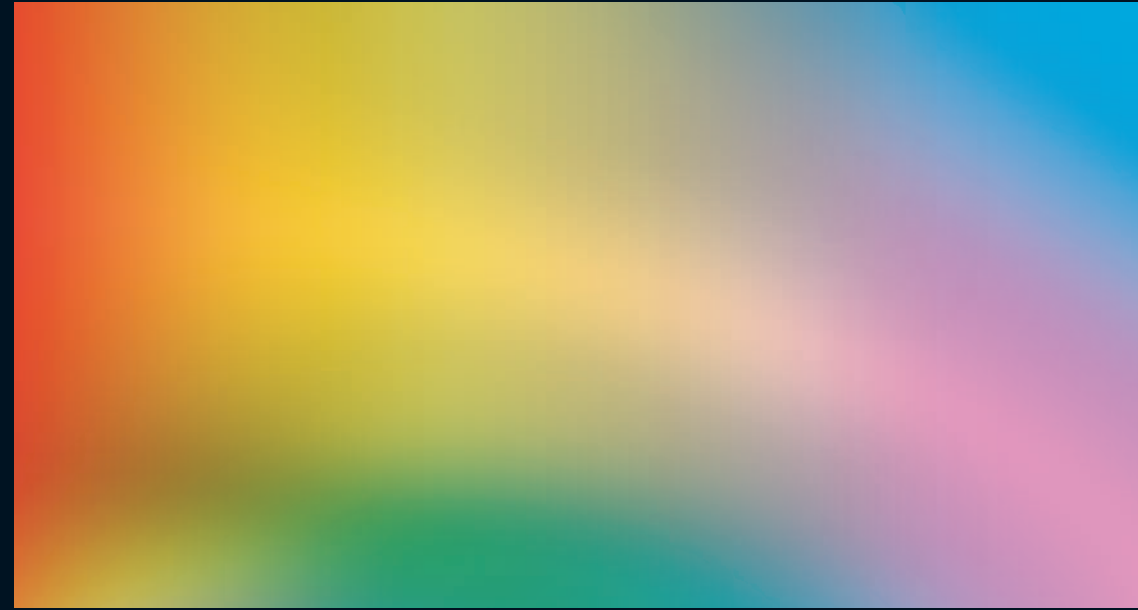


A seminar organised by the British Screen Advisory Council

**BSAC FILM CONFERENCE**  
**THE FILM INDUSTRY IN THE DIGITAL AGE**



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# FOREWORD

The British Screen Advisory Council is an independent advisory body to the government and policy makers at national and European level and to the audiovisual industry. It uniquely brings together the widest possible range of UK interests, experiences and contacts in the screen industries. Members include senior management from terrestrial, satellite and cable television, telecommunications and new media companies; technical experts, business people with media interests, media lawyers, communications consultants, TV producers and trade unionists; and the heads of training and trade organisations.

BSAC regularly commissions and oversees research on the audiovisual industry and uses its research to underpin its policy documents. In addition to regular monthly meetings, BSAC organises workshops, seminars, conferences, industry briefings and an Annual Reception in Cannes.

BSAC relies on industry funding for its activities and we are therefore particularly grateful to Time Warner for sponsoring this event. BSAC also wishes to express its gratitude to all the speakers and panellists at the conference for their interesting contributions. The Chair of the Seminar was John Howkins, Deputy Chairman, BSAC and Director of Equator Group plc, to whom the Council is most grateful.

Please note that the speakers' presentations and panel sessions in this report are edited transcripts. Presentation slides are available on request, or on BSAC's website ([www.bsac.uk.com](http://www.bsac.uk.com)).

Time Warner Inc. is a leading media and entertainment company, whose businesses include filmed entertainment, television channels, interactive services, publishing and cable systems. In Europe, Time Warner's businesses include Warner Bros. Entertainment, New Line Cinema, Home Box Office, Turner Broadcasting System, Time Inc. and AOL.

## **Warner Bros. Entertainment**

Warner Bros. Entertainment is a global leader in the creation, distribution, licensing and marketing of theatrical motion pictures, TV programming, animation, video/DVD and related products. In Europe, Warner Bros. is also committed to producing and distributing local productions. Films currently being produced in the UK include Batman Begins, Charlie and the Chocolate Factory and Harry Potter and the Goblet of Fire.

## **New Line Cinema**

New Line Cinema is the oldest and most successful independent film company in the world. In addition to the production and distribution of theatrical motion pictures, it has divisions devoted to home entertainment, television, music, theatre, licensing, merchandising and international marketing and distribution. New Line has been a pioneer in franchise filmmaking and its award-winning Lord of the Rings trilogy is the most successful film franchise in history.

## **Turner Broadcasting System**

Turner Broadcasting System is a major leader in news and entertainment around the world. In Europe Turner delivers cable and satellite television channels and Web sites, including CNN International, Cartoon Network, Turner Classic Movies, Boomerang and Toonami.

## **Home Box Office**

HBO is America's most successful premium television network, whether measured by subscribers, profitability, viewers, awards or critical acclaim. HBO sells its original programming such as The Sopranos and Sex and the City to broadcasters throughout Europe. HBO's film division is involved in local productions such as The Life and Death of Peter Sellers and the distribution of such acclaimed HBO Films as Gus Van Sant's Palme d'Or winning Elephant and Sundance winners Maria Full of Grace and American Splendour. HBO Central European ventures offers basic and pay television channels throughout Central Europe.

## **Time Inc.**

Time Inc. is the world's leading magazine publisher. Its more than 130 magazines reach total audiences of more than 300 million worldwide. In Europe, Time Inc. offers readers the best in serious journalism, including Time and Fortune, as well as popular consumer magazines. Time's IPC Media is the UK's largest consumer magazine publisher, with over 100 titles including Country Life, Loaded and Marie Claire. Time Inc. is also home to the Time Warner Book Group. In Europe, Time Warner Book Group UK is a leader in the industry and was named Publisher of the Year at 2004 British Book Awards.

## **America Online**

AOL is the world's leading provider of interactive services, offering a full range of online products and services to consumers around the world. AOL Europe's localised AOL subscription services in the UK, France and Germany have established themselves as leaders in their regions.

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## John Howkins, Deputy Chairman, BSAC and Director of Equator Group plc



John Howkins

The Chair welcomed guests, and explained that the discussions during the day would focus on the new business models for the film industry in the digital age. He said that the conference was taking place one year on from BSAC's successful first film conference, and that BSAC was very grateful to Time Warner for sponsoring the event for the second year running.

The Chair then introduced the Minister of State for the Arts, Estelle Morris, and reminded delegates that in her opening address a year previously, she had encouraged the film sector to be brave in the face of change, and to develop an effective way of distributing films online legally.

## Estelle Morris MP, Minister of State for the Arts

Since last year's BSAC film conference, I believe we have made some good progress. The reality of the issues facing the film industry has become more stark, however I think progress has been made in facing up to both the opportunities and challenges these issues present.



Estelle Morris

As you know, usually civil servants prepare politicians' speeches, and often useful quotes are provided. I don't usually like to use these quotes, as I'm not keen on plagiarising - however, on this occasion I found that the quote provided was very apt. George Lucas was recently quoted in the New York Times as saying, "I love film, but it's a 19th Century invention. The century of film has passed." Then he went on to say, "We are in the digital age now." It made me realise that essentially we drift from one century to another, and because change tends to be gradual for us, we sometimes don't realise the enormity of what has happened. I think one of the lessons I have learnt in politics - not just in this job as Minister of State for the Arts, but throughout all my time in politics as a Minister - is that the people who really get it right are those who can foresee the enormity of the change, can prepare for it and shape the change, rather than letting change shape them. The reason I plagiarised that quote, was because it is such a stark insight, "The century of film has passed". However, many people would say that the century of film has not passed. It depends on whether you think of film as the media or as the art form. Film as the art form certainly has not passed. But film as the media platform could pass before we actually realise it. The change that is upon us is not gradual, and it is not optional. The threat of not getting it right is dire.

We can draw parallels between the effect that digital technology will have on the film industry with other sweeping changes experienced by different industries - for example, the effect of the invention of antibiotics and the discovery of DNA on the medical profession. I have always reckoned that every industry has its invention of antibiotics, or its discovery of DNA. I think that the digital world is the DNA or the antibiotics of the film industry. Things will never be the same again, there's no ignoring it, and if you pretend it isn't there, people will go for the better option down the road. In film, the better option down the road has been the illegal, counterfeit, pirated option and also the use of online. However, looking ahead, we must be positive - at some point the language does have to change, and we must hold more conferences that explore the opportunities of the digital technology rather than concentrate on the threats.

I think that in these periods of great change it is really important to keep in touch with your roots. In that sense, I would say that the century of film is not dead, because even in the digital age or whatever comes after the digital age, the role of film in terms of educating, informing, inspiring, and entertaining will still be the same. As will be the power of film to describe complex issues in interesting and engaging ways, and to express cultural ideas. This power of film is absolutely unequalled and unparalleled in any other of media. The capacity of film to do all those things isn't lessened by digitalisation, it will actually become more powerful.

Digital technology gives us a way of fulfilling those core objectives of film in a far better way for far more people.

The digitisation of film provides many opportunities and also challenges. Firstly, the public is now becoming accustomed to the better quality of digital media, and is expecting better quality, sharper images and greater creativity. Secondly, more and more people have access to affordable digital filmmaking equipment and are now making movies of their own. Last month, First Light (which is the UK Film Council's programme for young filmmakers between 5-18 years old), had its award ceremony in Leicester Square. Some of the short films had been made by 8 year olds to a standard equal to what a 20 year old might have made only 5-10 years ago. If more and more young people are making films, this changes the relationship between the watching public and the film industry. It breaks down that secret garden - and changes the way these people will be viewing films. Thirdly, reduced distribution costs provide more opportunities. I believe that the print for a digital film is about £85, whereas the cost of a print for 35 mm can be up to £2,000. If we can distribute more films at less cost this will give a new life to those films that might never hit the mass popularity market - this means that they are more likely to be actually seen. Therefore, opportunities for minority taste films might actually increase.

We must begin preparing for the digitisation of film now. One of the most important ways in which preparation for the future is taking place is through the Digital Screen Network, which the UK Film Council is running. 200 Screens in 150 cinemas will be equipped with state of the art digital projection equipment, starting this May and finishing next year. This means that a quarter of cinema screens in the UK will have the most up to date digital equipment. This is good progress - but I have no doubt that we have got to go even further than that. We can't wait for a decade until the rest of the work is complete - we have to work in a much faster time space to get that technology in there. We must also prepare for the future in terms of skills. One of the great strengths of the British film industry at the moment is our skill base - we are providing good training opportunities, and money has been invested in learning about how to use the best of new technology.

I have been round to see some of our skill bases using new technology, and I know that they are held in very high regard by filmmakers from all over the world. I know that they are one of the reasons why we have attracted such large inward film investment levels over the past 4-5 years. If we want to keep that cutting edge, we must continue to invest in those skills in the digital age. The Skillset training programme is therefore extremely important. Skillset is again working with the UK Film Council to make sure that as a nation, we keep ourselves at the highest level of skill, and make sure that we can compete with other countries.

Alongside these opportunities, there are also threats. Technology has a dark side as well - the problem of piracy. For this, we are not fully prepared - over the last few years we have failed to actually conquer piracy, counterfeiting and illegal downloading. However, film has responded to these problems far more quickly than the music industry did, and therefore I hope that the chances of our getting it right are better. I think we learnt some lessons from music, and we are grateful in a strange kind of way to the music industry for going through the pain first. The UK has more incidences of counterfeiting and piracy than any other European country. We estimate that in 2003, 20 million counterfeit DVDs were sold in the UK. It was probably worse in 2004, and is likely to be even worse in 2005. Last week I was in Thailand looking at the counterfeiting and piracy problem - 40% of counterfeited and piracy goods in the UK come through Thailand. When I saw the extent and openness of the sale of phoney DVDs and videos on open markets, I realised the enormity of the problem. But even then in Thailand there was cause for optimism because the new Government has recently established an intellectual property court, which I think shows a willingness and understanding to face up to the problem. I think we are a little late in the UK - however, the IP Forum has been looking in to these issues for the past year.

I welcome this conference because creativity and IP underpins not only your industry, but many others also. The last three conferences I have attended have all been about the digital age or piracy - that has to be a good thing. This shows that there is a united agenda about seizing the opportunities, dealing with the threats, and a real understanding of what needs to be faced up to. We very much welcome your input, and any feedback you may have from this meeting today.

I don't mean to be pessimistic, but sometimes in my own mind I always like to ask myself, "What happens if we get this wrong?" It makes one realise the enormity of the task and the importance of getting it right. If we don't get this right, there is absolutely no doubt what we put at risk. We risk breaking that chain of creativity - i.e. people investing their creative ideas into an industry that can turn the ideas into a film to show to people, who will pay for the privilege of watching the film. That money can then go towards more creative ideas to make more films.

That cycle - from the first spark of the creative idea, to thousands of people paying to watch the film, to reinvest in the next generation of creative ideas - cannot be broken. The minute that cycle is broken, the investment is lost, and the journey or route map of that creativity is lost. We want to protect that chain. I don't think we will lose that chance, I think we will get it right, but there is no less sense of urgency this year than there was last year. However, I do honestly feel that progress has been made, and I think by the end of today there will be even more progress that has been made - even if it is no more than a sharing of good ideas and learning from each other.

I would like to finish by again thanking everyone for their work in this area, and to re-iterate that the work we are doing in Government is serious. It's not just words - and as far as I can, I will make sure that these words are followed up by actions. I know that I can depend on you to remind my successors of my words, and to hold us to the pledge that we have made in that respect.

The Chair thanked the Minister, and then opened up the session to questions from the floor.

