programmes on the basis of a programme schedule* (Article 1, sub e);
- Non-linear (or: on-demand): *'on-demand audiovisual media service' (i.e. a non-linear audiovisual media service) means an audiovisual media service provided by a media service provider for the viewing of programmes at the moment chosen by the user and at his individual request on the basis of a catalogue of programmes selected by the media service provider* (Article 1, sub g).

The definitions indicate that the main difference between linear and non-linear is the degree to which the user is in control: in control of *what* he sees and *when* he sees it. The AVMS Directive also has some additional characterizations, most importantly that the influence from linear services on society is much bigger than the impact from non-linear services, although it doesn't elaborate upon this idea. Societal impact appears to matter for the categorisation and hence the rules that apply.

We have defined two policy options for the definition and explanation of *non-linear services*.

<b>A – Broad</b>	<b>B – Narrow</b>
The viewer has some influence on the moment he or she watches a programme	The viewer chooses a specific moment to watch a programme
The viewer chooses one programme or a pre-selected set of programmes (whole evening) or asks another viewer or the media service provider to make this selection for him/her, based on personal preference	The viewer himself chooses one programme, or every single programme in a set
The size and availability of the catalogue is irrelevant	The programmes must be part of a substantial catalogue and must be available for a specific minimum period (e.g. a month)
The catalogue is organized according to tips and preferences of the media service provider or third parties	The selection and organisation of the catalogue is done by the media service provider alone
The size of the audience is irrelevant. Programmes may be watched simultaneously by one or many viewers	The programme cannot be watched or paused simultaneously with other people

We have labelled option A 'broad' and option B 'narrow'. In option A, non-linear has been explained in such a way that almost anything but traditional broadcasting will be considered non-linear. This implies that many services in the grey area between linear and non-linear will be categorised as non-linear and hence that these services only have to comply with the basic set of qualitative rules (not with the quantitative rules). Option B is a narrow definition and explanation of non-linear services which implies that many services in the grey area between linear and non-linear will be categorised as linear and hence that these services have to comply with the qualitative and the quantitative rules (including the restrictions on the length and frequency of commercial breaks and the quota for European and independent productions/content).

Below, we visualise that a choice between policy option A and B - how to draw the line between linear and non-linear services? – will influence the number of AVMS services that qualify as linear rather than non-linear. As was mentioned above, this paper does not address the line between AVMS services and other services.

<b>Policy option</b>	<b>Audio-visual media services</b>		<b>Other services (non-AVMS)</b>
<b>A</b>	Linear services (television broadcasting)	Non-linear services (on demand)	E-commerce, text only, non-professional, non-public, etc.
<b>B</b>	Linear services (television broadcasting)	Non-linear services (on demand)	

Policy option B implies that - compared to policy option A - more services will qualify as linear services, to which a set of quantitative rules apply.

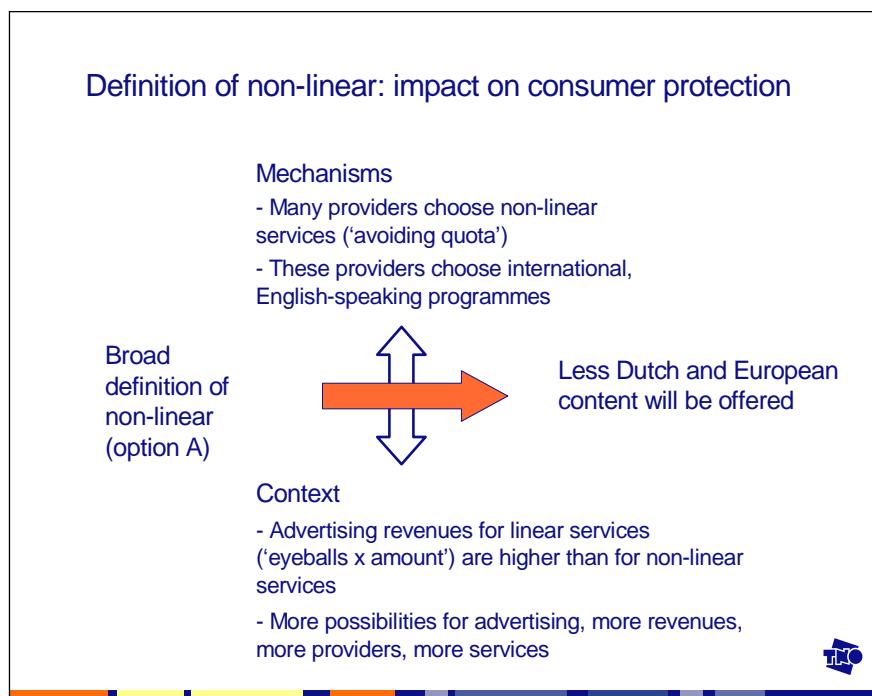
In this chapter we will discuss the impact of option A on consumer protection, investments, innovation and competition. In general, the impact of option B can be derived from the discussion of option A. Whenever appropriate, we explicitly discuss the impact of option B.

### **3.2. Consumer protection I**

#### *Pluralism and the quantity of national and European products*

As discussed in Chapter 2 we have captured arguments that we have encountered in our desk research in the following slide. It summarises the mechanisms behind the main hypothesis on impact (top half of the slide) and presents some context and mechanisms that may interfere. The slide was used as a starting

point for the discussion in the expert workshop. Consumer protection is defined broadly, to include topics such as commercialisation, advertising that is recognisable (rather than mixed with editorial content) and media pluralism. The first consumer topic to be discussed is the impact of the national implementation of the AVMS Directive on pluralism and – especially – on the quantity of national and European products/content.



**Figure 3:** Definition of non-linear: impact on consumer protection

#### Hypothetical impact

*A definition of non-linear that will cover almost anything but traditional broadcasting, will result in a decrease in the quantity of Dutch and European content” because:*

- most media service providers will provide non-linear services as this will free them from quota regarding European and independent productions. Media service providers will use this freedom, and;

- in the selection and production of content, media service providers will choose internationally orientated, English-spoken productions.

On the other hand,

- it is still questionable whether the advantages of non-linear services (e.g. less rules) compensate for the loss of a mass-sized audience. To target mass markets, e.g. with national content, remains a lucrative strategy. A service provider that (completely) leaves the linear realm and focuses on on-demand services, with more targeted yet smaller audiences, could earn less revenues than a mass media player;
- another mechanism is that the rise of non-linear services – with few rules and relatively large commercial freedom – will increase the overall advertising revenues of the sector. More revenues could lead to more media service providers, more services, new services and more revenues, which can result in more national and European productions.

## Conclusion

In general, the quantity of Dutch and European content (and its contribution to pluralism) is not expected to suffer from a broad definition of non-linear audio-visual media services (option A). The opposite effect might even be more likely. Firms will benefit from option A (nearly all new services will be classified as non-linear) and will explore this commercial flexibility. This includes new services and existing services that include national and European content.

One could argue that a narrow definition of non-linear (option B) does not stimulate national and European content. If a substantial number of (new) services will be classified as linear, the quota on European products/content apply to these services. This seems to have a positive impact on media pluralism. However, many linear services target the biggest possible audiences, with content that appeals to the 'average viewer' and that includes content that is cheap to buy or make. Yes, this will include European and national products/content but the quota do not influence the quality of the content.

#### About the mechanisms

Adopting a broad definition - that will result in less services for which quota apply - will mean more commercial flexibility, a broader range of services and content (Dutch, European, US, different genres) with more choice for users.

Users are still interested in Dutch (and European) content, including regional and local content. Therefore foreign programmes will not necessarily be a substitute for national (or European) productions.

Product placement as a means to generate revenues will become more important. Dutch advertisers that target Dutch audiences will not be able to apply product placement in non-Dutch programmes. The need of (Dutch or European) media producers and service providers to use product placement as a means of financing their productions provides an incentive to produce (or buy) Dutch content.

Not all business models depend on advertising. Paid content may become more important, e.g. pay-TV packages via cable and satellite and paid content on the internet.

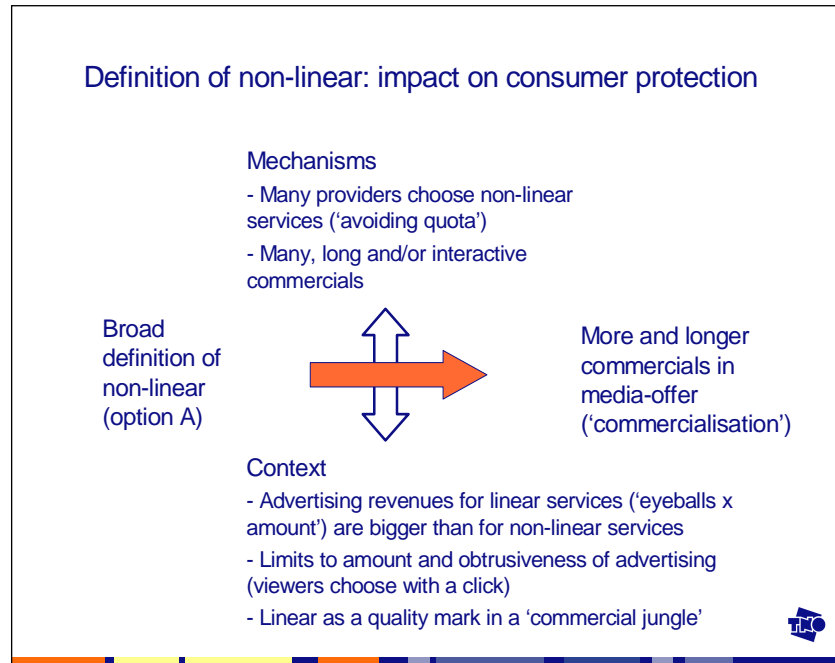
A broad definition of non-linear might indeed provide a small incentive for firms to introduce non-linear services (or to adapt services in order to fall within the category of non-linear services) and to exploit the freedom in the amount of advertising. However, traditional linear services still reach mass markets. Linear services are still (the most) interesting for advertisers. This is highly relevant for advertising for products that are used by large parts of the population.

It's difficult to assess how consumer preferences are different in a linear and non-linear context. For example, US or UK produced series may be prominent in TV schedules but may also be among the favourites in on-demand services on the internet. The preferences of users, the variety of content (e.g. on the internet) and the combined use of different platforms and services by users, must be taken into account when discussing the offering of Dutch and European content.

### **3.3. Consumer protection II**

#### *More advertising and commercialisation of the media landscape*

The following slide was used to structure the discussion.



**Figure 4:** Definition of non-linear: impact on consumer protection

#### Hypothetical impact

*A definition of non-linear that will cover almost anything but traditional broadcasting, will lead to an increase in both frequency and length of advertising. Because:*

- Most (new) media services will be positioned as non-linear services since this allows service providers to avoid quota for the frequency and length of advertising.
- Media service providers try to maximize their revenues by showing more and longer commercials and also by experimenting with new forms of (interactive) advertising.

On the other hand,

- Advertising revenues for linear services - that are still able to reach mass audiences - are bigger than advertising revenues for non-linear services. This is an incentive for media service providers to stick with more traditional, linear services.



- Secondly, if the quantity of advertisements will grow substantially, this will become a nuisance for users. They will switch to competing services with just one click of the mouse (or the remote control).
- Thirdly, to clearly present a service as a non-linear service – with more rules and restrictions – could become a quality mark in a commercial jungle. Users know that the amount of advertising will not be excessive.

## Conclusion

The choice for a broad or narrow definition of non-linear services will not affect consumer protection with respect to the frequency and length of advertising. Many firms will provide linear services (with a maximum amount of advertising) to target mass markets. Providers of non-linear services have incentives to prevent excessive advertising and to explore well received types of advertising such as product placement.

## About the mechanisms

When discussing the consequences for consumers, it is very important to take into account the perceptions of consumers with respect to different types of advertising. New types of advertising, such as product placement, are perceived less negatively than old fashioned commercial blocks. In fact, when people enjoy a certain programme, they are more likely to enjoy the product placement as well. Product placement is perceived more positively in non-linear services because users have chosen the non-linear (on-demand) service. Linear services – and the product placement in linear services - are more obtrusive. Furthermore, on-demand services allow for targeted forms of advertising, based on (aggregated) characteristics of viewers. If advertising is better targeted, it will be perceived as less obtrusive and negative.

Media service providers always try to optimize advertising revenues, both in quantity and in (new) forms of advertising. Optimise does not equal maximise. If the quantity of advertising will stretch viewers' tolerance to the limits, media service providers will loose viewers. People accept advertising in non-expensive linear services or free internet services, but they are less willing to tolerate advertising in paid services (linear or non-linear). Furthermore, to increase the quantity of advertising can devalue the

value of every individual advertisement. Service providers have an incentive to maintain scarcity (and high prices) in the context of specific programmes, e.g. one sponsor of a programme and not more than 10 advertisers before a programme starts. As a result, stretching the amount of advertising might not be the most profitable option.

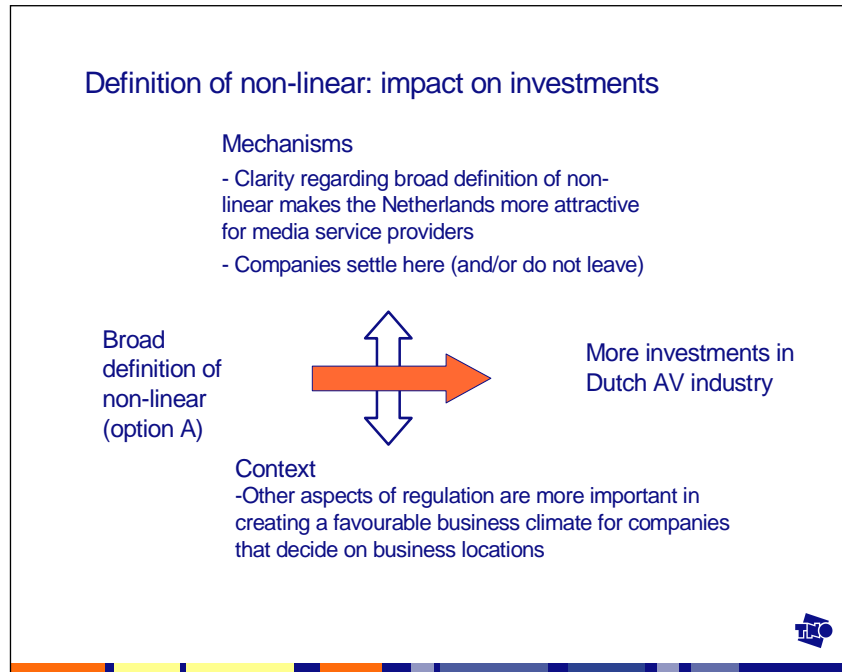
A linear service with limited advertising will not be a safe haven and a quality mark in the jungle of linear and non-linear services. This mechanism was not recognised. Many users will not differentiate between linear and non-linear services. Furthermore, several types of advertising play a role and advertising can be inserted without irritating users.

To use advertising-free content might become a privilege for the people who can afford to pay for the content. This leaves a substantial part of society that will only be able to consume advertising-funded media services. The difference between user groups (old-young, rich-poor, digital literacy, etc.) must be taken into account when assessing the impact of advertising.

There are uncertainties as to how advertising rules – such as quota – apply to linear services in an online environment. Advertisements can be loosely linked to the content, for instance banners next to videos rather than advertisements that precede the programme. These uncertainties have to be tackled before a more strict policy option (such as option B) can be expected to have an impact.

### **3.4. Investments**

The following slide was used to structure the discussion.



**Figure 5:** Definition of non-linear: impact on investments

#### Hypothetical impact

*A definition of non-linear that will cover almost anything but traditional broadcasting, will increase investment in the Dutch AV industry. Because:*

- A broad definition of non-linear services gives more regulatory certainty - any service in the grey area will be labelled a non-linear service - which makes the Netherlands a more attractive place for firms to locate and invest.
- A broad definition of non-linear services gives companies more commercial freedom when it comes to advertising and European products/content, which makes the Netherlands an attractive place for firms to locate and invest.
- New companies will settle in the Netherlands and the existing ones will not leave.

On the other hand,

- Other elements of the policy and regulatory framework are more important for investment decisions than possible exemptions from quota on advertising and national and European products.

## Conclusion

A broad definition of non-linear services could give a country an edge over countries that will apply a more strict definition. However, this element of the regulatory framework is only one of many factors to attract new firms or to keep firms within the country. Other factors include financial regulations, infrastructure and available competences. Still, when two countries are highly similar with respect to the business climate, media regulation and a broad definition of non-linear services could do the trick. The effect is small and depends on the decisions that are made in other European countries.

## About the mechanisms

The implementation of a broad definition of non-linear services (option A) could be one of the factors to attract new firms or to keep firms within the country. A narrow definition (option B) may have the opposite effect. This might be especially relevant for media service providers from non-member states who are looking for a location in Europe from which they can hold office to serve markets in several countries (e.g. a US or Indian media service provider).