**Lawrence Safir, Independent Film and Television Alliance:** I am wondering to what extent the IP Forum documents will be published and circulated so that the industry can respond to them?

**Estelle Morris MP, Minister of State for the Arts:** We will be publishing the Government response to the papers from the 3 working groups in March - but I am not sure whether we have promised to make that public or not. Yes, I believe we will be publishing them at some point, and I think we should publish both the working groups' reports and the Government's response - because I think not to do so would be less than open, and would not be inviting the sort of collaboration and discussion that I have discussed this morning. So, I will promise that we will publish each of the working groups' reports and the Government's response. However, I am not sure whether this could happen in March, or around the time of the next IP Forum in June. They are not State secrets, certainly in this age of freedom of information, therefore I can see absolutely no reason why they should not be published.

**Julian Friedmann, The Writers' Guild:** I was very pleased you mentioned that however rapidly film delivery systems are changing, the fact is that for the audience it does not make a difference to their enjoyment of film. The audience watches films whether they are pirated or not, for reasons that remain exactly the same as they have for the last century. It strikes me that there is not really enough discussion on the development and creative work that needs to be done on those original ideas which you referred to. The PACT/Writers Guild Agreement does not really work, we don't invest enough money in the development of writing, or the training of writers - we are waiting to see what Skillset does in this area.

There is perhaps too much emphasis in the industry on finding money through tax breaks, and on delivery systems etc. Yet we need to be prioritising the development of skills - in terms of writing, development and script editing - and I really don't see enough coming from the UK Film Council (of which I am a great fan), from the academic training institutes - which I think are failing lamentably, nor indeed in terms of Government policy on the creative process. I agree that we need to protect intellectual property, but I don't think we have got that much intellectual property to protect.

**Estelle Morris MP, Minister of State for the Arts:** I think that's a bit pessimistic, but apart from your last sentence I take your point. Technology is changing rapidly, and there are threats that go with this, therefore Government and industry's attention does seem to be focused on mainly technology related issues. There is also a sexiness about content delivery mechanisms in that they are important for our competitiveness, therefore Government speeches do tend to concentrate on the opportunities presented by broadband etc. So, I think that your words are a very timely warning - and I know that your organisation has made this point to us before. Sometimes it is necessary to focus on particular areas of concern, to see us through some particular challenges that lie ahead - but these periods of time are relatively short. You are right when you say that all this great technology comes to nothing unless it can be used on a good story - and a good story comes from a good script. I can't think of a film that has become incredibly popular that had a lousy story line, and a lousy script, but had some flashy technology. It doesn't work that way on the whole - I think good films have to have both a good script and great technology. I see there is a difference of opinion about that! We ought not to forget that writing is an enduring skill that will never change. I believe Skillset should be looking at script writing, development and editing. Interestingly, the meeting I am leaving for after this conference is another Forum I run on higher education institutions (which train people for the creative industries). No one has ever mention script writing in all the Forum deliberations. So, I will try to lodge script-related training somewhere in that process, and at least find out what the opportunities are, and try to put it in the agenda. If I remember rightly, the UK Film Council does provide some writing-related support, but perhaps not as much as you would wish. I agree with you that it would be silly to let writing skills fall by the wayside, otherwise we would have the best of technology and no films to use that technology on.

**Jonathan Davis, Strategy Advisor, UK Film Council:** You have spoken from a UK perspective, but we all know that these developments will have far reaching effects across the global film industry. How does the Government look to export all the great work that is going on in the UK, especially looking to the UK Presidency of the EU?

**Estelle Morris MP, Minister of State for the Arts:** Yes, intellectual property is very much a global issue. As many here will know, BSAC is organising a conference on behalf of DTI and DCMS as part of the UK's Presidency of the EU, which is taking place between October 5-7. The programme being developed looks very good, and the event will provide us with a great opportunity to discuss these issues at a European level. I notice also that at the Cannes Film Festival this year, the European Film Ministers will be discussing the issue of film online. I also gather that the European Media Programme will increasingly focus on online and digital content. So I think that these issues are being considered at a European level. The reason for my visit to Thailand last week was to make links with some of the other governments outside Europe. We will be working with them closely to tackle this problem of counterfeit content coming into the UK. In addition, we very much welcome the partnership we have had with the American film corporations on these issues. I learnt a lot from them when I visited them a year ago, and was able to see the initiatives they were taking to fight piracy and crime. There are open channels of communication, and the companies were generous in sharing their best practice - and I know that this relationship has continued.

# THE MUSIC INDUSTRY MODEL

## Brad Duea, President, Napster

Thank you very much for having me here this morning. I would like to begin by quoting a British band, "You say you want a revolution". We certainly have had a revolution in the music industry. It started about six years ago when the music industry was turned on its head. Some of the things that have happened since you are all familiar with - sales have fallen through the floor, tens of thousands of people have lost their jobs, labels have closed down, consolidation within the industry, artists being dropped and share prices suffering. You may even have heard some people asking, "Is this the death of the music industry?"



Brad Duea

What are some of the causes of this drastic change? For the past 50 years, music fans were forced into buying "album bundles" rather than just the songs they liked. Industry growth was being driven by consumers "repurchasing" their favourite records in each new format, rather than them buying music from the hot new acts in town. There was also some consumer frustration with retail - research shows that about 70% of the people were usually unable to find what they were looking for in record stores - and trying to discover new music by flipping through the bins (which in most cases you can't listen to) is a tough model for consumers. The other major development was radio - at one point it had broad play lists and the DJ was trusted as a guide to all the hot new music. However, consolidation within the radio industry has led to constricted hit-focused playlists, which aim to generate more traffic and therefore more advertising revenues. The ad minutes increased substantially, which again caused people to want music in a better form. Then along came the Internet, which offered instant gratification - faster than even fast food. One thing that is sometimes overlooked is that there was also competition from other media sectors - for example the cheap price of DVDs, games, mobile phone spend, etc. Crucially, the record industry had its defences down and seemed in denial - it didn't act quickly enough and embrace the opportunities. So, all that was really needed was one major catalyst, and then you'd have the ingredients for what I call a "perfect storm". And that perfect storm did take place. The Internet became the means of not only communicating, but also for providing the means of content acquisition. And that really began in about 1999 with Napster 1.0.

Napster was created by Shawn Fanning, who was a college drop out. He spent his time writing code - and the reason he wrote the code for Napster is that he found it difficult to find music online, and then share it. He didn't approach it with the intention of undermining the music industry at all, but his programme revolutionised the music industry. Soon, at any given time, 60 million people were online sharing files.

So, Napster became an incredibly efficient way to share music, and more so than I think Shawn ever imagined. This was not a revenue-generating model, so millions of tracks were being shared with no royalties for any rights holders, and as a result there was a debate within the music industry as to how it should deal with Napster. Should they embrace it? Should they leverage this amount of traffic and eyeballs? Or should they litigate? To make a long story short, litigation was the approach. The court actions led to unattainable requirements, and Napster was eventually bankrupted and shut down. The key issue for the Court seemed to be the "centralized" server model. At the time there were no good legal alternatives, there was only the dark choice, so people turned to "non-centralized" copycat models (e.g. KaZaA and eDonkey), which made the problem worse.

So, if Napster went bankrupt, how am I standing here, working for Napster? I worked for Roxio for over four years - Roxio was a digital media software company (e.g. software for CD burning, video editing, photo editing etc.). We were experiencing a flattening of our own sales, and wanted to embrace another growth vehicle. We thought that music was the growth vehicle and that the time was ripe for this model to catch on. So, Roxio acquired the assets of Napster out of the bankruptcy courts. We then acquired Pressplay, which was a joint venture between Universal and Sony. We felt that this technology was attractive, as it provided some features that would be appreciated by the labels (e.g. different catalogues of music could be made available in different territories) - also, the technology was able to support content other than just music. We combined the Pressplay technology with the Napster brand, and then launched a legal service, Napster 2.0, in the US in October 2003. In May 2004 we launched Napster 2.0 in the UK and in Canada. In January 2005, we announced that Roxio was selling its software assets (for \$80 million), we changed our corporate name to Napster, and we now trade on the Nasdaq stock exchange under the ticker Naps. We invested all the \$80 million on Napster and online music. Recently we announced our new model "Napster to go". This allows unlimited music downloads onto a PC and unlimited transfers to a portable device (some of which are manufactured by iRiver and Creative). Subscribers can fill and re-fill their players for a reasonable monthly fee - and all artists and rights holders get compensated.

When we acquired the Napster assets, we brought Shawn Fanning on board as a consultant. We asked him what the original users wanted out of Napster 1.0 - we also supplemented this with some additional research.

We found that people wanted the following features:- a massive catalogue of music; the freedom to explore and discover without the viruses, spy ware and spoof files of some of the illegal online services; a fast and easy to use service; the ability to stream, download, burn, transfer to a device; a community feel and the ability to share playlists with friends very easily; to be able to manage an entire collection in one place; choice in how to acquire music; fair pricing and compensation for artists; music that is localised in the various markets. So this is what we have tried to deliver with Napster 3.0. It's a legal subscription service and music store, which provides an immersive music experience built around discovery and sharing. It was designed and developed by music enthusiasts.

We have developed a two week trial for people who would like to experience the digital revolution. It works by new users going to the Napster website, downloading the software, registering. The integrated software provides:- the ability to search, play, download, buy or burn from a catalogue of over 1 million tracks; 40 years of the official UK charts; 25 interactive radio stations; a personalised 200 song radio station; new releases and exclusives; ready made compilations; the ability to rip your own CDs; the ability to send and receive songs and playlists, browse other members' collections, and share points of view on message boards; a newsletter; a step by step tutorial; a web shop. Because Napster is a legal service and compensates artists, it is now a friend of the artist, rather than a foe.

So why did we go after this opportunity now? What made us think that things were changing? We felt the time was finally ripe. By 2008, the US online market is projected to rise to \$1.4 billion. Within 3 years, digital music's share of the entire music market worldwide is expected to reach 25%, in other words, about \$9 billion. Some research studies have shown that subscription will overtake the a la carte download purchase model within four years. The main driver of this growth in online music is the rapid growth of broadband, and also MP3 players.

What are some of the differences between Napster and some of the other companies online? When we purchased the assets, the brand was one of the key assets we were interested in. We'd done research - 97% of online users recognised Napster, and associated it with online music. Interestingly enough, the No. 1 attribute was innovation, and the No. 2 attribute was that it was free. Our recent brand tracking study puts "free" at the bottom of the list, and "innovation" has stayed at the top. With regard to innovation, as you know many companies provide online stores. What we have tried to do is to achieve innovation by immigrating charts, community features, and now portable subscriptions - so we are constantly making the model better.

The big difference to our approach is providing consumers choice. Therefore, we do offer a store also, so that if users don't want to pay a monthly fee they can buy tracks for 79p instead. Or, users can subscribe and get a PC only subscription, or they can go for portable subscriptions which work for PCs and devices. Other companies have opted for the a la carte model only. We are trying to support as broad a range of players and devices as possible (currently over 75 different devices), and many of those are now supporting portable subscription. Some of our competitors have used the a la carte model to drive their hardware sales. Apple is a great example and they have done an excellent job and are having tremendous success - but iTunes is an a la carte model intended to drive up sales of their hardware the iPod, so it's a completely different approach.

We have put together a partner "eco system". So, instead of trying to own the pie ourselves, we have partnered with retailers and with media companies. We have even partnered with the labels to address the issue of piracy on campus. Last week we won the best digital music service in the UK from Music Week magazine. We have some of our colleagues here today - congratulations to Leanne Sharman, our General Manager for the UK.

I guess another big difference of Napster's model versus others is that we have created our whole service to be about the music. We want to create the best music experience for consumers. We are not trying to use music to sell hardware, and we're not trying to use music to sell advertising. You will see many ad-supported online models, and you will also see companies promoting soda pop brands and other products with music. But Napster is about the music experience.

So, are we making any money? Yes, we are beginning to generate some serious revenues. Napster has recently seen double digit revenue growth quarter over quarter, and we are currently projecting total revenues of \$15 million for 2005. By the end of December 2004, we had over 275,000 subscribers worldwide - this is a 50% quarter over quarter growth.

What about piracy? I guess in the music industry, piracy was eventually dealt with by creating a carrot and a stick. The "carrot", or the incentive, is the availability of excellent legal alternatives. Therefore, Napster has partnered with the labels - we have licensing deals with all the majors, and thousands of independents - and we have created a service with over 1 million tracks. But, this took a while to come about. However, in terms of the "stick", enforcement came into play in the shape of lawsuits and enforcement actions both by Government and by the RIAA. These enforcement actions were not necessarily intended to recoup all these damages, but the music industry has definitely made people aware that as well as the risks associated with viruses etc., there is also a risk of being sued.

The suits also helped educate the public that using certain P2P sites was illegal. Eventually the labels partnered closely with Napster to enable us to deliver a service - but for a while it was quite frustrating. We were trying to build this great legal alternative, and in many cases the labels were attempting to squeeze every last penny or pence out of legal services, while billions of tracks were going out the back door.