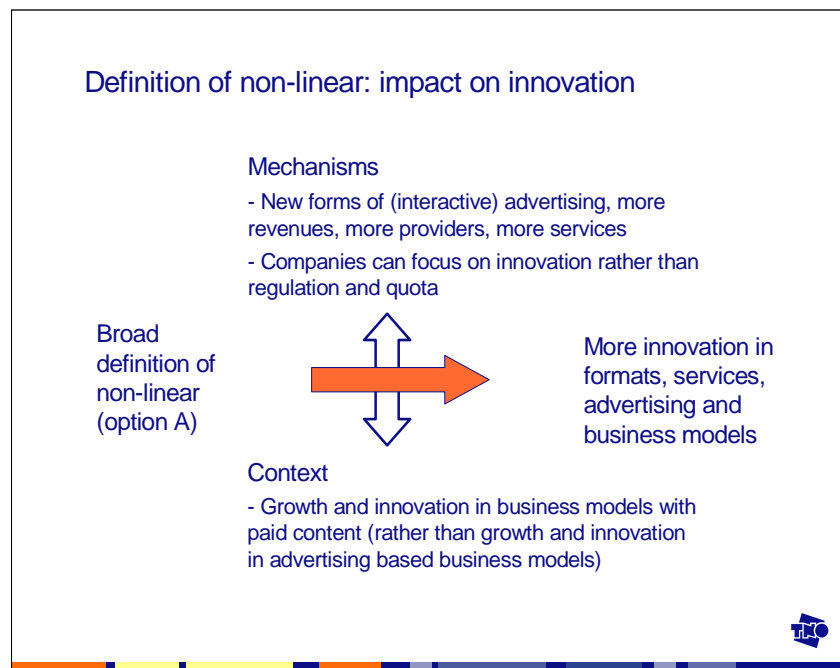
With respect to location, investments and innovation, it must be mentioned that media service providers often combine linear and non-linear services. The Netherlands (e.g. Endemol) has a good position in media formats for linear services, including linear services that include interactive elements (e.g. voting) and that are combined with on-demand services. For investment decisions, the regulatory framework for both non-linear and linear services is relevant. A broad definition of non-linear (with many new services being classified as non-linear) will make the regulatory framework more appealing to firms. Investments in non-linear services could trigger investments and innovation in linear services.

It is impossible to know what the media industry will look like in five years. Therefore, a broad definition of non-linear will be more likely to hold in the future: any service in the grey area between linear and non-linear will be labelled a non-linear service. Future proof policy, with legal certainty, is known to stimulate investments.

Media regulation is one of the factors that influences location and investments decisions. Media service providers – especially those that are not yet located in the Netherlands - might be more sensitive to other incentives. This includes financial regulations, infrastructure, available competences and other facilities. A less strict regulation will only be an advantage if these 'basic' requirements are sufficiently covered. It's the combination of AVMS regulation and other factors that has to attract media service providers. Furthermore, regulation regarding the definition of non-linear can only create a competitive advantage for the Netherlands if other countries implement a more strict definition.

### 3.5. Innovation

The following slide was used to structure the discussion.



**Figure 6:** Definition of non-linear: impact on innovation

### Hypothetical impact

*A definition of non-linear media services that will cover almost anything but traditional broadcasting, will result in more innovation in formats, services, advertising (tools and formats) and business models.*

Because:

- A broad definition of non-linear services will allow for more and new forms of advertisements, which will lead to increasing revenues, more media service providers and more media services. This will create a virtuous circle of more innovation in the field of formats, media services, advertising and business models.
- A broad definition of non-linear services will allow start-ups to focus on innovation rather than checking which definitions, rules and quota apply to their services.

On the other hand,

- There could be more innovation in paid services and business models than in advertising based services and business models. For example, innovation in micropayments and subscription models can be more important than innovation in product placement.

### Conclusion

In this case, the general principle applies. The light and clear regulation of option A (nearly all new service will be classified as non-linear services) provides for more commercial freedom and innovation. As was mentioned earlier, regulation is one of many factors. The extent to which a broad definition of non-linear will lead to (radical) new formats, services, advertising techniques and business models, is influenced by user demand, entrepreneurship and other factors. Still, a broad definition of non-linear service allows for more innovation in the non-linear domain. It also allows for more innovation in formats and services that explore the synergy between the linear and non-linear domain.

#### About the mechanisms

If media services providers don't have to worry about regulation, they can focus more on innovation. This applies to large firms and especially to small (new) firms. This can benefit non-linear services as well as linear services.

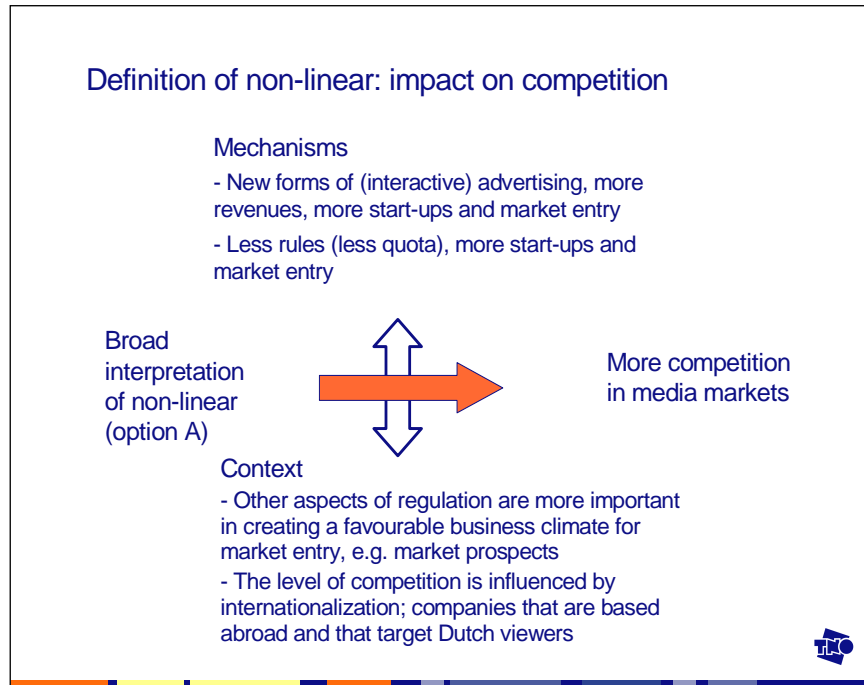
A focus on innovation does not necessarily mean that media service providers will only create new, revolutionary formats, e.g. to be piloted from/in the Netherlands and to be exported to other countries. Firms will still cater to popular demand and the general public might not be ready for too much change. For more than ten years, interactive television has been hailed as the next big thing, but it still failed to appeal to a mass audience. Even in the non-linear domain, most popular are premium series and films that were produced for traditional linear TV channels.

Innovation in business models and in advertising (tools and formats) will also be influenced by viewers/users and other factors. Still, a broad definition of non-linear services will provide more commercial flexibility to firms that innovate in business models and advertising.

Furthermore, it is questionable whether the total advertising revenues of the media industry will continue to increase and – especially – whether these revenues will be used for innovation. Whether money is available for innovation, and how the money is spent, is also influenced by other policies and by factors such as shareholders and entrepreneurship.

### **3.6. Competition**

The following slide was used to structure the discussion.



**Figure 7:** Definition of non-linear: impact on competition

#### Hypothetical impact

*A definition of non-linear media services that will cover almost anything but traditional broadcasting, will lead to more competition in media markets. Because:*

- A broad definition of non-linear services will allow more and new forms of advertisements, which will lead to more revenues and more start-up media service providers and market entrants.
- A broad definition of non-linear services will allow large and small firms to focus on innovation rather than regulation and quota. Especially for small (new) firms, light regulation may be crucial, given the lack of skills and scale to address legal issues (e.g. no legal department).

On the other hand,

- The number of market entrants is predominantly determined by other factors than regulation.



- Competition mainly comes from international companies that target Dutch viewers from abroad. They target Dutch consumers while respecting the rules in their country of origin.

## Conclusion

The experts assessed that competition is probably not influenced by the definition of non-linear services. If there is an impact, it is likely to be small (e.g. less burdens (red tape) for small firms). It may also have a small and negative impact on the level playing field between traditional broadcasters and firms that provide similar services via the internet. It may also have a small and negative impact on competition between firms that operate from the Netherlands and firms that operate from other European countries. This is relevant for competition between countries (the competitiveness of the Netherlands) rather than competition between firms in the market. The decisions taken by other member states will also influence whether a European level playing field will emerge.

## About the mechanisms

The experts recognised the mechanism related to a broad definition of non-linear services. More and new forms of advertisements, increasing revenues, more start-ups and market entrants can increase competition. However, the impact was assessed as uncertain. For instance, the size of the media market and the advertising market will not grow due to a definition in the law. The pie may be rearranged but this need not stimulate entry and competition.

The second mechanism was assessed as relevant yet small. Especially for small (new) firms, light regulation is crucial, given the lack of skills and scale to address legal issues. Small firms will not have a legal department and they may be reluctant to hire lawyers.

It was mentioned that most media service providers have adopted cross media strategies, offering both linear and non-linear services. This combination is becoming more important. Competition between media service providers is becoming more complex, e.g. linear against non-linear, competition between individual services and between bundles, competition between firms that operate from the Netherlands and firms that operate from abroad, and competition between different platforms (such as internet).

From the perspective of the Netherlands - and competition between countries - a broad definition of non-linear media services may be useful to attract firms. However, foreign media service providers might be

more sensitive to other incentives, like financial regulations, infrastructure, available competences and other facilities. See above the section on investments.

With respect to a level playing field, it was mentioned that services in the online domain may be designed to fall under the definition of non-linear services, whilst competing head-on with traditional broadcasters. The possibilities to tilt the level playing field are higher with a broad definition of non-linear.

Furthermore, it is questionable whether competition is something to strive for when it comes to pluralism, as too much competition will stifle diversification in the media market (ruinous competition).

### **3.7. Conclusion**

A broad definition of non-linear (option A) implies that almost anything but traditional broadcasting television will be regarded as non-linear rather than linear. This means that relatively few services will have to comply with the quantitative rules that apply to linear services (limits to advertising and quota for European and independent content). The analysis demonstrated that this does not lead to less consumer protection. This is mainly because firms will explore the commercial flexibility, with a mix of existing and new services, with national, European and non-European content. Media pluralism need not be affected. A broad definition of non-linear (option A) is expected to not harm consumer interests with respect to the frequency and length of advertising. Many firms will provide linear services (with rules on the maximum amount of advertising) to target mass markets. Providers of non-linear services have incentives to prevent excessive advertising and to explore well received types of advertising such as product placement.

With respect to investments, it was concluded that a broad definition of non-linear services could give a country an edge over countries that will apply a more strict definition. When two countries are highly similar with respect to the business climate, media regulation and a broad definition of non-linear services could make a country slightly more attractive for firms to locate their business and to invest. The effect is small and depends on the decisions that are made in other European countries. It was acknowledged that this element of the regulatory framework is only one of many factors to attract new firms or to keep firms within the country.

A broad definition of non-linear may also stimulate innovation. To some extent, this is because the Netherlands is more attractive for business (see above). To some extent, this is because firms know that nearly all new services will be classified as non-linear services. This provides more commercial freedom and innovation. Again, regulation is one of many factors. Still, a broad definition of non-linear service

allows for more innovation in the non-linear domain. It also allows for more innovation in formats and services that explore the synergy between the linear and non-linear domain.

The impact on competition in media markets is uncertain. There can be an impact on the level playing field in Europe, but this depends on the implementation of the AVMS Directive in other member states.

Because the impact assessment method allows for an analysis of several policy objectives (several types of impact) some experts expected that the analysis would reveal a trade-off between consumer protection and business interests. This has not been the case. Option A – a relatively light and business friendly option – does not provide policy makers with a difficult trade-off between the interests of consumers and the media sector, or a trade-off between the interests of different segments of the media sectors.

#### **4. Responsibility and editorial independence**

##### **4.1. Introduction and policy options**

From the first sketches in 2003 to the final version that has just been passed by the European Parliament, the AVMS Directive has contained a number of ambiguous terms regarding advertising. One example is thematic placement. This has been a topic in the first version of the directive and in the discussions on advertising. There is no definition of thematic placement in the final version of the AVMS Directive.

Thematic placement has been discussed in combination with product integration. Product integration is defined as: *"The intervention of any undertaking or body in the plot of a film or fictional programme seeking to promote in particular a product, service or brand"* (Amendment 72 EP First Reading).

Although thematic placement, as a term, has made it into the final version, its definition did not. The term product integration is not mentioned in the final version. Because the AVMS Directive doesn't contain a definition of thematic placement, it's also difficult to determine its relation to product placement. Based on the draft versions of the directive it is very likely that thematic placement is a specific type of product placement. Whereas 'normal' product placement is about showing a product or brand in a service (e.g. an actor that is drinking Coca Cola), thematic placement involves more subtle influence of advertising on the plot (e.g. actors that always meet in a bar, that always drink beer, including Heineken). This implies that the influence of thematic placement can be substantial yet difficult to recognise for viewers/users. There have been similar discussions on sponsoring.

The AVMS directive explains that product placement can not have (too much) influence on the responsibility and editorial independence of service providers (and programme makers) and that the

influence must be made explicit to viewers/users. The directive states that product placement must be mentioned at the start of a programme. Furthermore:

*"The programmes that contain product placement shall meet at least all of the following requirements: (a) their content and, in the case of television broadcasting, their scheduling is in no circumstances influenced in such a way as to affect the responsibility and editorial independence of the media service provider" (Article 3g).*

A similar description is used to describe the limitations regarding sponsoring. Member states may choose to waive these requirements if the programme in question has not been produced or commissioned by the media service provider (e.g. a programme that has been produced for the US market). In another paragraph the AVMS Directive mentions that Member states can further specify the idea of editorial responsibility themselves, as well as of 'effective control':

*"The notion of editorial responsibility is essential for defining the role of the media service provider and thereby for the definition of audiovisual media services. A definition of editorial responsibility is therefore also required. Member states may further specify aspects of this definition, notably the notion of 'effective control', when adopting provisions to implement this Directive. This Directive is without prejudice to the liability exemptions established in Directive 2000/31/EC of the European Parliament and of the Council of 8 June 2000 on certain legal aspects of information society services, in particular electronic commerce, in the Internal Market (Directive on electronic commerce)." (preamble 23).*

Here, the Directive refers to editorial responsibility whereas the articles on product placement and sponsoring refer to *responsibility and editorial independence*. This is a slightly different phrasing. It is clear that there is room for national interpretation, definitions and explanation. The AVMS Directive clarifies that responsibility and editorial independence concern the actual content of media services, but also the selection and programming of the content. It is not explained what this means in detail, and in which situations product placement or sponsoring are considered as a breach of the responsibility and editorial independence (too much control for advertisers).

The AVMS Directive allows member states to define a set of rules regarding product placement, to prevent influence on responsibility and editorial independence. Existing Dutch media regulation contains rules on specific do's and don'ts regarding the blending of editorial content and advertising. This includes rules on zooming in on products, mentioning the advantages of products, the name of products, etc. Ofcom, the

British communications regulator, has addressed this issue with a focus on 'undue prominence.' If advertising elements have found their way in editorial content, there must be editorial justification rather than a commercial deal: "The way in which a brand is presented or referred to in a programme should not be subject of negotiation or agreement with any supplier"<sup>6</sup>.

We have defined two options with respect to responsibility and editorial independence and the influence of product placement (see below). Option A is labelled 'A strict set of rules.' This option consists of a set of strict, detailed and clear rules. This option is inspired by the current Dutch legislation in which product placement is prohibited. This option also includes a detailed yet clear national implementation on how users/viewers are informed about product placement. This is combined with the obligation for media service providers to publish a programme statute, to protect consumers and to protect programme makers vis-à-vis management and advertisers.

Option B is labelled 'Focus on final responsibility.' Option B is less detailed and provides more freedom for media service providers and advertisers. The focus is on the final responsibility by media service providers when it comes to the selection, organisation and actual content of media services. In some cases, there can be influence by advertisers, as long as the final decisions and responsibility remains with the media service provider and the programme makers. Undue prominence is – of course – not allowed but the focus is on the clear and explicit promotion of products. The main example is to provide sales information such as product characteristics, price, availability, etc. In option B, media service providers can decide how to inform users/viewers about product placement. Furthermore, a programme statute is not compulsory.

In this chapter we will discuss the impact of option A – a strict set of rules – on consumer protection, investments, innovation and competition. The discussion had a clear focus on product placement. Elements of the discussion are relevant for sponsoring since sponsoring – like product placement – needs to respect responsibility and editorial independence.

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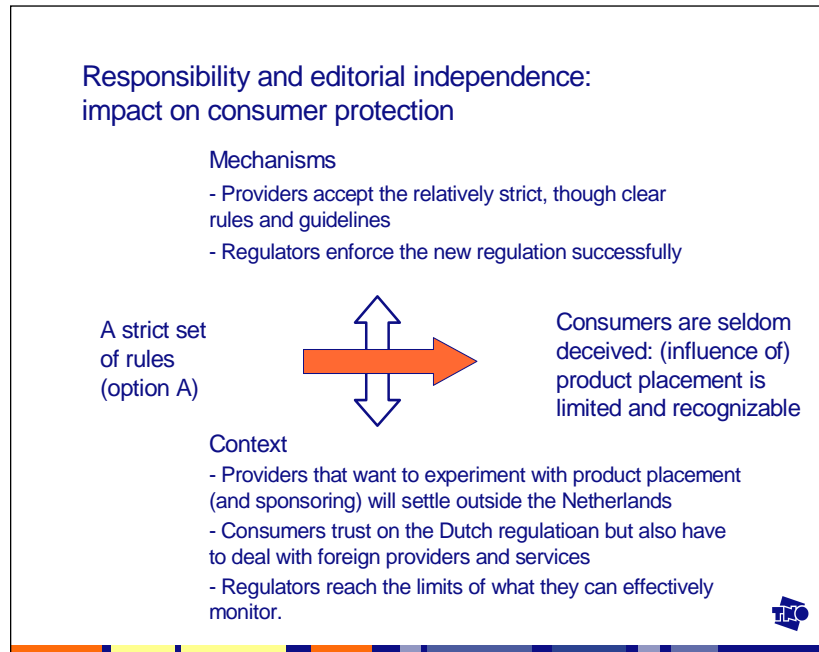
<sup>6</sup> Ofcom (2007). Guidance Notes. Section 10: Commercial References and Other Matters, 13 December 2006.