So, what are the lessons from the music industry that can be applied to film? I will compare some scenarios. The question I ask is, is there going to be another "perfect storm", but this time for film? 1) As I have already mentioned, in the music industry CDs were experiencing tremendous growth leading up to 1999. The growth was spurred not by new developing acts, but from people replacing their cassette collection with CDs. Are some of the DVD sales that are having tremendous traction in the movie industry hiding some of underlying problems? Perhaps over-costly movies? Are the margins not large enough? 2) Up until 1999, CD burning had been in existence for a while, people had been creating compilations - and CD burning made it very efficient to rip tracks and create a compilation. The popularity of DVD ripping is perhaps a similar scenario - while it technically violates copyright law, a lot of DVD ripping programmes are available. The DCSS programme is so popular it is now actually printed on T Shirt. 3) Is there any disappointment in the DVD retail experience? Perhaps. Is a wide range of filmed content available via the legal options at exactly the same time that they are available online illegally? In most cases, no. Movies are often available on illegal online sites long before they hit the theatres. Because of current window policies, often films are only available much later though legal services. 4) Do consumers really understand why they may not see a movie online right now instead of going to a theatre? Is there potential consumer hostility with regard to having to wait for movies to be released on different platforms? 5) We know that there is strong competition for "wallet share" from other forms of entertainment e.g. games, music, mobile phones, other consumer electronics etc. 6) MP3 players have now become media players that support video, photos, as well as music, and people need to feed these machines. The sad thing is that there's not a lot of legal content that you can put on these devices. In our service, we actually stream videos - but because of publishing restrictions and licensing rights issues we cannot allow consumers to download or burn videos at this time. 7) Are there bigger broadband pipes? Yes - and we are getting to the point where unlimited packages are being offered for very reasonable fee. 8) Do people understand that when they go online, grabbing a TV show violates copyright? For example, with regard to music copyright, some people argue that they listen to music free on the radio, so why can't they grab it online for free? So there's not a lot of education. Do people understand that they can copy a CD legally, but they can't do that with a DVD? Many think they can legally.

9) Are there excellent legal alternatives? There are some great legal online film services - but do they offer more content than the illegal services? 10) Are people in the film industry embracing the changes, or are many in denial?

Hopefully, this is not quite the "perfect storm", but I think you will see that there are some similarities.

So what are the key conclusions? 1) I would encourage film folks to embrace change. This is an incredible opportunity - yes there are threats - but it is important to embrace change and find solutions. In the music industry, there was frustration that we were unable to put new legal models online sooner. Many labels were waiting for the perfect solution, rather than trying things out and researching how consumers were behaving. 2) I would also say, work together with the legal services. Your best partners are content owners who are willing to put this stuff online and actually invest in new businesses. Make the content available - and also make unique content available (that hasn't been released from the catalogue), so that there is something new to offer in these services. Another point is, why can't the film industry try educating people about legal online alternatives in every DVD issued? 3) Listen to consumers. Consumers tell you what you need to know - but often you will not want to listen because they want what does not fit with the current model. Therefore, look at the illegal models - what are they offering that you are not. Should windows be reconsidered? I think they should. Putting movies online earlier is recommended - the windows system needs a complete overhaul. 4) Standards and interoperability - one of the frustrations that we hear a lot of the time from consumers is "I've got the iPod but I can't use Napster on it". Therefore, embrace standards, rather than creating hardware traps or proprietary/closed models. 5) New platforms - explore them. The music industry discovered that there was actually a multi billion dollar ring tone opportunity on the mobile platform. 6) Finally, there does need to be enforcement - without it, people will not take copyright infringement as a serious issue. Intellectual property is an incredibly valuable asset that we need to continue to invest in.

Thank you for giving me the opportunity to speak with you this morning.

Brad Duea's PowerPoint presentation will be made available at the BSAC website:- [www.bsac.uk.com](http://www.bsac.uk.com)

# GLOBAL VIEW FROM A GLOBAL PLAYER

## Josh Berger, Executive Vice President & Managing Director, Warner Bros. Entertainment UK

It's a pleasure to be talking to you about moving the film industry into the digital age - a theme which undoubtedly occupies an increasing amount of all of our time. Like many of you here, I woke to a digital alarm clock; I am wearing a digital watch; I've watched the morning news on a digital TV set; the car that drove me here has a digital radio; and, of course, tonight I might watch a movie on my digital pocket video recorder, or on what now seems like old digital technology, a DVD... so, we are moving into the digital age and it's a good place to be.



Josh Berger

If you are a consumer, then the digital age is pretty exciting: all these great products; this mass of information; so much wonderful entertainment. There's more for you; it's coming at you faster than ever; and there seems to be no end to the improvements. But what about those of us in the industries that supply these consumers...how good is it to be us right now? Well, we're also feeling pretty good. We've just come through another amazing season of film and television awards and the quality of what we're producing is as outstanding as ever and the revenues and profits of our industry continue to climb on a global basis. And it's at this time of year - when the industry reviews its most recent past performances - that we like to assess the future; to search for a new movie-making trend; to uncover what audiences want next.

For us in this room today, one of our future challenges is to take advantage of the fantastic number of digital platforms available to that audience. Digital multiplies and expands the way people can consume our films and see our television product-whether that's in their new home-cinema; in the car, on screens in the train station, on the move with their portable DVD player or the kids watching their own portable player-mini-DVD. And there's more coming-the day is not too far off when the latest movie promo will be streamed onto the inside of the lenses of your sunglasses. Sometimes we think that stuff like this is only in the latest sci-fi movies-but this is actually the promise of the digital world. Our promise to ourselves is to figure out how to continue to sell the experience of watching these films-multiple times on multiple platforms-and so continue to grow our business. We need to be smart and come up with straightforward solutions that serve our customers well.

As we move into this exciting digital age, one thing is clear - we cannot be as sure of the future as we once were. There are plenty of good things about making and marketing movies in this new millennium, but there are also some pretty daunting threats. Today I'd like to take a little time to look at some of the new opportunities that we see coming; to take a look at what will safeguard our industry today, and what will help send it into a prosperous future. And no discussion of this new and exciting digital world is complete without talking about the threat that accompanies it- film piracy.

So let's take a look at what the digital world looks like today. The way people are consuming media is changing: globally there are already 800 million people with access to the Internet. In several markets in Asia-like South Korea, Hong Kong and Singapore-almost every Internet connection is a broadband connection. Here in the UK, the broadband numbers have been improving sharply-they grew 71 percent last year and now include about a third of all homes. This is significant because broadband greatly enhances the speed of distribution of video content over the internet.

The UK is also particularly interesting for digital television. Over half of UK TV homes already receive digital TV and the Government has set 2012 as the switch-off year for analogue signals. High Definition TV will be launched by BSkyB in 2006 and James Murdoch's new HDTV set top box will also include PVR capabilities so Sky subscribers will be able to record in High Definition. Sky predicts that HD will help it reach 10 million digital pay TV subs by 2010. By then some 25% of all those Sky subs will be equipped with Personal Video Recorders.

The UK mobile market has also been one of the strongest in Europe and 3rd Generation mobile technology or 3G is also beginning to take off. "3" the UK's largest video mobile network, announced that more than 10 million music videos had been watched by its customers on their mobiles since the launch of its video jukebox service last August, only six months ago.

If you want the future, then the UK can give you another insight-it has the fastest-growing digital terrestrial TV market in the world with licenses for a DTT broadcast channel now reportedly commanding more than £5 million! Freeview is the fastest-selling multichannel platform today with an estimated 5m boxes in the market and may very well surpass BSkyB within the next two years. Not even Greg Dyke predicted that! And the UK is also one market where companies like Microsoft are launching their 'media centres'-set top boxes which are actually computers with the technology to take video content from the internet and transfer it onto the television.

Clearly we need to know not just how this technology works, but how consumers want to use it. As an industry we need to develop consumer insight at a deeper level. In the future, all of us in this room need to think and act more like fast moving consumer goods businesses, companies like Unilever and Procter & Gamble, who make knowing their consumers and how they behave a huge priority. In fact, our DVD businesses are looking more like these FMCG businesses every day.

Before I go any further, let me share with you the day of my own digital epiphany: A few years ago I was on my honeymoon in Central Java Indonesia. My wife and I had landed on a dirt airstrip in the middle of nowhere to visit the village of Borobudur, famous for its Buddhist monastery. We saw monks in saffron robes and bare feet going about their simple, daily rituals. This was as remote a place as we had ever been and seemed very far away from the digital world we had both travelled from. Then we went deeper into the village and there was a small wooden storefront. It looked inauspicious enough, but inside I found a DVD and VCD shop. Wall to wall disks. And these weren't just any movies; they were all the newest films—some that hadn't even opened theatrically in Asia—but all available to the local clientele... Even to the monks. Actually, this was about the best video shop I had ever been in, in the middle of nowhere. I remember thinking "Holy —Mother of God" do we have a problem. On one hand, I marvelled at what digital had enabled the pirates to do—to get all the newest movies into this remote village...I also wondered if our own company could have got the product that far, that fast?!! But I thought then—and I still do now—that as an industry, our challenge is to figure out how to harness the good that comes from digital technology—in short, the ability to distribute movies around the world virtually immediately—and at the same time limit the negative effects—namely reversing as much as possible the illicit trading of our films.

Digital technology means our consumers increasingly expect us to deliver to them the films they want, when they want them. We have to work to satisfy this demand. We have to offer solutions that are smart and straightforward for us and for our customers. We can do this and we will. For me, the most incredible statistic about film piracy is the estimated size of this illegal business. My experience in Java is an example of the strength of people who sell bootleg DVDs across the world. The MPAA believes that bootleg DVDs—or physical piracy—is worth \$3.5 billion a year in lost revenues. The UK pirate DVD market alone is expected to be worth some £1 billion by 2007, according to the UK Film Council's Film Theft report. Then there are the online pirates—websites that provide illegal downloads, or more insidiously Peer-to-Peer services, that allow punters to search thousands of other people's PCs for the film or TV show or the song they want. Deloitte Touche says that the cost of online piracy is even higher than the bootlegs, worth an estimated \$4 billion in 2004.

Now, as part of getting to know our customers better, we've carried out quite a bit of consumer research on how people relate to and consume movies. We were relieved to find that movies are still extremely important to all age groups. So the good news is - people still love movies. What really alarmed us in the focus groups was the extent of physical and digital piracy today, enabled by digital technology. 13% of UK adults are buying pirate DVDs and 9% are actively engaged in digital piracy. If you take the example of a tent pole title today, this level of piracy translates into a loss of over £12 million. Interestingly, what we've discovered in the focus groups is that we're losing considerable amounts of money during the theatrical release due to piracy. We all thought it was only a video problem but actually the exhibitors and the distributors lose an estimated £2.3 million as a result of people buying pirated disks or downloading the film instead of going to the cinema. And perhaps not surprisingly, we're seeing that heavy pirates are also our best legitimate customers - so we have a bizarre situation where our best customers are also our worst customers. And in their words what motivates them is the kudos of seeing the film before everyone else and—surprise, surprise—to see it cheaply or even for free.

I had my own brush with digital piracy a few weeks ago. I was on a long-haul flight and a well-dressed man sitting next to me took out his Arcos portable video player and proceeded to watch Million Dollar Baby. Now everyone here knows that Million Dollar Baby is not yet available on portable video players. Yet Clint Eastwood was making this man's day... Here's the dilemma we are facing as an industry: I am certain that my seat companion would have been willing to pay for the privilege of watching Million Dollar Baby that soon and on that device, but today there is no legal way for him to do that, so he becomes a pirate.

So here is the basic quandary: how do we serve our customers better than the pirates? Answering this question satisfactorily is central to our future in the digital world. As an industry we certainly need to continue to push to combat piracy on many fronts. And we are making progress: on the continent, the French government has taken the lead on anti-piracy, with President Jacques Chirac himself making it a top priority. The Republic of Ireland has also been very active in looking at more aggressive laws to thwart bootleggers in particular. In this country Estelle Morris and Tessa Jowell at the DCMS and Patricia Hewitt and Lord Sainsbury at the DTI have all been very supportive and I commend their initiative in organizing this October, during the UK's EU presidency, a conference focusing on piracy. But we need more help, like encouraging the new EU accession countries to crack down on piracy. We need tougher enforcement with police and Trading-Standards-Authorities making combating copyright theft a high priority. Given the importance of the audiovisual sector in the UK, it would also be very nice to hear Tony Blair personally weighing in against this illicit and illegal activity.

The industry is already working hard to help itself. The IP Trust for Industry Awareness has been a very good cross-industry initiative started by the home video distributors and retailers, and we would encourage exhibitors, broadcasters and all other stakeholders to join in. The MPAA in the U.S. has started to sue individuals for acts of movie piracy and while suing your customers is probably not the best business model, it is part of what we need to do: if there is a violation, there should be a consequence, and like the music business before us, we have to take a stand to protect our intellectual property and send a clear message. In one of our consumer focus groups, one 25-year-old said, 'If it was illegal, it wouldn't be so easy.' At Warner Bros., we were the first distributor to establish a worldwide anti-piracy unit, something that began in April last year. We did this to put substantial resource, both financial and human, to combat this problem. It is clear to us that as regards piracy there is no single solution—it is a multi-pronged approach that includes enforcement, consumer education, technological solutions, and new business initiatives. One issue in this area of immediate concern is the much-discussed topic of Windows. Staggered release dates—another way of saying windows—have worked for many years. Nowadays with piracy putting the pressure on, we all must question how we work in the future. Windows have been very good for studios but they have been very, very good for pirates.

So, what can we do? Well one example is when Warner Bros. Pictures released *The Matrix Revolutions* on November 3rd 2003 as a one-off theatrical release worldwide. No geographic delays; no chance for pirates in the US to send illegal copies to other countries; no possibility of pirates using their camcorders to dampen a single country's launch day. Mind you, these pirates still managed to put out a bootleg within three days of the release. That's all the exclusive time we have, but in my opinion, it's worth it. Day and date release is the trend of the future. The good news is that the film producers and exhibitors still get their opening weekend kick-off and the pirates lose out for a change. It's all about securing the future by recognising that the traditional movie release windows are evolving, and will continue to do so. It's about convergence and finding a profitable way to market, exhibit, rent and sell our films. It's about more joined-up thinking across different exploitation media to ensure we are making decisions in the long-term interest of growing the overall pie.