<b>A – A strict set of rules</b>	<b>B – Focus on final responsibility</b>
"responsibility and editorial independence" can be observed from the selection and content of media services	"responsibility and editorial independence" refers to the final responsibility by media service providers
No undue prominence: rules and criteria that are inspired by the current Dutch media regulation	No undue prominence: focus on sales information (that is not allowed)
Programme statute is compulsory	Programme statute is not compulsory
Viewers must be informed according to strict rules defined in Dutch media regulation	Viewers only have to be informed according to the specifications in the AVMS Directive

#### 4.2. Consumer protection I

##### *Non-surreptitious advertising*

The following slide was used for the discussion in the interviews.



**Figure 8:** Responsibility and editorial independence: impact on consumer protection

Hypothetical impact

*A strict set of rules on product placement will guarantee better protection for consumers; they will be misled less often because product placement will be limited and recognizable. Because:*

- Media service providers accept the strict yet clear rules.
- Regulators enforce the rules successfully.

On the other hand,

- Media service providers who want to experiment with product placement (and sponsoring) will settle outside the Netherlands, while still targeting the Dutch audience.

- Consumers will trust Dutch regulations ('content is based on editorial motives rather than the influence of advertising') but not all content is originated from the Netherlands, not even all content that is primarily aimed at Dutch consumers.
- Regulators can only monitor a certain amount of media services. They reach the limits of what they can effectively monitor, which creates possibilities and uncertainties for firms, and a false sense of protection for consumers.

### Conclusion

A set of strict and clear rules on product placement (option A) will increase the level of consumer protection. Firstly, strict rules can lead to less product placement. If product placement is applied, a strict set of rules will decrease commercial influence and increase editorial independence. It was mentioned that *very* strict rules will create incentives to 'hide' product placement. This comes at the expense of consumer protection, even if regulators can identify subtle and illegal types of product placement. Secondly, a programme statute can protect programme makers (*vis-à-vis* media service providers and advertisers). Indirectly, the independence of programme makers has a positive impact on the protection of consumers. Thirdly, it is important to assess whether consumers are aware of the distinction between editorial content and advertising. Nearly all consumers know that media services in general contain product placement, but 28% can't pinpoint product placement in specific programmes. The most effective way to guarantee consumer protection is a mix of clear rules on how to inform consumers that a programme contains product placement, to make programme statutes obligatory, and to stimulate media literacy.

### About the mechanisms

The main mechanism is that strict rules on product placement will lead to better consumer protection. A strict set of rules may decrease the volume of product placement (some advertisers switch to other types of advertising) and will decrease the number of services/programmes where editorial independence and responsibility is at stake.

Maybe more important than focussing on the extent to which product placement should be allowed, is whether consumers recognise product placement. Empirical evidence is needed to determine to what extent consumers are uncertain and confused about the distinction between editorial content and



commercial communications. In 2006, 95% of the Dutch population was aware of the prominence of product placement in general (as opposed to 73% in 2000). However, less people were able to recognize product placement in specific programmes (72%). This implies that 28% of consumers did not recognise product placement in specific programmes. Still, only 12% thought that product placement was unacceptable. Another conclusion was that many people favour product placement over spot-advertising (commercial blocks) (Van Reijmersdal, 2007).

These figures that were presented indicate that it is important to inform viewers about the existence of product placement in a specific programme, with clear guidelines on how this must be done. This approach could be more effective than to apply general notions of 'undue prominence' or to minimise product placement.

One possible disadvantage of very strict rules on product placement, is that firms are given an incentive to 'hide' product placement. This may trigger illegal types of product placement. Advertisers and media service providers may opt for very subtle product placement, that is not mentioned to consumers (at the start of a programme) and that will not be noticed by the average viewer. It may take regulators some time to identify subtle and illegal types of product placement.

Consumer protection is not only a matter of curtailing product placement in media services. An important aspect is digital literacy and media literacy.

Furthermore, protecting consumers is not confined to the national legislation of one specific Member State. It is important to consider the decisions that are being made in other member states. Consumers do not only watch Dutch programmes on Dutch channels from Dutch media service providers who are located in the Netherlands. They watch foreign programmes (in which case the rules on product placement can be waived), they watch services that are provided by foreign media service providers (that operate under different rules). Foreign media service providers can even focus on Dutch market (e.g. RTL). Especially on the internet, the number of foreign media service providers is unlimited. Because these services and service providers are subject to another set of rules on product placement (the country of origin principle) they do not necessarily provide the same level of consumer protection. As a result, viewers are asked to develop a schizophrenic viewing pattern – to anticipate different levels of protection. This is not realistic. Furthermore, viewers are generally not aware of the country of origin of a programme. The reality of media consumption calls upon member states to steer to a European average for consumer protection, or at least some sort of coordination with countries with the same language (e.g. the Netherlands and Flanders; UK and Ireland) and countries in which international players are based (e.g. Luxembourg).

The internationalisation of media markets – and the differences between national regulations – does *not* create complications for digital literacy and media literacy programmes. The skills to be obtained are

relevant for all programmes that are consumed, including programmes that originate from countries with less strict rules on product placement.

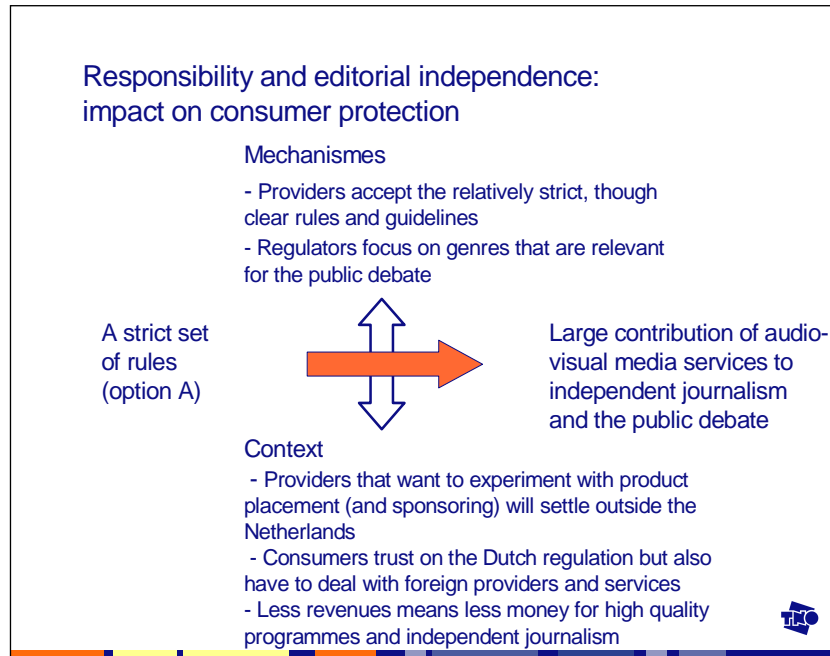
It will not be possible to keep out foreign media services on basis of ethical objections to excessive product placement. This option is not within the scope of the AVMS Directive exception-rule.

One of the instruments to ensure editorial independence for programme makers is a programme statute. Policy makers can oblige media service providers to introduce and publish programme statutes, in which the creative freedom and the abolishment of commercial interference is guaranteed. To protect programme makers (and indirectly consumers) policy makers and other stakeholders should be clear about the content of programme statutes, procedures, appeal mechanisms and sanctions.

A strict set of rules on product placement presents regulators with a challenging task. The number of media service providers and services is large, especially in the online environment. An effective monitoring and sanction framework is required.

#### **4.3. Consumer protection II**

The following slide was used to prepare and structure the interviews.



**Figure 9:** Responsibility and editorial independence: impact on consumer protection

#### Hypothetical impact

A strict set of rules on product placement will guarantee better protection for consumers as it will result in a more independent public debate, free from commercial interference. Because:

- Media service providers – management and programme makers – accept the set of rules, including guidelines for a programme statute and how to inform viewers that a programme contains product placement. The issues, experts and positions in programmes such as series and documentaries, are not influenced by commercial interests.
- Regulators focus on those services and programmes that are relevant for the public debate.

On the other hand,

- Media service providers that want to experiment with product placement (and sponsoring) will settle outside the Netherlands.

- Consumers will trust Dutch regulations, but not all content is originated from the Netherlands, not even all content that is primarily aimed at Dutch consumers.
- Less advertising revenues will lead to less high quality services, less independent journalism and less contribution of audio-visual media services to public debates.

## Conclusion

It is unlikely that the advertising rules in the AVMS Directive will have an impact on the contribution of audio-visual media services to independent journalism and the public debate. Programmes that have the most immediate influence on the public debate, such as news, are already protected by the AVMS Directive. Here, product placement and sponsoring are prohibited. Other genres and mixed genres (e.g. infotainment) can include journalism and can be relevant for the public debate. However, there are many uncertainties in the links between policy option A or B, product placement, and the contribution of audio-visual media services to independent journalism and the public debate. For instance, one could claim that programmes that are highly relevant for the public debate (e.g. documentaries) are likely to be of little interest for advertisers.

## About the mechanisms

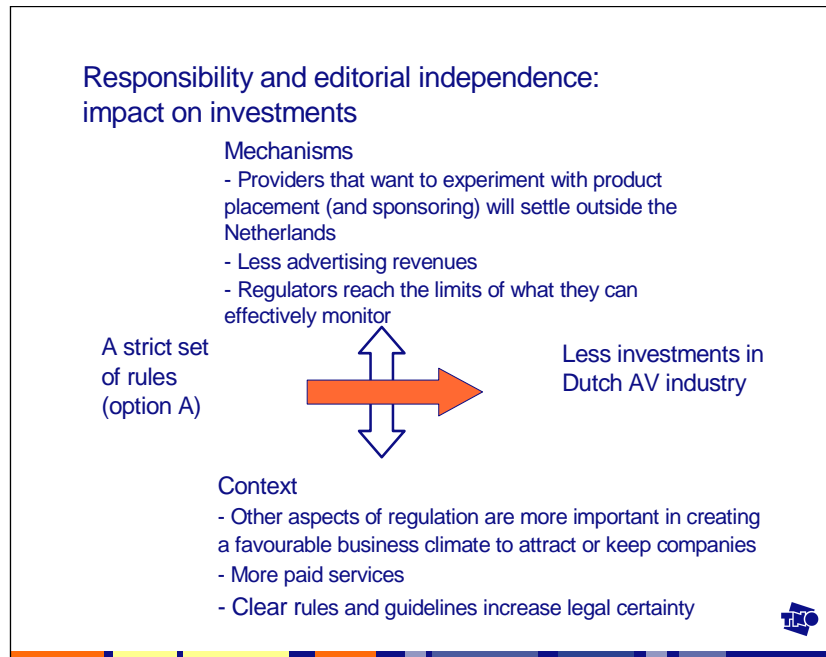
In general, the links were assessed as highly uncertain. The choice between a strict set of rules on product placement (option A) and a less strict approach (option B) is not very relevant for independent journalism and the public debate.

The AVMS Directive prohibits product placement (and sponsoring) in programmes that are considered to be highly relevant for the public debate (such as news). Furthermore, programmes such as documentaries, infotainment and series that touch upon societal issues, may not always be interesting for advertisers. Product placement will mainly be present in entertainment programmes that are less important for the public debate.

Furthermore, it is a question whether it is necessarily a bad thing if programmes that have some influence on the public debate contain product placement. For instance, product placement in popular soaps need not be a bad thing, as long as product placement is recognisable and as long as the programme makers are protected from advertisers.

#### 4.4. Investments

The following slide was used to prepare and structure the interviews.



**Figure 10:** Responsibility and editorial independence: impact on investments

#### Hypothetical impact

*A strict set of rules on product placement will reduce investments in the Dutch AV industry. Because:*

- Media service providers that want to experiment with product placement (and sponsoring) will settle outside the Netherlands, in countries with less strict rules.
- Less advertising revenues (or less growth in advertising revenues) because of the restrictions on product placement, an important type of advertising.
- Regulators reach their limits, which creates uncertainty in the market, one of the main factors to decrease investments.

On the other hand:

- Other aspects of national policy and regulation are more important in creating a favourable business climate.
- There will be many new and innovative paid services for which product placement is less relevant.
- Clear yet strict rules and guidelines will increase legal certainty.

### Conclusion

It is difficult to assess the impact of product placement regulation on business location and investment decisions, because there are many other factors involved (other regulations, infrastructures, taxes, education, demand, quality of life, innovation networks, etc.). However, although the impact might be small, strict rules on product placement might just be the straw that will break the camel's back. Media regulation is a relevant factor for the business climate in which media service providers operate. For firms that expect large revenues from product placement, strict rules on product placement can influence decisions on business locations (headquarters and operations) and investments. This applies to firms that are planning locations in Europe and for firms that are now based in the Netherlands.

### About the mechanisms

When discussing the impact of product placement rules on investments, it is important to consider that other factors, like other regulations and infrastructure, taxes, education, demand, quality of life (for the staff) and innovation networks are important as well. Furthermore, it is difficult to tell how important each factor will be, when a specific type of service provider is looking for a location to (re)settle.

Still, service providers have to deal with regulation upon regulation and although the impact of the product placement regulation in itself might be less substantial than others, it might be the straw that will break the camel's back. Media regulation can trigger media service providers to look for a location in a Member State with less strict rules.

This is not just (although mostly) a matter of money. Sentiment also comes into play. Media service providers may have to turn down product placement ideas of their advertisers, which is a nuisance for

commercial companies that rely on advertising revenues. To add some nuance: there are no (large) cases known with broadcasting regulation pushing a firm outside the Netherlands. The rise of Dutch commercial TV located in Luxemburg (RTL) was due to the *prohibition* of commercial TV. It had nothing to do with the *details* in Dutch media regulation. Furthermore, RTL has located many activities in the Netherlands, which creates employment. A new international player, Joost, decided to locate in the Netherlands. Despite the nuance, a Member State must prevent losing its competitive edge over other member states.

It was mentioned that the rules on product placement need not decrease or increase the total volume of advertising revenues that are linked to Dutch viewers and/or firms that operate from the Netherlands. More commercial freedom regarding product placement does not mean that the total expenditure on advertising will rise more quickly. It is expected that the total pie of advertising revenues will grow moderately, due to economic growth and other factors. Different types of advertising will compete for the pieces.<sup>7</sup>

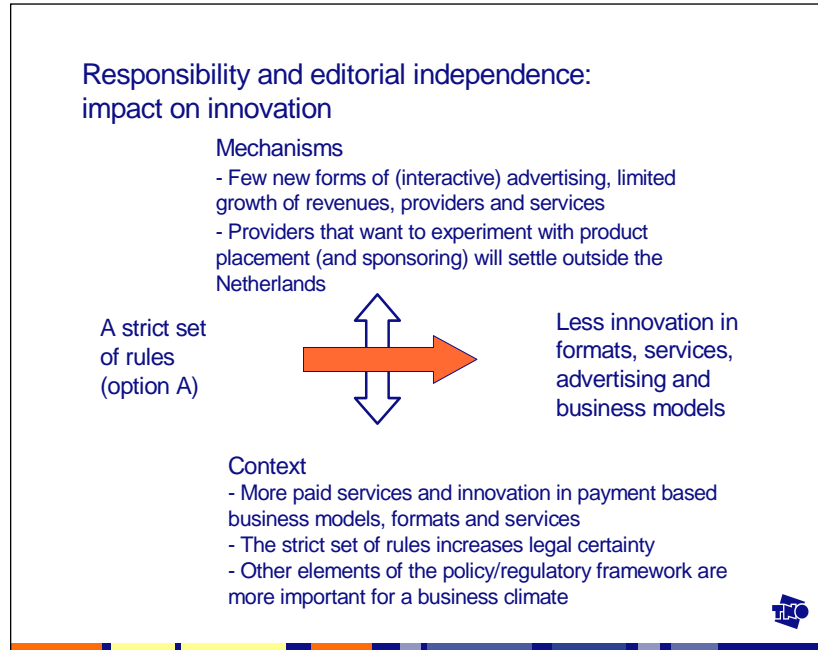
Furthermore, product placement also has its downsides as commercials and even products and brands are sometimes relevant for a few months or years only. This isn't a problem for programmes that focus on current affairs (which have a short life-span) but it can be a problem for films or television series for which many re-runs are foreseen. For these programmes, product placement is less relevant. This reduces the impact of product placement on business location decisions, revenues and investments.

#### 4.5. Innovation

The following slide was used to prepare and structure the interviews.

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<sup>7</sup> According to a 2006 TNO report by Leurdijk et al. (Reclame 2.0), advertising expenditure will grow from 858 million Euro to 996 million Euro in 2008 and up to 1.5 billion Euro by 2012. Television broadcasting will remain highly important, with advertising expenditures of 1.2 billion Euro in 2012, 80% of total advertising expenditures. Advertising revenues on the internet will reach 220 million Euro by 2012. In 2005, the ratio spot/non-spot advertising was 89:11, but it is expected that in 2012 it will be 50:50.



**Figure 11:** Responsibility and editorial independence: impact on innovation

#### Hypothetical impact

*A strict set of rules on product placement will reduce innovation in formats, services, advertising and business models. Because:*

- There will be few new types of (interactive) advertising, which will only lead to a small increase of revenues and the number of service providers and services.
- Service providers that want to experiment with product placement (and sponsoring) will settle in other member states.

On the other hand,

- There will be more paid services and more innovation in payment based business models, formats and services (e.g. micropayments and subscription models).



- The set of strict yet clear rules (e.g. detailed guidelines) will create legal certainty, which is a key factor for investments and innovation.
- Other elements of the policy/regulatory framework are more important for a business climate.