It's about being smart and straightforward. This is how we secure our future. One good example of this is the step we took in February that we hope will kick-start China's legitimate DVD sales market. Today in China the pirates control over 90% of the market. It's the first time something like this has ever been done: We're offering retailers in China our movies at prices that will compete with the bootleggers. More than 125 movies priced at around \$2.65. The pirate versions may be as low as \$1, but will not be of our high quality.

This is an example of a smart and straightforward solution that serves our customers and protects our business. Now let's take a look at what digital means specifically to cinema-going. People still clearly enjoy the communal experience of seeing a film in a quality cinema with popcorn, Coke and all the rest of it. UK cinema admissions are healthy at 170 million plus in 2004, but steps need to be taken to ensure the cinema's future in a digital world.

Warner Bros. is a big supporter of the Film Council's plan to install 250 screens with digital equipment over the next couple of years. It's clear that investment will pay off in a better quality experience for the movie-goer and—in the long run—lower costs for the exhibitor and distributor. This is important because as digital downloading to home cinema-style screens becomes easier, there have to be more and better reasons for people to go out to the cinema. Why couldn't cinemas offer customers who buy their tickets by mobile phone or online a free, exclusive downloadable preview of coming attractions or a loyalty voucher for a DVD of the film they have just seen? Maybe customers could be offered an exclusive ring tone from the film they paid to see at the cinema? These are just some of the beyond-the-box-office partnerships I think the studios and the cinema owners should be discussing. This is using digital to all our advantage.

Let's talk about some other new business initiatives made possible by digital technology: The studios have already set up legitimate download sites in the US and plans include the rollout of other legal ways for consumers to access our films. Let's just remind ourselves of some of these opportunities - Internet Protocol TV or IPTV, 3G phones, PDAs and PVRs, (and every other acronym I could possibly imagine). So we have a window of opportunity here to create the same culture for movie downloading as the music industry is beginning to enjoy through legitimate services like Napster 2. Apple has done a great job with its music-downloading site, the fabulous iTunes.

We need to focus on creating a customer experience for movies and TV programmes similar to what the iPod and iTunes have done for music. That's both smart and straightforward. Our industry is on a learning curve: it's not inconceivable that Blockbuster will be renting portable video players pre-loaded with films or TV shows one day; can't you imagine Odeon or HMV or even Tesco doing something similar? Couldn't BSkyB begin offering a portable PVR service that was topped up with content from their subscriber's set top box? These are the kinds of things being imagined right now, and much more. And in the online space, we already have MovieLink and CinemaNow - Internet sites available in the US, that aim to provide the same kind of solution as the best of the legal music download sites. It's still early days for these businesses, but the point is we are experimenting with different business models to make our content available legally. And let me say here today, we are in the advanced stages of creating in the UK a legitimate, online movie downloading service and we hope to make an announcement

# PROFITABILITY OF EMERGING SERVICES IN THE LONG TERM

Clearly, when and how we make our films and TV programmes available to our customers, and what we charge, continue to be crucial questions for our industry. But whereas the theatrical release will continue to be a critically important moment because it establishes the film in the market, digital will allow us to also make our movies available to consumers on new digital platforms at different price points, potentially closer to the theatrical release. In the UK, Warner Bros. has taken the digital reality to heart: We are pursuing deals with a variety of distribution platforms from VOD to mobile to IPTV to broadband. Warner Bros. already licenses films to Sky for its near video-on-demand services and subscription pay television channels; to IPTV service Home Choice in London for its VOD service. We also sell PPV movies to both UK cable operators and a VOD deal will be next. And as I mentioned, we will launch a web based, movie-downloading service and we are working closely with our sister company AOL in this regard. With the emergence of increasingly sophisticated mobile phones and the rollout of 3G networks in the UK and elsewhere in Europe, we are also actively licensing our content to this emerging multimedia platform.

This month our wireless team will launch our most advanced mobile game to date in Europe with Constantine, based on the film of the same name. It's a stunning game and importantly, it allows us to make our marketing spend go further, while tapping into an emerging market that will bring in additional revenues. And it's now common practice to offer alongside the game a complete suite of mobile content, including exclusive behind-the-scenes video, wallpaper, screensavers and voice & ring tones. Mobile multi-media is just one way that the future will open up for our business. There are many more ways and a whole bunch of others that we haven't even thought about yet, all care of digital technology. One thing we know is that the time to sort all this out-to have these new ideas, to stretch and challenge ourselves in the digital age-is right now.

There's never been a more exciting time to be in this industry. The fundamentals of filmmaking remain the same-telling great stories on film. But the advent of digital technology means that we're at the threshold of a radical shift in how we experience movies. Even though it's early days, movie lovers have already shown us they want our movies faster, easier, and on as many devices as we can imagine-and more. The man who sat next to me on the plane recently watching Million Dollar Baby is all the example we need to show us what we have to address. In the digital age we must provide secure and easy ways for them to see movies when and how they want to. It's as simple as giving the people what they want.

Thank you very much for listening.

**Chair: Theresa Wise, Partner, Media and Entertainment, Accenture**

**Josh Berger, Executive Vice President & Managing Director, Warner Bros. Entertainment UK**

**Bruce Eisen, President, CinemaNow, Inc.**

**Brad Duea, President, Napster**

**Terry Ilott, Chief Executive, Hammer Film Productions Ltd and Partner, Bridge Media**



Theresa Wise

The Panel Chair, Theresa Wise, introduced the panel members and invited Terry Ilott and Bruce Eisen to begin the session by responding to the previous two speeches by Brad Duea, Napster and Josh Berger, Warner Bros. Entertainment UK.

**Terry Ilott, Chief Executive, Hammer Film Productions Ltd and Partner, Bridge Media:**

I was here last year, and I am very pleased to see how much has changed in only a year. I am not sure if we are up to speed with the events that are happening out there in the world, but we are trying hard to catch up. However, I do feel that the discussion on business models, and how they are changing, is still very much focused on distribution and revenue generation - or, in the case of piracy, on the loss of revenue. I think there is a case for saying that the business model needs to change in the origination/development and the production areas, and not just in the distribution areas. Its not just a question of Josh Berger delivering Warner content in faster and more efficient ways - its also thinking about what kind of content will be demanded in the future. And this has not only commercial implications, but also implications for education, training, regulation and policy. I was of the same mind as Julian Friedmann (who asked a question during the Minister for the Arts' Opening Address), when he talked about the dearth of adequate training in the area of script writing and development.

Brad Duea's presentation asked, "What does the consumer want?" This is important. I think that some things that come out of his presentation are applicable also to the movie business. Its clear that what consumers want is choice, ease of access, and ease of navigation. This is the Google generation - the generation that knows how to use search engines. Some implications of this are that there will possibly be greater demand for niche products, for cult and genre products, for example similar to those that we have at Hammer i.e. horror films.

I think there is also the possibility of bringing new products through something akin to the "garage band" type phenomenon in the music business.

You could think of radio as having been a Big Band kind of medium, and digital audio distribution via the Internet as being a garage band medium.

Something similar could happen in film, with low-cost, semi-professional products targeting niche audiences. Also, the interactivity of audiences with certain event television brands is something to consider in terms of movies.



*l-r Terry Illott and Josh Berger*

However, there are differences between music and TV and film. For example, films cost a lot of money, both to make and to market. Also, the fragmentation of the audience implied by digital is running in completely the opposite direction from the cost of delivery. There is a paradox, in that digital leads the audience to have a higher level of expectation of production values, while the economics of the business is following possibly a music-type model even though the essential economics of film are not like music at all. For film there is the prospect of high unit costs, high marketing costs and audience fragmentation - these do not add up. I'm not quite sure where that's going to go. I think one way out of that is through branding and spend on marketing - which means stars. The film industry is good at that - it's good at maintaining consumer interest in specific products. But I wonder whether in fact what we'll see is a new kind of movie product - a new way of telling stories. I think narrative may change, and it may change in ways that are quite surprising. The younger generation is being brought up on video games and on interactive media. They are using new skills when they consume media and are beginning to experiencing different kinds of narrative. I would agree with Brad's comment, when he said, "It's about the music". With movies, it's about the story - not the pipeline.

**Bruce Eisen, President, CinemaNow, Inc:** CinemaNow provides many different types of content (but mainly films) via video on demand (VOD). We've got deals with all the major studios in the US, except Paramount. We also have a deal with ABC TV for news content, and various deals for sports content, music video, and children's programming. We make the content available via the Windows Media format, which is protected using Microsoft's DRM solution. CinemaNow has territorial blocking, for example if you go to the site from the UK, you will not be able to see any of the Warner, Fox or Sony films because we do not yet have the UK rights. Films are available in one of three ways:- 1) Rental (available for the studio films), 2) Monthly Subscription (2,000 independent films are available, news, sports, music videos - studio films are not available on this option yet), 3) Purchase (download-to-own - again, studio films are not available for this yet, however this might change this year).

We know what customers are looking for. They are frustrated because the range of films available on CinemaNow is much smaller than, for example, Blockbuster. Another factor is that when a title is in Blockbuster - it stays in Blockbuster. With CinemaNow, because we are in the pay per view window, a title comes in - we have it for 90 days - and then it goes out. We won't see that title again until it's a library title, which could be 10 years later. So, customers are very confused about that. They think that everything should be available on video on demand.

I think they're right. They want TV programming - we do offer TV programming, but we can't offer Friends, or ER, or any of your favourite current/recent TV shows, because we may only have material which is over 10 years old. Interestingly enough, the highest amount of digital piracy occurring currently is for TV shows. So, we can see that people want different offerings online.

We talk to the studios a lot - and there are legitimate business reasons why things are the way they are for the most part. However, the limitations are frustrating - particularly when the piracy behaviour shows that there is a huge demand for current TV shows and studio movies online. Other than CinemaNow, there is also MovieLink in the US, which is owned by 5 of the 7 studios. So, there are the means for getting the content that people want out to the people, but for various reasons the studios are moving very slowly in doing that. Another thing to consider is that when people acquire content, they want to be able to watch it in the way they want and wherever they want. This does not mean sending content all over the world for free - it means having the ability to watch it in the living room, or in the bedroom, on the handheld etc. You can do all these things with a DVD - as to whether or not that's allowed is still up in the air from a licensing point of view. Frankly, the value proposition that is currently being offered via online film services is less than optimal. Again, this is related to licensing issues but nevertheless presents problems here. If you rent a film from CinemaNow, or MovieLink, you have it for 24 hours. So, once you hit "watch movie", you can watch it as much as you want, but you have to finish in 24 hours. Compare this to a video store in the US where you can rent a film for a week. This is a significant difference.

I think that the industry should be less focused on suing the customers. Recently I spoke with the daughter of a friend of the family who is in college. I asked her, "Have you heard of CinemaNow?" No. "Do people download music and movies illegally?" Yes. "Have you heard of people getting sued for this?" Yes. "Has that stopped anybody?" No. The answer is not to sue - but to make content available in a way that Josh's friend on the airplane would have paid money for, given the option to do it. One last anecdote - I spoke to one of the tech people at a different studio.

This guy was paranoid beyond all imagination about piracy. Somebody wrote a book that pointed out that if you owned a \$100 million electronic microscope, you would be able to peer into the silicon on the chips and be able to crack the DRM code. This guy was paranoid that people were going to start doing this. He held up a new DVD that they had developed and said, "Do you see this DVD? This is the greatest DVD ever made. Nobody can watch anything on this." To him, that was Nirvana. I think there's a better way of dealing with the problem.



*l-r Brad Duce and  
Bruce Eisen*

**Panel Chair:** In order to exploit these new revenue sources, companies will need more insight into the customers. However, it would seem that there is a trend emerging, whereby some media majors are actually disposing of some of those touch points with the customer, for example Viacom's disposal of Blockbusters, and Warner Bros. selling their cinema chains. Studios are now beginning negotiations with telecoms operators to deliver video on demand. Is this an area where Warner Bros. is looking to get closer to the customer? Also, is it challenging negotiating with telcos?

**Josh Berger, Executive Vice President & Managing Director, Warner Bros. Entertainment UK:** It's an interesting issue - how much studios want to own distribution media as a way to get close to customers. You don't have to own the cinema or own a VOD platform to understand your customer. You just need to talk to your customers and see how they behave, what they want, and how they listen and then respond. We've gone in and out of owning different distribution media. Our parent company, Time Warner, certainly owns many different distribution outlets that that distribute films. And, we've all heard that it works incredibly well between them, and then other times it doesn't. The telcos are just another distribution channel among many today. The focus for us is to understand the various ways that different audiences want to watch movies, and to provide movies to them.

**Panel Chair:** The music industry has had a tough time, and is now looking to get revenues not just from the physical formats like CDs, but it is also investing in the wider music proposition including live concerts etc. Is the music industry getting these things right now?

**Brad Duce, President, Napster:** It's really interesting when you look at some of the models out there. I mentioned that one of our competitors is doing a great job, but their model is a hardware driven a la carte model. I think that's a concern for content companies. Our approach is different - we say to customer, if you subscribe for a year we'll give you a brand new MP3 player.

So we're making it about the music, and marginalising the hardware. This makes sense when you look at the cell phone model approach, or even the Sky set top box model. I think when you see music being used for advertising models, or for driving hardware sales, or promoting soda pop - it does actually reinforce the feeling that it's for free, rather than that the music has value. I think there needs to be more focus on making the content valuable, not the other way round.

The Panel Chair opened up the session to questions from the floor:

**Mark Isherwood, Rightscom:** Is MovieLink likely to experience the same kinds of difficulties as Pressplay and MusicNet?