## Conclusion

Advertising spots (commercial breaks) are still the most important revenue source for media service providers. The importance of product placement is growing. Advertisers are always looking for the most effective way to reach consumers. A strict set of rules on product placement (option A) will limit commercial flexibility and innovation with respect to product placement. This is a small and negative effect. Strict rules for product placement will provide advertisers (and media service providers) with incentives to explore other types of advertising in audio-visual services and in other media (e.g. print and outdoor). The impact on innovation will be more substantial for firms that focus on product placement and on services (e.g. genres) and business models that rely on product placement. To some extent, the impact on innovation is indirect. As was mentioned above, a strict set of rules has a small and negative impact on the business location of media firms and on investments; i.e. less firms and less investments. This does not stimulate innovation. Option B – with less strict rules and with a focus on final responsibility – is expected to have a small and positive impact on investments and innovation. A small disadvantage of option B is that it can be more difficult to implement option B into clear rules that increase legal certainty. Furthermore, it must be stressed that the impact of option A or option B will be small, that the impact will be different for different types of firms, and that the impact will depend on the rules that are implemented in other countries.

## About the mechanisms

At least for now, product placement in the Netherlands is not the most important revenue source for the AV industry, with spot advertising still being far more important. However, there is no clear line between firms that rely on product placement and firms that rely on spot advertising. Many advertisers, media service providers and services explore a combination of product placement and spot advertising. This means that a strict set of rules – that will limit commercial flexibility – is relevant for a range of firms.

The importance of non-spot advertising is growing, especially in the on-demand environment. Advertisers always look for the most effective way to reach consumers. Strict rules for product placement will provide advertisers (and media service providers) with incentives to explore other types of advertising in audio-visual services (e.g. sponsoring). Firms will also explore options in other media (e.g. print magazines, free newspapers, outdoor advertising). The impact on innovation will be more substantial for firms that focus on product placement and on services (e.g. genres) and business models that rely on product placement. This can decrease the revenues of audio-visual media service providers, with a possible effect on the sources for innovation and the incentives to innovate in audio-visual services. The impact of strict rules on product placement on innovation is assessed as negative yet small.

To some extent, the impact of product placement rules on innovation will be indirect. As was mentioned above, a strict set of rules has a small and negative impact on the number of media firms in the Netherlands and on investments. This is highly relevant for firms that want to invest and innovate in product placement (and in sponsoring, where similar rules will apply).

The small and negative impact of option A (as opposed to option B) must not be overestimated. Four issues were mentioned.

No matter if rules are strict or light, the rules should be as clear as possible. Media service providers require clear, predictable and stable regulations. This is highly relevant for innovation. Which rules will apply to which new services? What will (not) be allowed? The expert assessment is that option A (more strict and detailed rules) appears to be a bit more clear than option B. Option B has a focus on the *final* responsibility of media service providers, a narrow interpretation of undue prominence and a light approach on how consumers are informed that a programme contains product placement. What is *final* responsibility? How will regulators decide on cases where viewers are informed 'quickly' that a programme contains product placement?

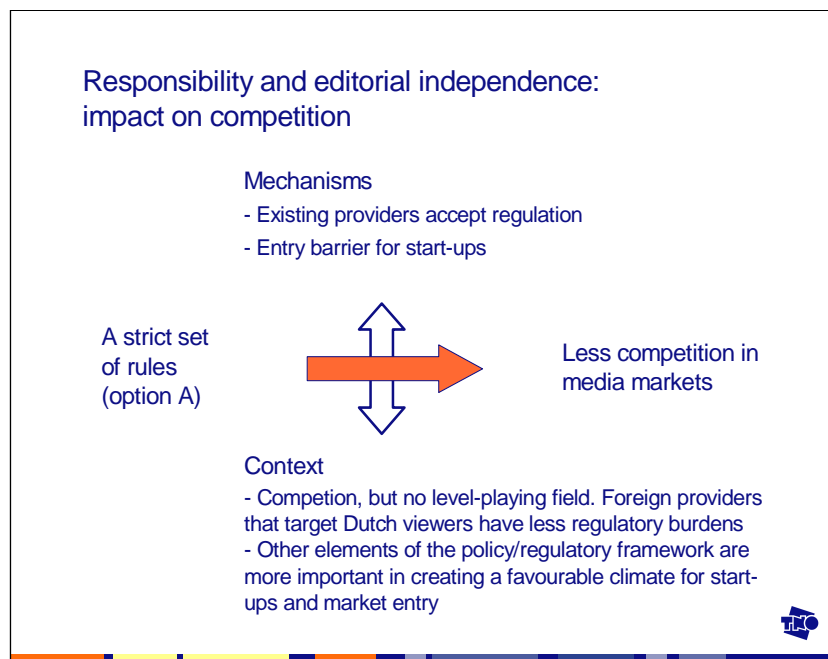
It must also be mentioned that components of option A – such as a very clear message before a programme to announce product placement – will not reduce the incentives to innovate. Other components of option A can have a negative impact on innovation. For example, the rules that will be used to monitor content and to identify product placement, can signal that several types of product placement will not be allowed.

A third remark that nuances the disadvantages of option A (a strict set of rules) is that there are many ways to innovate in advertising and services. Product placement is only one option. One could claim that product placement fits the traditional broadcasting system, with programmes for large audiences. Many innovations concern interactive and personalised services, where banners, sponsoring and micro-payments may be more efficient than product placement.

A fourth remark is that the impact of option A (or option B) will depend on the implementation of the AVMS Directive in other countries.

#### 4.6. Competition

The following slide was used to prepare and structure the interviews.



**Figure 12:** Responsibility and editorial independence: impact on competition

Hypothetical impact

*A strict set of rules on product placement will lead to less competition in media markets. Because:*

- Existing media service providers accept the new rules.
- A strict set of rules can be an entry barrier for start-ups and other small firms.

On the other hand:

- There will be competition but no level-playing field. Foreign media service providers can target Dutch consumers and have to comply with less strict rules on product placement.
- Other elements of the policy/regulatory framework are more important for a favourable business climate for start-ups and other firms that enter (Dutch) media markets.

### Conclusion

A strict set of rules on product placement (option A) could have a very small and negative impact on competition. A strict set of rules, with restrictions for product placement, can decrease the commercial options to enter the market and to earn revenues. A strict set of rules can also pose an administrative burden and an entry barrier for small firms and start-ups that are based in the Netherlands. Small firms may avoid the regulatory complexity and put more emphasis on other types of advertising (such as sponsoring) and possibly on other media markets (such as text-based services and services that rely on user created content) and other fields of business. This can reduce market entry and reduce competition in markets for audio-visual media services. However, if the set of rules is strict yet clear, small firms can easily assess whether specific types of product placement will be allowed. Competition in media markets also comes from international players, large and small, that are located in other countries. Strict rules in the Netherlands do not hinder foreign firms for the eyeballs and advertising revenues in Dutch media markets. If other countries adopt less strict rules, Dutch players have to compete in a non level playing field.

### About the mechanisms

A strict set of rules, with several restrictions for product placement, can decrease the commercial options to enter the market and to earn revenues. Small and large firms that consider entering media markets (or to leave media markets) will assess the different sources of revenues. Together, the different sources of revenues should allow for a profitable service and firm. Product placement can be an important source of revenues. A strict set of rules may have a small and negative effect on the revenues from product placement.

A strict set of rules can be an administrative burden and an entry barrier for small firms and start-ups that are based in the Netherlands. In general, the less rules the better. Small firms may avoid the regulatory complexity. They can redirect their strategy towards other types of advertising (such as sponsoring) and possibly to other media markets (such as text-based services and services that rely on user created content) and other fields of business (non-media). This can reduce market entry and reduce competition in markets for audio-visual media services. In general, administrative burdens are more burdensome for small companies or start-ups than for large companies. Large companies can spread administrative and legal costs across a large volume of revenues and a set of services. Often, a legal department exists.

As was mentioned in the context of investments (see above), rules must be clear. It is expected that a strict set of rules (option A) can be implemented a bit more clearly than the less strict approach in option B. A clear implementation of option A should allow small firms to easily assess whether specific types of product placement will be allowed. Clear yet strict rules need not decrease market entry.

Firms that compete in Dutch media markets – the markets for Dutch consumers and advertisers – can be based in the Netherlands or in other countries. Especially for services that are provided via the internet, a business location need not be close to consumers and advertisers. Regional offices may be sufficient to understand and to strike deal. A strict set of rules on product placement in the Netherlands does not hinder foreign firms. The rules will probably have more impact on the level playing field than on market entry and effective competition in Dutch media markets. If other countries adopt less strict rules (or more strict rules), Dutch players have to compete in a non level playing field. To some extent, this is a fact of life when European harmonisation leaves room for national differences, to fit with national policy objectives and the national market context.