**Brad Duce:** The original strategy of Pressplay was to cut out the middleman and deal with the consumers direct. The problem was that the Pressplay's labels (Sony and Universal) and MusicNet labels (BMG, AOL Time Warner, EMI) would not licence their own music for use on the other service. So each service had only half the music catalogue. This was very frustrating for consumers. When Roxio acquired Pressplay, the labels eventually came round to the idea of licensing their content to digital distribution experts who could make a business out of it. Therefore, there are some big differences between Pressplay, MusicNet and MovieLink. However, there are also some similarities - for example, when Pressplay was first set up, you couldn't buy more than two songs from the same artist in a given month, and burning wasn't allowed. As Bruce Eisen has mentioned, it would seem that there are restrictions currently for online movie models. I would encourage folks to embrace the online distribution model and get the rights and the content there faster. I do think that it's more appropriate for distribution to be handled by a third party. The final comment I'd make is that you also have to allow those distributors to actually build a business. There is virtually no margin for download purchasing, but there is a margin for subscription - which is why Napster has invested \$100 million in its own subscription model. I think that if the content owners try to squeeze the middleman out of business, they will actually experience more problems, not less.

**Paul Kafno, HD Thames:** What is the future for interactive content?

**Bruce Eisen:** If history is any guide, the porn industry will be leading in this area. There is also a strong demand for interactive content in the form of games, which are also getting more and more movie-like. However, there will always be a market for more passive entertainment.

**Panel Chair:** Interactive content tends to be very device dependent - for example, games do not generally translate very well to devices other than the console. Therefore, interactivity is very much a function of the specific genre and the specific device.

**Josh Berger:** The way kids interact with content is astounding - they actually prefer interactive entertainment to passive entertainment. Unlike adults, they will watch movies on small devices, they will watch TV programmes, play games, and they will play with each other through wireless connections. These kids will drive the different types of content and the way it's made available.

**Ben Keen, Screen Digest:** Bearing in mind Brad Duea's comments that there are more attractive margins with subscription models compared to download models, how will CinemaNow's business evolve?

**Bruce Eisen:** I think that both subscription and download-to-own models are likely to prevail, and rentals will become the least important. The subscription model is great because companies know how much money is coming in each month, and the margins are better. Subscription is also good for the consumer because of the unlimited access to content. The CinemaNow subscription package has a large collection of "long tail" content - not immediately popular content which people tend to watch fragments of, rather than watching the whole movie in one go. On the CinemaNow download-to-own model, there is a lot of high definition content available, and this is very popular. The advantages of download-to-own is that people don't have to worry about their subscription expiring etc.

**Josh Berger:** There is already an interesting example of a successful subscription model in the market - BSkyB has about 5 million subscribers paying decent amounts of money every month for their movie channels. Sky's NVOD offering - about 60 channels of pay-per-view movies - is a fantastic offering as well, and it has an earlier window. The economic activity created between those two offerings is like night and day - the subscription business creates hundreds of millions of pounds, and the pay-per-view and NVOD service doesn't even come near that. The subscription model is definitely very powerful, and we are likely to see more companies offering content on this basis.

**Roger Lynch, Video Networks:** VOD services are actually not dissimilar to video stores, yet studios are treating them as though they are extensions of pay per view - this prevents services like CinemaNow from flourishing. Might this treatment of VOD change in the future?

**Josh Berger:** I agree 100% that there are currently some barriers because of the way that Hollywood is organised. I wish things were different, but the industry has to take a joined up view on the home entertainment model.

**Bruce Eisen:** In the US, HBO is very powerful because it pays the studios vast amounts of money every year. Their contracts with the studios are therefore relatively favourable, whereas with CinemaNow they impose restrictions. However, CinemaNow is currently in discussions with several of the studios for the download-to-own rights - and perhaps this would swing in its favour this year. The discussions seem to indicate that CinemaNow could pay wholesale prices for films, and then set the prices for downloads. Films would be available for longer than 90 days (which is the norm for the pay per view window), therefore it would seem that the studio lawyers have determined that making the digital file available on a sell-through basis should be different to the current licensing system for VOD, in order to avoid problems with HBO and/or any other conflicting licences.

The Panel Chair thanked the panellists for a fascinating session.

# THE BATTLE FOR FILM AUDIENCES IN THE HOME

**Chair: John Howkins, Deputy  
Chairman, BSAC and Director of  
Equator Group plc**

**Roger Lynch, Chairman and CEO, Video  
Networks**

**David Thatcher, MD Sales and  
Marketing, NTL**

**Karen Saunders, Head of Pay Per View,  
Sky Networks, BSkyB**

**Saul Klein, CEO, Video Island**

The Panel Chair, John Howkins, invited the panellists to outline their companies' technologies and business models.

**Roger Lynch, Chairman and CEO, Video Networks:** Video Networks is a convergence company. It's consumer brand, HomeChoice, provides digital TV, video on demand, broadband Internet, and free phone calls - all delivered down a phone line, i.e. DSL. The technology is complicated, and we have a lot of investment in the network. Video Networks is similar to cable companies, in that we have to put the network in the ground, and we have a head end where all the broadcast channels are captured (off fibre or satellite) that is connected over a wider network to server centres. Video Networks has three server centres (in London), where all the on-demand content is kept. Each centre can store about 10,000 hours of on demand content - so at any one time we will be offering well over 1,000 films from most of the major studios, lots of TV content and music videos, as well as a large range of broadcast channels. The servers are connected by very high capacity fibre links to BT telephone exchanges. Inside each exchange we have installed DSLAM equipment which enables DSL to be put on a phone line. Currently, over 99% of all DSL lines in the UK are provided by BT directly - the problem with that is that BT's network can't support some of the services we provide, therefore we are building out our own DSL network. So, we have a network that is ready to add customers. When we add one, it's as simple as a normal phone line. A new customer is disconnected from the BT network, and then connected into the Video Network equipment in the exchange. Our service is delivered over the phone line, and then to a set top box - which then connects both to a television and to a PC (because we do provide a broadband internet service).



*l-r David Thatcher,  
Roger Lynch, John Howkins,  
Karen Saunders, Saul Klein*



*Roger Lynch*

HomeChoice offers entertainment and communications services in a bundle with a range of options. The typical entry level package is £27.50, which provides a 1 megabit broadband service, a digital TV package that includes many of the most popular pay channels, free video on demand content, plus access to pay per rent video on demand content, digital radio channels, and free phone calls.

From entry level, customers can upgrade to a number of different options. Our average subscriber (ex VAT) is paying over £40 per month. Roger Lynch then showed a short promotional video for Home Choice.

We have created some of our own on demand channels. Scamp, for example, is a pre-school channel - it is the most watched kids channel on our platform. V:MX is a personalised music service - it gets a 60% share of all the music video channels on our platform. C1 is a general entertainment channel (i.e. mainly comedy and dramas), with lots of content from Warner Brothers, Fox and other studios, as well as the BBC. At any given time, C1 has 300 - 350 hours of content on it - it is generally the 2nd or 3rd most watched channel (the most watched channel is BBC1). Got to Know is a factual channel that we created with Discovery. I think that our programming success shows how effective aggregating content can be. Although we do provide Sky's movie channels in traditional linear form, we also have our own VOD-based channels. Film 1st is a premier channel which provides all the latest studio releases - films are available for 24 hours at £3.50. Movies Now Unlimited is a library film channel with thousands of films at £2 each. We launched Movies Now Express last summer with Disney and Warner Brothers - this is a subscription-based channel providing 50 films per month for £5. Screenies is a kids-based VOD film channel. I think that getting the right mix of transactional revenue models as well as subscription models is important. Since we launched Movies Now Express, which is a library VOD channel, we have noticed that the viewership of library films has increased dramatically. In fact, it does not hurt our library pay-per-rent channel, Movies Now Unlimited - so I think getting the right balance is very important. In addition, it really helps monetise library content, which is precisely where studios are looking for better ways to derive revenue. The pay-per-view model, especially for VOD, I think is very successful. Our buy rates on these films are generally 3-5 times higher than what pay-per-view operators would see.

Earlier we have heard about the success of HBO in the US. HBO has an on demand service, as does Show Time, Starz, and many other providers. The services I have seen in the US are a bit problematic - if you want to watch film, where do you go? You have got to go into HBO and look down their silo - if they don't have it you go to Starz, and then perhaps on to Show Time. This does not result in a very good consumer experience. So, the ability to aggregate all the films in to one spot where people know where to go is a much better consumer experience. This requires lots of licensing relationships with studios, record labels, children's entertainment providers, broadcasters - it's an important part of our business to enable that.

This paradigm shift has a dramatic effect on broadcasters, and they are starting to realise this now. There is a lot of talk about how PVRs will impact on advertising, and the effect of TV piracy. I think that the studios and other filmed entertainment rights owners are a step removed from what is happening. When music downloading started, people stopped buying music. Although broadcasters are still licensing TV content and selling advertising around it, people have started downloading these programmes. In time, as the audiences go down for these premium shows, broadcasters will have less money to pay the rights holders. Therefore, enabling broadcasters to extend their brand into the VOD space is something that we are interested in doing. Through our EPG we have developed a PVR service that broadcasters can take advantage of. The service helps broadcasters extend their brand into the on demand world, and importantly, keep it within their own brand environment. The service is simple to use - it currently provides quite a lot of content from the BBC and some from Channel 4. We are hoping to get the other broadcasters involved in this also.

HomeChoice was launched in September of 2004, and is currently available in London only. We have been responsible for about 1 in 5 DSL net adds in the fourth quarter of 2004. About 90% of our new subscribers take the full triple play. We are hoping to expand the subscriber base to 2.4 million by May 2005 - the next step will be to move out to other cities around the UK.

Roger Lynch's PowerPoint presentation will be made available at the BSAC website:- [www.bsac.uk.com](http://www.bsac.uk.com)

**Karen Saunders, Head of Pay Per View, Sky Networks, BSkyB:**

One of the questions we were asked to consider was, "Is new technology going to challenge the current business models?" I think there is a place for a lot of new models, and we shouldn't just be thinking about the introduction of new services like video on demand, or the growth of the rental by post industry. We also need to look at other competition for film audiences in the home. There are a huge number of other channels in multichannel homes that are providing movies now - ITV2, ITV3, BBC4, SciFi, Paramount etc. There are lots of other places where customers can watch films - not just on the pay TV services. There has also been a massive growth in DVD - driven by marketing from the studios and a sharp reduction in pricing. People are acquiring large collections of DVDs and upgrading their viewing systems at home (to LCD panels, plasma screens etc.) for a better quality viewing experience. So, in terms of competition for audiences in the home, there are lots of other ways in which the models are being challenged.



Karen Saunders

All this is very good news for the customer, but I still think there is still a very big place for traditional models of subscription and pay per view. Sky has over 5 million customers, most of whom are on the DTH platform subscribing to 11 film channels. There must be a reason that they still subscribe, and not dashing off to just take advantage of these other services. Josh Berger mentioned the combination of the pay per view and Sky Movies: many of our Sky Movies' customers are also buying pay per view - and they are also going to the cinema, buying DVDs and renting movies. People who love movies, love movies, and they will access them in as many different ways as are provided.

So, in the face of so much competition, why are they still subscribing? It's because Sky provides a lot of choice. We show over 2,000 movies every year, including almost all the top 100 theatrical movies across the Sky Movies service and also on pay per view. In addition, we also license movies from British distributors, and last year we introduced the world cinema strand, which is serving quite a niche audience. But it's not just about choice - it's about managed choice. It's about how we get customers to the right movies at the time that suits them. I agree that companies need to build relationships with their customers, which is something that Sky does very well. The PVR is one area where we are able to do that. When we introduced Sky +, we gave people the opportunity to create their own schedules. Our PVR customers are not tied to the TV schedules - they can record their own programmes watch them when they want. However, we have discovered that in Sky + homes, many people first check what is on their favourite channels before they look at their recorded programmes - because at the end of the day, there might just be something that they'd rather be watching that they didn't think to record. So there is still a certain amount of trust that the broadcasters will be able to schedule a programme that they would like to watch. PVRs also produce high satisfaction ratings, and this means low churn. This is why Telewest is also going to introduce PVRs - they are hoping that it will not just help their network management for their VOD services, but that it will increase customer satisfaction and "stickiness". Our research shows that movies and drama are the most watched genres on PVRs.

In terms of alternative distribution systems - Sky is platform agnostic. As Roger Lynch mentioned, we make some of our services available to Home Choice, to the cable companies etc., but we are not necessarily sure that the experience they get there is as good as the experience they can get with Sky. If we thought there was a demand for another technology, I think we would provide it if we felt it would improve our customer experience. In terms of broadband, currently connection speeds in the UK are quite low compared with the US. About 30% of people have broadband connections. Prices are coming down, and pipes are getting bigger in terms of what they can provide - so we are likely to see some improvements in the future. We did launch Sky Sports Broadband some time ago. However, in terms of taking our broadband proposition further, we feel that the speed and capacity of broadband needs to improve.

The key to all this is going to be security. We have a very secure platform, and the studios are very rightly concerned about piracy. They don't want to licence content to new services and technologies that are going to allow their films to be pirated. However, I do think that they really do need to embrace new technologies and provide legal alternatives, because otherwise piracy will grow further, and demand will increasingly make people want to use illegal means to get the films.

The last thing I would like to touch on is High Definition (HD). Sky will be launching HD next year - I think that with the growth of plasma TVs and LCD screens, HD is going to be something that is going to satisfy the increasing demand for better pictures. In the US, movies and sports have been big drivers of HD, and I think they will be in the UK too. We haven't finalised our programming offering yet, but we will ensure that people are given a first rate experience. I saw a demonstration of HD this week, and the difference was truly amazing.