#### **4.7. Conclusion**

A set of strict and clear rules on product placement (option A) will increase the level of consumer protection, compared to a focus on final responsibility (option B). Several mechanisms were identified. For example, a strict set of rules will decrease commercial influence and increase editorial independence. As was mentioned above, several elements of option A are perceived relevant. This includes clear rules on how to inform consumers that a programme contains product placement, and to make programme statutes obligatory. An effective policy mix to protect consumers also includes initiatives to stimulate media literacy. This is relevant for policy option A as well as policy option B.

It has been very difficult to link policy option A (and policy option B) to the contribution of audio-visual media services to independent journalism and the public debate. Programmes that have the most immediate influence on the public debate, such as news, are already protected by the AVMS Directive. Here, product placement and sponsoring are prohibited. Other genres and mixed genres (e.g. infotainment) can include journalism and can be relevant for the public debate. For these genres, it is not clear how policy option A or B will have an impact.

The impact of product placement regulation on business location and investment decisions is probably small and negative. For firms that expect large revenues from product placement, strict rules on product placement can influence decisions on business locations (headquarters and operations) and investments. Many other factors are involved (other regulations, infrastructures, taxes, education, demand, quality of life, innovation networks, etc.).

A strict set of rules on product placement (policy option A) will limit commercial flexibility and innovation with respect to product placement. This is a small and negative effect. Strict rules for product placement will provide advertisers (and media service providers) with incentives to explore other types of advertising in audio-visual services and in other media (e.g. print and outdoor). The impact on innovation will be more substantial for firms that focus on product placement and on services (e.g. genres) and business models that rely on product placement. To some extent, the impact on innovation is indirect. As was mentioned above, a strict set of rules has a small and negative impact on the business location of media firms and on investments. Option B – with less strict rules and with a focus on final responsibility – is expected to have a small and positive impact on investments and innovation. A small disadvantage of option B is that it can be more difficult to implement option B into clear rules that increase legal certainty. Furthermore, it must be stressed that the impact of option A or option B will be small, that the impact will be different for different types of firms, and that the impact will depend on the rules that are implemented in other countries.

A strict set of rules on product placement (option A) could have a very small and negative impact on competition. A strict set of rules, with restrictions for product placement, can decrease the commercial options to enter the market and to earn revenues. A strict set of rules can also pose an administrative burden and an entry barrier for small firms and start-ups that are based in the Netherlands. This can reduce market entry and reduce competition in markets for audio-visual media services. However, if the set of rules is strict yet clear, small firms can easily assess whether specific types of product placement will be allowed. Competition in media markets also comes from international players, large and small, that are located in other countries. Strict rules in the Netherlands do not hinder foreign firms for the eyeballs and

advertising revenues in Dutch media markets. If other countries adopt less strict rules, Dutch players have to compete in a non level playing field.

The impact assessment indicates that policy makers are confronted with a trade-off. A set of strict and clear rules on product placement (option A) will increase the level of consumer protection, but this may come at the expense of investments and possibly innovation and competition. Policy option B is more 'business friendly' and provides less consumer protection. The impact will be different for different players, and will depend on the implementation of the AVMS directive in other countries. This must be analysed. To some extent, the solution to the policy problem could be in the detailed design and implementation of policy option A or policy option B. It was also mentioned that additional policy instruments are relevant. Examples are programmes to stimulate media literacy, and education and consumer empowerment in general.

Also note that the analysis is relevant for sponsoring as well. Sponsoring – similar to product placement – may not influence services in such a way to affect the responsibility and editorial independence of the media service provider. It is likely that a strict set of rules on sponsoring will increase the level of consumer protection, at the expense of investments and possibly innovation and competition. Again, this will be different for different players, and it will depend on the implementation of the AVMS directive in other countries.

## **5. Conclusion**

Europe's member states are in the process of implementing the 2007 Audio-visual media services Directive. This report has addressed two implementation issues. For each implementation issue, two policy options have been formulated. An impact assessment method was used to assess the impact of each policy option on consumer protection, investments, innovation and competition. The method combines desk research and expert consultation. It is an explorative method with a focus on understanding the mechanisms via which policy interventions can have impact.

The first implementation issue concerns the definition and explanation of non-linear services. How to draw the line between linear services and non-linear is relevant because linear services will be regulated more strictly. Linear services have to comply with quantitative rules regarding the length and frequency of commercial breaks, and quota for European and independent productions. A broad definition of non-linear (option A) signals that a very small level of control for users is sufficient for a service to qualify as non-linear. This implies that almost anything but traditional broadcasting television will be regarded as non-

linear rather than linear. This means that relatively few services will have to comply with the quantitative rules that apply to linear services (limits to advertising and quota for European and independent content). Option B, a narrow definition of non-linear services, will mean that more services will qualify as linear (compared to option A). For example, a number of new (internet) services with limited user control will qualify as linear.

The analysis demonstrates that - compared to policy option B – option A does not lead to less consumer protection and that it has a small and positive impact on investments and innovation. It must be stressed that the impact is small and that it depends on the decisions that are made in other European countries. The impact of policy option A or B on competition was uncertain. To summarise: option A – a relatively light and business friendly option – does not provide policy makers with a difficult trade-off between the interests of consumers and the media sector, or a trade-off between the interests of different segments of the media sectors.

A trade-off did emerge for the second implementation issue. The directive allows member states to define a set of rules regarding product placement, to prevent influence on responsibility and editorial independence (to protect consumers and programme makers). Option A consists of a set of strict, detailed and clear rules. This option includes a detailed yet clear national implementation on how users/viewers are informed about product placement. This is combined with the obligation for media service providers to publish a programme statute, to protect consumers and to protect programme makers vis-à-vis management and advertisers. Option B has a focus on final responsibility by media service providers when it comes to the selection, organisation and actual content of media services. In some cases, there can be influence by advertisers, as long as the final decisions and responsibility remains with the media service provider and the programme makers. In option B, media service providers can decide how to inform users/viewers about product placement. Furthermore, a programme statute is not compulsory.

It was concluded that a set of strict and clear rules on product placement (option A) will increase the level of consumer protection, but it may come at the expense of investments and possibly innovation and competition. Policy option B is more 'business friendly' and provides less consumer protection. The impact will be different for different players, and will depend on the implementation of the AVMS directive in other countries. This must be analysed in more detail, e.g. with a quantitative analysis on the impact on specific players (e.g. Dutch or foreign players for which product placement is the main source of revenues). To some extent, the solution to the policy problem could be in the detailed design and implementation of policy option A or policy option B. For example, option A includes elements such as clear rules on how users/viewers have to be informed about product placement. This element of policy option A may not have a negative impact on investments and innovation.



It was also mentioned that other policy instruments are relevant. The full policy mix matters. Relevant for consumer protection are programmes to stimulate media literacy, education and consumer empowerment in general. For this type of policy interventions, there will be few trade-offs between different policy objectives or between different stakeholders. With respect to investments and innovation, it can be mentioned that several policy instruments can be used to attract foreign media players (e.g. fiscal instruments, business locations, infrastructures and innovation programmes). Still, media regulation can be one of the factors.

The analysis of the product placement issue is relevant for sponsoring as well. Sponsoring – similar to product placement – may not influence services in such a way to affect the responsibility and editorial independence of the media service provider. It is likely that a strict set of rules on sponsoring will increase the level of consumer protection, at the expense of investments and possibly innovation and competition. Again, this will be different for different players, and it will depend on the implementation of the AVMS directive in other countries.

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## Annex A: experts

### External experts

- *Drs. Wendy van den Broeck* is researcher at the research centre IBBT-SMIT (Studies on Media, information and telecommunication; Free University of Brussels).

- *Prof. dr. Fred Bronner* is a part-time Professor of Communication Science at the University of Amsterdam. Furthermore, Fred Bronner works at the SWOCC, the institute for scientific research in commercial communication.

- *Prof. dr. Nico van Eijk* (IViR) is Professor by special appointment of Media and Telecommunications Law at The Institute of Law; University of Amsterdam.

- *Dr. Wolter Lemstra* is Senior Research Fellow Economics of Infrastructures at the Faculty Technology, Policy and Management of the TU Delft, and Senior Lecturer at the Strategy Academy, the Netherlands.

- *Prof. dr. Peter Neijens* is Full Professor and Chair of Persuasive Communication in The Amsterdam School of Communications Research *ASCoR* at the Communication Science Department of the University of Amsterdam.

- *Dr. Eva van Reijmersdal* is a researcher at The Amsterdam School of Communications Research *ASCoR* at the Communication Science Department of the University of Amsterdam.

- *Mr. Machteld Robichon-Lindenkamp* is an attorney at Kennedy Van der Laan, an independent law firm. She is specialized in telecommunications and media law.

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- *Drs. Kees Bijl*

- *Mr. Helga Zeinstra*

- *Mr. Herman Hofenk*

- *Mr. Rob van Iersel*

- *Mr. Katja Mutsaers*

- *Mr. Thijs Tuik*

### **TNO**

- *Dr. Andra Leurdijk*

- *Drs. Matthijs Leendertse*