I think there is room for all kinds of services - subscription models are especially strong. Sky Movies provides both choices - subscription for the slightly older titles, which can then be topped up with pay per view for the newer titles. I believe that windows will probably collapse - I see perhaps a transactional window comprising electronic retail, rental, physical retail and pay per view, followed by a subscription window. I don't think that that will take as long to arrive as it did for the studios to drop the pay per view window from 6 to 3 months. This time the windows will collapse much quicker.

But there will always be a place for Sky Movies and the subscription model because people do want an easy experience. Some people want to work hard for their choice, i.e. to go and search for a movie, but a lot of people are very comfortable to come home, sit down after a hard day, and actually trust the broadcaster to provide a movie that suits them. So, I think Sky Movies will always be a valued service.

**David Thatcher, Managing Director, Sales and Marketing, ntl:**

Good afternoon everybody. My eight-year-old boy thinks I have the best job in the world. When I got home yesterday, he asked me what I had been doing that day. I told him that I had been to look at the new football stadium where we have sponsored a stand. He asked me if I had met the manager of the local team. I said yes. "Wow Dad, your job's great. What are you doing tomorrow?" I told him that I was speaking at a gathering of experts in movies. He asked me if I could tell you his film joke. The joke is: "What is ET short for?" Extra Terrestrial? No. "He's only got little legs." So, I apologise for that, but you have made an 8-year-old boy very happy.



David Thatcher

Today I am going to talk to you about ntl and ntl On Demand. I have not brought a promotional video with me, but if I had, it would look much like HomeChoice's video. Our service has many of the same features as HomeChoice - there is a good reason for that, both our businesses are highly customer driven. This theme has come out loud and clear in the previous panels - it's not rocket science, but customer driven services is what it's all about. Ntl has been in business for 15 years. We spent £9 billion building our network, which passes nearly 9 million homes. Over 3 million of those homes are ntl customers. We still think of our network as a triple player (i.e. a telephony service, TV and Internet).

I think it is fascinating to hear Roger Lynch describe his network as a quadruple player. Our on demand proposition is intrinsically entwined with our television proposition, and we have constructed a 21st century network. Although there are some areas in London the rights to upgrade are still a debating point (because there are some old bits of the BT network remaining), but broadly we can offer IP on demand, and/or complex telephony propositions.

Until seven weeks ago, our TV proposition was very much like the one Karen Saunders was describing. We looked a lot like Sky frankly - we carried all the channels that really matter, we carried their movies and sports propositions in much the same types of packages. However, seven weeks ago, in Glasgow, 80,000 people went to bed and the following morning they woke up with an on demand service. I guess that's the difference in terms of scalability that the £9 billion investment gives us. Last week, our customers in Cardiff and Newport had the same experience. By the end of this year, ntl On Demand will be in well over 2 million homes. By the end of next year our entire network will be on demand. That's a huge change for us, and we think it massively changes the customer experience. The consumer needs portability, choice, convenience and control. If we don't deliver that I think we're all in trouble. So we have worked hard on making it very easy to use - we have menu-driven options, red button interactivity, special offers, and pay-to-download content as well.

One of the critical differences between our proposition and others is the way our partnership works with the studios. Our partnership choices are for a specific reason. We have created something that we call the "farmers' market", whereby we - the platform - don't set the prices, set the release windows, run the promotions, do the scheduling. The scheduling is down to the customer. But what's accessible to customers, and how much is charged, is largely determined by the studios. Our job is to facilitate, help, support and provide the infrastructure. The joint venture that we have established with Sony and Disney, with the help of the On Demand group, has really helped us to move our business forward.

We have the benefit of having come to the party slightly later than HomeChoice and others in both the UK and the US, and being able to learn from their experience. We spent longer than we anticipated putting this offering together - part of the reason for this was some of the financial issues we were dealing with. Another reason was that we made an absolute determination not to do what cable has some history of doing in the past - i.e. launching something that doesn't work as well as it is capable of. I'm very proud of our new service - after substantial research into what consumers want, we have tried very hard to build a service that makes content easily accessible.

With apologies to Gil Scott Heron, we think this evolution will be televised. It's very difficult to make decisions - I suspect that you will be told to back all the horses. That's what all of us would like to do, but normally funding makes that impossible. The world will change, perhaps over next 10-15 years - but linear TV will also remain. As Karen Saunders was explaining, Channels 1-5 are still consumers' default choices, followed by some of their other favourite channels. Even now, long after Sky first launched its analogue multichannel proposition in the UK, 40% of viewing in multichannel homes is on terrestrial channels. But, there will be a gradual transition - and we are seeing our customers embrace it now. I am not able to provide you with our subscription data, but I can say that we are exceeding our expectations, and we are receiving complimentary comments on our service from our customers. Our focus going forward is choice, convenience and control.

David Thatcher's PowerPoint presentation will be made available at the BSAC website:- [www.bsac.uk.com](http://www.bsac.uk.com)

**Saul Klein, CEO, Video Island:** Video Island uses a three hundred year old distribution system called the postal network, and also the relatively new technologies - the DVD player and the Internet. These three forces combine to deliver on demand entertainment at home.



Saul Klein

Here are some facts and figures about the UK market. 89% of all online homes in the UK have a DVD player. Nearly 10 million adults in the UK rent a DVD at least once a month - this is segmented by people who rent more than four times a month (about 2.3 million), to people who only rent once a month (about 3.7 million) - so Video Island is addressing quite a large available market. Our business is all about what the consumer wants, and selection. We have now 30,000 titles available, which, when you compare it with the high street store or the leading pay TV platforms like Sky, gives consumers an unbelievable choice of movie content. It's also an incredibly convenient service, direct to your door.

It's a monthly subscription service, so customers can cancel at any time. It's superb value for money- about £1.99 per rental on average, and the postage is prepaid. Like Napster, we also offer a free trial. We have built in some popular features such as personalisation and social navigation. When a customer enters our website, the page will offer 10-15 movies based on their rental habits, and on the rental habits of people like them.

In a short space of time we have built the largest franchise in the UK market. We currently take about 37% share ahead of Blockbuster, which is our nearest competitor. We've done this by creating a platform which some of the largest brands in the UK use to get into home entertainment business. The Video Island business currently runs five consumer brands on its DVD rental platform:- Screen Select, Tesco, MSN (which launched its DVD rental service last month), ITV; and next week we will launch the new Easy DVD rental service on our platform. We also have distribution relationships with some of the largest high street franchises including:- Comet, Curries, Dixons, Boots, Toys R Us etc. We also work with Top Up TV to provide a movie choice on the Freeview platform. We recently also announced relationships with the Sunday Times, The Times and Real Networks.

We are focusing our efforts on the customer and what they want. Over 80% of every DVD that we send out are subscribers' "highest priorities", and over 90% are dispatched within 1 business day. We have the largest selection of DVDs to rent in Europe. 17% of our rentals are TV shows, and over 17% rentals are titles that have had been out for more than 3 years [?]. Even after only 12-14 months of operations, we are beginning to see an effect on consumer behaviour. 64% of people who we surveyed in December said that they no longer rent DVDs from high streets. In a very short space of time, the online sector in the UK has captured between 6-7% of the entire UK DVD rental market, with Video Island taking between 3-4% last year (based on the MRIB figures). Best of all, the consumers love the service - 84% are very satisfied or satisfied with the rental experience, and 94% of our customers would or do recommend our service to friends.

So, on average our subscribers rent about 27 movies per year, compared to the UK average of 7 per year. Our customers are religious about telling us what they think of the movies - we have got 3.5 million ratings in our system, and nearly 100,00 reviews. In addition to renting movies, 54% of our subscribers go to the cinema at least once per month, 51% buy a DVD to own at least once per month, 20% of them watching Sky, NTL or HomeChoice.

So, these guys love the movies and will try to get them wherever they can. We have won some awards and had some great reviews this year, e.g. from Which, Revolution, Net Imperatives and BVA.

We are working very productively with some of the studios, both in the UK and in the US. We are beginning to see that by offering people a choice of 30,000 titles, this is an excellent way for studios to exploit their niche and older catalogue titles. Thank you very much.

Saul Klein's PowerPoint presentation will be made available at the BSAC website:- [www.bsac.uk.com](http://www.bsac.uk.com)

The Panel Chair then opened up the session to questions from the floor.

**Charlie Sandbank, DTI:** Does Video Networks have any plans for high definition TV? Also, is Video Island's subscription fee subsumed in the £1.99 average cost per rental?

**Roger Lynch:** Video Networks does indeed have plans for high definition. High definition requires 4-6 times as much bandwidth as standard definition, and in order to deliver it over DSL there needs to be more bandwidth on the DSL network and better compression. Therefore, the key to delivering high definition over DSL will be MPEG 4 advanced encoding. All our set top boxes in the field are MPEG 4-capable, and we will be launching MPEG 4 very shortly. High definition also requires more bandwidth on the phone line - currently in the UK there is only one standard that is used, ADSL, but soon the new standard ADSL 2+ will be approved for use. This significantly increases the amount of bandwidth that is available on phone lines - HomeChoice's equipment is already capable of using this.

**Saul Klein:** Video Island offers monthly subscription packages that start from as low as £7.97 for unlimited DVD rentals through Tesco, to fixed rental packages of 5 movies per month for £10. Easy DVD will be pioneering a new model which is similar to a pay-as-you-go top up model. Our model enables brands to test different packages and price points. The average rental cost comes out at £1.99, which is favourable compared to high street rental costs and pay per view.

**Josh Berger, Time Warner:** Are the panellists considering providing download-to-own film services? If so, when?

**Saul Klein:** The starting point is understanding the consumer experience well. Video Island has acquired a large number of subscribers and a large amount of customer knowledge. This will enable it, perhaps in the next 6-12 months, to start offering people the ability to rent and buy movies via downloading as well as physical distribution.

**Roger Lynch:** The download-to-own model is a great natural extension of most of the offerings represented on the panel, because DVD purchasing has proven very resilient so far. Combined with the ability to choose from a list of thousands of films, whether you want to watch or own it, is a great service. HomeChoice already offers a similar service through its music channel V:MX, whereby subscribers can select and download tracks for their MP3 players.

**Karen Saunders:** Download-to-own is a very interesting proposition, but storage is a consideration. Would films be stored on a PC, or copied to DVD, for example? If people are buying something to keep, most will want to have a physical copy - at least for some time yet.

**David Thatcher:** The consumers will be able to decide for themselves about storage. The critical point is that this is happening already, mostly illegally. The question is how much we can learn from what's happened in the music business. The second challenge is that if we don't have an infrastructure that supports it, there's a problem.

**Fiona Clarke-Hackston, BSAC:** What is the future for the TV advertising model?

**David Thatcher:** Although it is probably too early to say for sure, it does seem that the advertising model is likely to change. We are beginning to see a demand for a different form of advertising from both consumers and the advertising community.

**Adrian Barr-Smith, Denton Wilde Sapte:** How do you view Tesco's role in the filmed entertainment market? Is it a normal retailer, or is it more of a warehouse?

**Saul Klein:** Tesco increasingly sees itself as a service provider as well as a retailer. It is a multiple service businesses, offering insurance, mobile and fixed line telephony etc, and it has recently launched a music download service as well as the DVD service through Video Island. Although they haven't necessarily stitched all the pieces together, they are in "triple play" mode, in that they are offering a home entertainment service, telephony, and also broadband access. Tesco is an incredibly powerful force in understanding what consumers want - it has 12+ million consumers on its club card database. We've had a fabulous experience working with them because they really understand their customers. I can't answer for the studios, but I would suspect that Tesco is one of their top 5 sales points now, whereas it may not have been 10 years ago.

**Karen Saunders:** Tesco is more than just a retailer or warehouse, it is brand that has created strong relationships with its customers. In the same way, I would say that Sky is not just a pipeline - it's a brand that is very good at putting together packages and marketing propositions that are attractive to customers and build loyalty.

# THE ARRIVAL OF DIGITAL CINEMA

We work very closely across the film industry putting together propositions that are attractive and exclusive for customers - we definitely don't see ourselves as just a pipeline.

**Roger Lynch:** Tesco is a phenomenal retailer - they garner £1 in every £8 pounds of retail money spent in this country. They have a relationship with their customers, and have one of the strongest loyalty card programmes in the country. I think we'll all be doing business with them over time.

**David Thatcher:** Tesco understands its customers brilliantly. They know what to sell them and how to sell it - but they are also a retailer in that they drive a hard bargain, but they work very closely with their wholesale partners.

The Panel Chair thanked the panellists for an interesting session.

**Chair: John Howkins, Deputy Chairman, BSAC and Director of Equator Group plc**

**Peter Buckingham, Head of Distribution and Exhibition Fund, UK Film Council**

**Fiona Deans, Director Digital Cinema, Arts Alliance Media**

The Panel Chair, John Howkins, welcomed panellists and invited Fiona Deans to begin the session with an overview of digital cinema developments.

**Fiona Deans, Director Digital Cinema, Arts Alliance Media:** Arts Alliance Digital Cinema is a builder and operator of film related companies. We have four main companies at the moment:- Love Film, which is the largest online DVD subscription company; Cinema Services which develops box office and software rentals; the Metropolitan Film School, a small film school for aspiring filmmakers focusing on digital technologies; and Arts Alliance Digital Cinema, which offers digital logistics and equipment integration service and support.



Fiona Deans

Arts Alliance has been running a trial digital cinema circuit in the UK - this has been focused on technical and operational learning? A large number of companies are now looking into digital alternatives to 35 mm, considering the different types of compression technology and resolutions - but what we really wanted to understand was what the practical implications are for this work. Arts Alliance has shown more than 20 feature films digitally, working with over ten distributors - films range from blockbusters like The Incredibles and The Village, to more cult/minority appeal films like the Director's Cut of Donnie Darko; Bright Young Things; Touching the Void, and The Sorrow and the Pity. All the distributors were very keen to understand how to work with this technology. We ran a digital cinema advertising trial with Carlton Screen Advertising - so for the 6 cinema films we had installed we supplied them their adverts every week in digital. We also provided a number of "alternative content" presentations - which included a live Q&A with M. Night Shyamalan about The Village which was beamed down into three other cinemas across the country, screenings from digibetas, corporate presentations, etc. Arts Alliance has also supplied equipment to film festivals, for example the London Film Festival, the Edinburgh Film Festival, the Cambridge festival, and Cannes. We are also rolling out the Digital Screen Network for the UK Film Council - which Peter Buckingham will tell you about later.

We are also operating the Arts Alliance Film Network, which is a sales and marketing VOD-type network, which enables sales agents, distributors, exhibitors, and film institutes to show and share content online over an IP connection.

So, what is digital cinema? It is the digital distribution and exhibition of film. It is not anything to do with filming using a digital camera - Digital cinema can include films that are sourced on any format (including 35 mm). The emphasis is on the final exhibition of the film - not the way the film is made or post produced, or the digital playout of advertising, live broadcasts, or alternative content (which is generally known as E Cinema).

So, what are the advantages of digital cinema? The main and most obvious advantage is that the prints cost less. At the moment, you can pay from £500 to £1500 for a copy of a print - with digital this is reduced to about £100. The impact of this is that saving on costs, and it's easier to get a return on the investment. The cost saving in turn leads to more flexibility in programming. Another important point is that the international capabilities for digital cinema are huge - for example digital masters can be subtitled for a couple of hundred pounds which saves between £500-£1000 per print - the same applies to a dub track. Therefore, the same master can be used for transferring films between different European countries. The other key advantage for the exhibitors is that it provides new sources of revenues - e.g. they can use the equipment for corporate presentations, sports shows, gaming etc. It's not clear exactly how to make money out of alternative content, but the possibility is there.

Currently there are very few digital cinemas worldwide. China is leading the world at the moment - they are effectively rolling out new cinemas which have only digital technology in them. Belgium - the home of two of the biggest digital cinema manufacturers Barco and EVS - has 10 installations. Obviously there are more digital cinema screens in the US (84) but out of a total 35,000 screens that's not very high.

So, what is stopping the take up of this fantastic technology? Digital cinema technology has been around in a commercial way for about 5 years, but in that time there have been a number of factors that have prevented uptake:- a) Quality - there were questions as to whether the high quality technology projection standard, 2K, would be rendered obsolete by 4K - however, it has now been recognised that 2K really is good enough even though 4K is around the corner;

b) Standards - no one has decided up until recently exactly which compression standard people are going to use, however recently there has been more comfort about the direction things are going; c) Price - prices for equipment started off extremely high at well over £100,000 for an installation - however, price levels are now more acceptable if buying in bulk and with hard negotiation; d) Availability of content from the studios - I think it's fair to say that the studios have been holding back while some of these other issues have been sorted out - however, it does seem that Hollywood is more persuaded, and more content is being made available on digital formats.

But, there is one question that is still outstanding. Who should pay? Distributors or exhibitors? Reduced print costs obviously accrue to the distributors - but, equipment costs would fall to the exhibitors. Therefore, the motivation for exhibitors to buy the equipment doesn't exist. One idea would be for a third party player to pay for the equipment and installation, and then it would take money from distributors in order to use that equipment. This has been tried in the past by companies like Boeing and Technicolor. It hasn't been hugely successful - mainly because some of these other problems weren't sorted out, but also because there are issues about access, control and about funding as well. The industry isn't really that keen on letting someone set up a proprietary network that everyone is tied into over the next 5-10 years.

To conclude, digital cinema has some clear advantages, and many of the barriers are nearly resolved, but the main question is who pays? A third party solution could be the way forward provided that access and control issues are addressed.

Fiona Deans's PowerPoint presentation will be made available at the BSAC website:- [www.bsac.uk.com](http://www.bsac.uk.com)

**Peter Buckingham, Head of Distribution and Exhibition Fund, UK Film Council:**

On a personal level, I have worked as distributor or an exhibitor for twenty years. I am not a teccie - my background is understanding the relationship between production, distribution and exhibition. I work for UK Film Council - most of our work is focused on increasing the range, breadth and diversity of film going in the UK. In 2003, there were approximately 10 million admissions for non-Hollywood or specialised/art house films - this compares to a total 176 million admissions i.e. non-Hollywood films take approximately 5.6% of the market place.



*Peter Buckingham*

There is another killer stat, which perhaps illustrates why both exhibition and distribution are supportive of our objective. The top 10 films in the UK in 2004 took 35-36% of the box office. There were 440 films released in that year. Therefore, there is a strong skew towards tent pole pictures - this is not healthy.

So, how does a public body intervene strategically? Fiona Deans has laid out the advantages of digital i.e. principally the reduced cost of prints. This is especially good news for specialised films, because they are generally at a disadvantage in the 35 mm universe because of the high costs. An average mainstream cinema release will have about 300 prints. Tent poles such as Harry Potter film can reach up to 1,000 prints. Compare this to specialised films, which will be lucky to get 60 prints (as was achieved recently with *The Chorus*). So, the intervention that we are making is to remove the barrier to the market.

So, what are we aiming for with our Digital Screen Network initiative? It's about providing an audience-focused programme, greater access, effective marketing and promotion etc. UKFC have recently entered into a deal with Arts Alliance - and we are now in the process of processing cinema applications for the equipment. We offered cinemas the use of top level digital kit at a heavily discounted price, in return for a programming commitment. We asked them to commit to setting aside a certain amount of time per week for playing specialised film (i.e. non-Hollywood). We have approximately 320 applications, for 230 screens (260 companies have applied). Each company has committed contractually to playing more specialised films than they did in 2003, and to market and promote these shows. Therefore, at the end of this process, there will be a completely different landscape for distribution - and specialised films will have more of a chance of being watched.

Why would distribution supply those cinemas with more specialised content? The big barrier, i.e. the cost of 35 mm print, is gone. It will cost £84 to put a film on a disc put a security key on, and then deliver it to the cinema. Now that the barrier has been removed, all that remains is to connect with the audience. Cinemas will be able to be more flexible with their programming, and respond to audiences. From a distribution standpoint, there is also much more flexibility in terms of marketing campaigns.

How can specialised films get media attention? Currently, the more mass market the media, the less attention specialised films get. A 20-30 print release, 10 of which are in London (which is standard currently), it is unlikely that it will get enough much of a profile in a national newspaper, TV show etc.

UK Film Council has asked each cinema to set aside one slot per month on the same day - I am not quite sure what we will do with this slot yet. This is a way of easily unifying the circuit to give scale. This is how UKFC is intervening in the market place and trying to push up the profile of these kinds of movies in all the opinion making sectors. We have also asked the cinemas to devote one show per day to specialised film for a week - nearly 100% agreed. Therefore, 230 screens will be contractually committed to playing one specialised film per day for a week - this means that for the first time ever, there is a capacity and a possibility of having a nationwide festival for specialised films. This means scale, promotion, and larger audiences for these types of film. That is what UKFC's policy is, and why digital works for us.

**Panel Chair:** What is the timetable for launching the Digital Screen Network?

**Peter Buckingham:** Cinemas will receive their awards in mid May. We expect the first wave of screens to be ready in the third quarter, and it will take approximately 18 months to complete. The final screen will be completed in the first quarter of 2007. The agreement with the contractor and the cinemas are for four years. Therefore, we have four years to achieve our objectives, i.e. to increase the market of this particular sector.

The Panel Chair then opened up the session to questions from the floor.

**Mark Isherwood, Rightscom:** How will UKFC monitor the commitments that the exhibitors have made?

**Peter Buckingham:** We can get reports on anything that plays through digital projectors, and we can also audit.

**Lawrence Safir, Independent Film and Television Alliance:** Is UKFC intending to effectively act as the distributor? Where will the product come from?

**Peter Buckingham:** No, we are not programming at all - this is an extremely light touch initiative. Distributors will own and distribute the content. We will not be involved in programming outside that one slot per month - so the business will continue as before. The only difference is that it is an agreement within a sector about what they will show on average over a period of time. We have built a Rolls Royce digital cinema system which both specialised films and Hollywood will benefit from.

The Panel Chair thanked the panellists for their interesting contributions.

## Erik Lambert, Media Technology Consultant

By way of background, I have been very much linked to the story of the Canal Plus Group, which plays an important role in European cinema. Nowadays, I am working as a consultant for Telecom Italia. For the last two years, I have been discovering the world of the telecoms operator, and the strange relationship they have with content. I will try to explain some of the issues that telecoms operators have been considering in terms of digital media distribution. These are my personal opinions, not the official view of Telecom Italia.



Erik Lambert

What is piracy telling us? Everybody is agreed that piracy is a pest - loss of revenue is a reality for everyone. Telecom operators believe that making them bear the responsibility for piracy in the online world is too much. The equation, 1 download = 1 lost sale, is not true. In fact, one could argue that there is something else happening. If you look at how piracy works, the most dangerous part of the cycle is when pirate releases are first made available, usually before the first cinema release. Looking at how the industry works - essentially, marketing tactics of producers are intended to try to create inelasticity in demand. This is a rational strategy to get people to the movies and maximise box office income. Marketing costs for Hollywood films are rising dramatically - they have now reached close to 40% of the budget of a movie - even for independent movies marketing costs have risen dramatically. Music industry research shows that high levels of marketing lead to higher levels of downloading, but with a limited impact on sales (at least according to some research). So what is happening there? You simply have to look at your business models. Maybe you are at the end of this model whereby you maximise revenues by creating maximum inelasticity at the beginning of release cycle. Essentially, it is "bad" movies that lose the most from piracy at the beginning of the cycle. This is an interesting conclusion.

So, don't expect that even when piracy is reduced, everything get back to how it was before. In the connected world, the "e-word of mouth" also changes everything. Piracy is not only about not buying a copy, its about people talking about it too. Another important shift is that windows for on-demand are moving towards an earlier time frame. The resulting increased availability of films is likely to result in a reduction of the inelasticity of the initial demand. Hopefully, the blockbuster tent pole movies will have to be created in a different way. As a consequence, maybe there'll be more space for other types of movies.

The new motto of telecom operators is "any content, any platform, any time, anywhere". This is also a political objective here in Europe (i.e. the Information Society and the Lisbon Agenda). Traditional film business models are based on micro market segmentation through windows linked to specific distribution formats and technologies. Licensing is linked to the specific medium. This is becoming an issue. The transition from VHS to DVD was easy to understand, but the move from DVD to VOD is different, as the networks are evolving.

Telecom operators are investing in what they call Next Generation Networks (NGN). NGN do not represent specific technologies, but rather a vision and a market concept enabled by different technologies - they are coming up with a range of different telecoms packages, integrating existing technologies (from IP, P2P, fixed, wireless, mobile), and creating new interaction models for users and new business models. The telcos are investing about Euros 35 billion per year in different forms of broadband i.e. creating a new infrastructure which will link up different networks and terminals. This means that any digital content can be delivered to any terminal via any network e.g. WLAN, Multicast Datacast, 3G etc.

Telecom operators are clear that having digital content flowing freely across these new networks raises some issues. The film industry has not quite grasped what these issues are. I call this the "great divide". Telecoms are working within the completely new regulatory environment of the "Telecoms Package". For them, there is a clear separation between content, networks and electronic communication services. "Technological neutrality" is a central concept which is integral to the legislative and regulatory environment for telecoms operations - networks and terminals are becoming fully interoperable. This means that old content strategies are no longer workable.

As "services" represent an ever-growing share of the income, you arrive quite logically at the concept of a "content platform". I believe that this is something that is going to change distribution completely. Content platforms would be technologically neutral, but would cater to specific sales models. The classic windowing system is likely to disappear - staggered releases may still provide an element of differentiation, but it would be difficult to segregate consumers on that basis alone. I was very happy to hear that Sky sees itself as a content platform, independent from the media or the network. There will need to be specialised content platforms as intermediaries, companies that know the business, know how to sell, know how to promote in specific windows etc.

# THE ALL-DIGITAL NEW WORLD - IMPLICATIONS FOR THE FILM INDUSTRY

This means there will be a need for new distribution “know-how” - this is the greatest difficulty. Peter Buckingham spoke about what is happening in digital cinema. This is the same idea - it's about being an intermediary and developing a different kind of know-how. This is something that I believe we will all have to confront in order to be able to make the most of the converging media and communications technologies.

Eric Lambert's PowerPoint presentation will be made available at the BSAC website:- [www.bsac.uk.com](http://www.bsac.uk.com)

**Chair: John Howkins, Deputy  
Chairman, BSAC and Director of  
Equator Group plc**

**Josh Berger, Executive Vice President  
& Managing Director, Warner Bros.  
UK**

**Erik Lambert, Media Technology  
Consultant**

**Costas Daskalakis, Acting Head of Unit,  
MEDIA Plus Programme**

**Marc Samuelson, Managing Director, Samuelson Productions**

**Jonathan Davis, Strategy Advisor, UK Film Council**



*l-r Erik Lambert, Josh Berger  
John Howkins, Costas Daskalakis  
Marc Samuelson, Jonathan Davis*

The Panel Chair introduced the panellists and invited Costas Daskalakis to begin the session.

**Costas Daskalakis, Acting Head of Unit, MEDIA Plus Programme:** Thank you for the opportunity to be here and follow the discussions. I will firstly respond to some of the contributions throughout the day. I agree entirely that this use of new technologies in digital cinema presents a golden opportunity for European film - in terms of getting more specialised films seen by more people. I would also agree that business practices are likely to change - so, producing blockbusters and exploiting them will probably be different in the future. The Media Plus Programme supports the UKFC's digital cinema initiative wholeheartedly. However, I would be more reticent about the third parties, as I believe they may not be accepted as easily as people think. Not everyone will be able to agree to the involvement of certain telecommunications operators for example. One additional difficulty is that content delivery is a moving target - as soon as business models evolve, so do technologies, and then everything changes again. So, we are going after something that will never be stationary.



*Costas Daskalakis*

Therefore, its not easy to say, for example, what will happen at the end of the four year period, because don't know where we'll be by then in terms of quality standards, compression, etc.

The convergence of telecoms and media is upon us. Most of you will have noticed that at the beginning of this year the Media Programme moved from what was the Education and Culture Directorate General to the Information and Society DG - which is now known as Information Society and Media DG. This shows quite clearly that there is every intention that there should be a merging of telecoms and content interests.

The Commissioner has stressed on a number of occasions that it was not a case of one taking over the other, rather, it was a necessity for content to be taken into consideration in discussions on developing communications technologies. The Media Programme has been very preoccupied with the issues raised by the introduction of new technologies in the content sector. As you know, the Media Programme deals primarily with film and cinema - not other media, as its name might suggest. The new programme, which will continue to focus on film, has already been submitted to European Parliament and Council. We hope that, after the discussions on the so-called financial perspectives are concluded, we will be able to start work as soon as possible - with a view to launching the new programme on 1 January 2006.

**Marc Samuelson, Managing Director, Samuelson**

**Productions:** I'm very struck by how little changes. In the first quarter of the last century, my Grandfather started buying some silent movies. He would buy a print and then go round the country, renting halls, and showing that film where he could. That was the way it worked back then. There were lots of other people doing this with more clout, so it was difficult to get hold of good prints - so he decided to be the person who actually imported those new films. This way, he had access to lots of good prints, and started to sell them to other people. Effectively he became a distributor. But then he realised that in fact, the only way he could get really good stuff was to make it himself, and so he became a producer. His decision to become a producer himself was a very elaborate way of trying to connect directly with an audience. I should add at this point that as a producer he ended up with a first look deal with Universal in 1911, and an office on the Loft in the Valley.



Marc Samuelson

He was always complaining about the hideous mark up and overhead that he was being charged on his productions - so really, nothing does change at all! Nevertheless, I believe that we are effectively going to end up doing what my Grandfather did, but in reverse. I think that producers and audiences are going to be able to have a very direct relationship. Having been an exhibitor and a producer, I found it fascinating and terrifying to occasionally be showing my own film in one of our cinemas. If you are separated from that process, as most producers are, you will never experienced quite how appalling it is if you make a film that you are incredibly proud of, and the audience just don't come. It is a shocking and revealing lesson, but one that very few people have.

In the future, I think that many of the current mechanisms for getting a film to its audience will disappear. For example, perhaps 10 years from now, all home watching will have become completely converged - and there will be a number of screens on which will all be able to function in the ways that TVs and computers currently do. Clearly, some version of downloading over the net is going to be the way that people will acquire and watch movies. I can't see how the old rental shop model can compete. If that's case, then what will be the role, if any, for the intermediaries - the middleman between the producers and the audience? I think that perhaps audiences will prefer to go directly to the website of the artist/group, production company etc, and pay to download the content directly. In this scenario, the only function of the intermediary would be marketing. However, if the artist/group/production company was well funded enough, perhaps they would do the marketing themselves. To me, that's really interesting, and a lot follows from it. One or two independent distributors I know are moving into production precisely because they believe that the future for distributors is unclear, and that existing as both a producer/distributor would make more sense. I do wonder whether there is a long-term future for pure distributors. Although distributors currently play a vital role in marketing films for theatrical release (which then triggers the home video market), if all cinemas do go digital very quickly then it seems likely that producers will be able to gain access to cinemas themselves. In effect, producers may be able to communicate directly with the public. That is an entirely new revolutionary model.

There is currently a very live discussion inside the UK Film Council on video on demand, and there has been quite a lot of research in this area. I would like to look at the feasibility of a neutral platform being created for independent distributors or producers to provide one place for the end users to download their movies from. I think that if we want to avoid a monopoly position this latest new medium, then the creation of a platform or some other way of accessing independent content is going to be necessary. That is maybe something that the Film Council could take a lead in.

**Jonathan Davis, Strategy Advisor, UK Film Council:** I would like to talk about why the UK Film Council, other European national film agencies, DCMS and the European Commission embracing the opportunities of this technological revolution that has been explored today.



*Jonathan Davis*

I have seen an evolution over a very short amount of time - I would date it back to April of last year when UKFC were preparing for a Seminar in Cannes on piracy. In his speech, John Woodward said that one way or another we need to get to a "one stop shop", which is perhaps another formulation of the content platform that Erik Lambert has spoken about, and that Marc Samuelson has eluded to - i.e. a destination where the customer goes and finds what they want, when they want, and wherever they want. The discussions about piracy continued the following September in Venice, bringing together many of the same people as well as the telcos and ISPs. Today we have been discussing quite freely the need for the creation of a legal alternative - but as early as April of last year, the idea had not yet been born. Even last January, our discussions on piracy had centred on how such a service might work, rather than the extent to which public bodies might intervene to accelerate the development of legal online services. This is now the focus - and we are now brainstorming to prepare for "Europe day" in Cannes on 17 May, which Commissioner Reding has decided should be dedicated to online film services and new platforms.

In January, the Minister for the Arts, Estelle Morris, said that there had been perhaps too much of an emphasis over the last 10 years on driving broadband take up - and a lack of consideration of the impact it would have on the creative industries or IP. She said that it had been a mistake to drive the development of the knowledge society while neglecting the issue of how to foster a very strong creative industry - and that this was something that needed to be redressed.

Our colleagues at CNC (the French national film agency) have been fretting about how in this new environment they are going to safeguard film financing and film production in France (which is Canal Plus and pay TV). As you may have heard, CNC are going to unveil a convention which has been agreed by French telcos, ISPs, distributors etc. - an exclusive 12 month theatrical window. There will be no VOD for 12 months, which I know the Commission disagrees with. Therefore, not everyone is enthused by this new technology. The French can foresee how these new developments could destabilise their film market completely - a structure that they have built up over 50 years with amazingly astute and sophisticated instruments.

I suppose we are in a very enviable position in the UK in that life is a lot simpler here. We don't have an equivalent of a Canal Plus (in that it provides essential funding for French films), we don't have to worry about broadcasters pouring in investment into film (because our broadcasters are not currently obliged to do this). So, as Mark has already set out, we see this as an opportunity and a means to correct some of the current flaws in the European film industry.

The Panel Chair opened the session to questions from the floor.

**Mark Allen, Pathé:** In international sales, there is a problem with frozen rights - it's difficult to move forward because people are still playing a waiting game to ensure that overlap does not occur. Does the panel think a working group should be established to iron out these technology issues?

**Marc Samuelson:** The background to this question is that currently independent films are sold internationally on a territory-by-territory basis. Currently every contract states that Internet rights in a particular territory are owned by the local distributor but that they can't exploit them until "technology exists" that can prevent overlap into different territories. I'm not sure that such technology ever will exist - in my view we may have to find a totally different model.

**Jonathan Davis:** I think perhaps we are moving inexorably to a compulsory licensing system, as in music, but within the framework of a new type of "content model" that Erik Lambert is referring to.

**Erik Lambert:** I think we should put away the idea of compulsory licensing. Perhaps instead there should be some form of automatic licensing in limited cases - or rather an obligation to limit transaction costs. Although it's interesting to make a comparison between the music business and the film business, the music business is very different because it lives under this general compulsory licensing regime - their revenue levels are lower because of this. The music business tried to use the digital revolution to move to a limited licensing regime, but that didn't work, so now they are searching for something else. I think, for film, it is a question of how to manage and balance the micro markets i.e. different windows, platforms, and territorial markets etc. - how many can you manage without pushing up transaction costs? At what point does this become totally counter productive? That is the issue.

Although currently territoriality does have a *raison d'être*, piracy is likely to force release dates to become aligned anyway. Having territoriality within Europe, which is a single market, is very strange in any case. In the US, no one thinks of having territoriality state by state - Europe should not be any different. But balancing between global regions is crucial - for example, in China, DVDs cost \$2. We'd love it if they cost \$2 in Europe, but we would not be able to finance them if they were sold worldwide at \$2. It's a question of balancing and re-balancing to allow electronic distribution to happen, but also to maintain different legitimate interests. Therefore, pure compulsory licensing would not work in that case.

**Bruce Eisen, Cinema Now:** Mark Samuelson stated that geographical limiting is not working. In fact, Cinema Now and other companies on the net are doing it - I wouldn't say its 100% foolproof, but I don't think anything is.

**Marc Samuelson:** Maybe so, but I am not sure how much pressure the US-based services will be getting from overseas, as they are not yet known outside the US. Once the demand is there, this might be a good test. I do think that the differential of the pricing is going to make a huge difference. For example, if enough people realized that Napster was available for \$14 in the US and £14 in the UK - this would be an interesting test. Internet savvy people are generally very good at finding their ways round things. If people could find a way of downloading movies from a Chinese site at \$2 per movie, that would also be very interesting.

**Panel Chair:** The leakage out of an Internet Protocol-delivered video is far more easily protected than a pay TV broadcasting stream. Sky has had a far larger leakage out of its subscription service than any IP operated downloading video system that I know. It is surprisingly easy to segregate, and stop people with particular IP addresses from getting a product.

**Carolyn Dailey, Time Warner:** I would like to ask Erik Lambert what he meant when he described the US and European film markets as being similar? Obviously there are language differences, and different genres work differently in different countries. Also, I would like clarification from Jonathan Davis on how the Commission sees these new technologies as a way to restructure the European film industry?

**Erik Lambert:** Cultural differences are something to be promoted in Europe, but it does not prevent Europe from being a single market - and that's a difficult exercise. Yes, territories are different in that they speak different languages and have different tastes, but there are more and more commonalities, and more and more operators working across borders.

There is a block exemption from single market rules for many copyright related matters; I think this is something that has to be looked at seriously. I was putting forward the point of view of telecom operators i.e. that there are difficult cross-border issues to resolve relating to the delivery of content.

**Jonathan Davis:** The EC is not intending to restructure the European film industry - rather, the emphasis is on the desire to correct the flaws. So, what are those flaws? Commissioner Reding raised some of these points last week in Luxembourg. She believes that our film market is too fragmented, and that as a result our European products don't travel well. The fragmentation is both between different territories and also down the value chain. In order to correct these flaws we need to have bigger companies that are better resourced, and which have better access to finance and other markets. The UK Film Council is addressing this by awarding money to strong companies, rather than to single projects.

**Panel Chair:** How do the panellists see the film industry developing over the next five years, in terms of the proportion of total revenues that will be derived from the box office, DVDs, Internet downloading and other methods? Which models are likely to dominate e.g. subscription/rental/download-to-own? **Jonathan Davis:** This relies totally on the studios, and how they decide to do their pricing, segmenting and marketing. I think that what everyone will be aiming to do is to drive up the level of spend, and to improve the margins - and also maybe even increase the speed with which they recoup the money. The big problem is going to be how we make sure in this brave new world that creators don't finish up with either the thin end of the wedge.

**Mark Samuelson:** I think it's very difficult to predict, and certainly 5 years is too soon to form any kind of view. I think that we'll quickly get to the point where everything is available to everyone at any time, and it won't matter how the films are grouped and presented because people will find their way to them. Perhaps there will not be much need for companies that group and present films - however, the success of iTunes does seem to demonstrate that at least for the time being there is a place for these types of services.

**Costas Daskalakis:** I would agree that it is difficult to predict. However, I do not think things will have changed that much, and that in 5 years time, most of the income will still come from DVD and video - I would hope that the exhibition sector will not suffer too much.

**Josh Berger:** I would go along with the rest of the panel in their reluctance to predict. However, I think that until there are more radical changes (i.e. to the windowing), the revenue proportions per sector will probably remain about the same. However, I think revenues will improve as a result of the introduction of better measures against piracy. I would also imagine that home entertainment will continue to be the biggest contributor - but the new media technologies and models, if marketed effectively, could grow very quickly and could cut into home entertainment. I think that cinema is also in a pretty safe place - but that will be really down to the producers to continue to produce good movies that people want to see. I think that the TV advertising model is threatened by PVRs, but advertisers will find other ways to spend money on television. Pay TV will also continue - especially in this country because Sky is singularly excellent at it.

**Erik Lambert:** I do not think that it is possible to prepare accurate 5-year business plans. I would hope that that the share of online home entertainment will be superior to the share of second hand DVDs, which do not provide revenues to anyone.

**Panel Chair:** Having asked the question, I should probably answer it myself. My view is that theatrical is likely to decline. I think that revenues from DVDs will continue to increase, but will then decrease as online revenues begin to explode. However, I am probably less certain about this now than I was at the beginning of the conference - as it seems to me that everything hinges on marketing. Although the film industry has been good at marketing certain types of film, it is not as skilled in marketing itself as other industries. In addition, unlike other industries, the film industry does not do consumer research. My first job after leaving university was working for Unilever selling soap. Our soap was the same as Proctor and Gamble's soap - but we spent a lot of money on marketing to persuade the public to buy our soap rather than Proctor and Gamble's. I feel that we are now getting to the point where producers and distributors can use several different delivery systems, but we haven't quite grasped how to market these new services. We have to think harder about marketing messages, branding and customer satisfaction. We have to offer a better product than what is on offer from the pirates - good content, at good prices, and above all marketed effectively.

The Chair thanked the panel and all the conference participants for their fascinating contributions and insights. He also thanked Time Warner for sponsoring the event, and Fiona Clarke-Hackston, Amy Seely and Helen Baehr for putting together such an interesting and useful event.



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