Connected TV: net neutrality hides a more important commercial economic debate

January 2015

David Abecassis and Nico Flores

This article closes our series on connected TV and the associated policy debate. It focuses on the parallels between the net neutrality debate in Internet policy, issues around carriage agreements in the pay-TV market, and implications for the nascent connected-TV space.

The meaning of 'net neutrality' is becoming a matter for debate

Traditionally, net neutrality was seen mainly as a technical issue that has implications for free speech and innovation. In particular, much of the debate and regulatory activity has centred on the 'traffic management' practices of Internet service providers (ISPs). In this context, net neutrality refers to the guarantee that Internet traffic of similar content from different sources will be treated equally. This definition of net neutrality recognises that there are legitimate grounds for traffic management based on objective reasons (for example, all voice-over-IP traffic may be treated the same irrespective of the source, but may be treated differently from email traffic), while seeking to ensure that any content provider can access any Internet user without being discriminated against.

This somewhat 'technological' definition is increasingly being challenged by business reality. In recent months, for example, Internet content providers, such as Netflix, have entered into highly publicised deals in which they pay specific ISPs to provide sufficient interconnection bandwidth to ensure the smooth distribution of video content to end users. Compared to a situation in which bandwidth is unsatisfactory, this is advantageous for ISPs because they receive a payment, but it is also valuable for content providers, because they are better able to deliver a good quality of experience for end users, thus helping stimulate demand and consumption of services. However, not everybody is happy – while everybody agrees that this falls outside the usual definition of net neutrality (because it relates to interconnection capacity rather than traffic management), Netflix and other stakeholders have argued that this is a technicality, because the effect is the same: ISPs have been able to charge content providers in return for ensuring that their customers' quality-of-experience is not degraded.

ISPs have argued that these payments are only fair in view of the need to invest in network capacity to carry the traffic in question. However, some parties, including Netflix, have argued that ultimately these deals reflect ISPs' ability to levy a "toll" for access to their customers, which may be significant and independent of any costs. They claim that ISPs have a privileged 'gatekeeper' relationship with consumers, and should be prevented from monetising this relationship by charging content providers. Instead, they argue, ISPs should use the revenue they receive from consumers to ensure that the necessary network capacity is in place. This line of argument appears to suggest that net neutrality should extend to the commercial relationships between content providers and ISPs, and not just neutral treatment of traffic, specifically by banning ISPs from charging content providers, at least in some cases.

Carriage in linear TV is not 'neutral' – but it is highly regulated

It is interesting to draw parallels between 'net neutrality' in the Internet context, and content and network relationships in the context of linear TV services.

Over the years, content providers and broadcasters have embraced multiple TV distribution platforms (terrestrial, satellite, cable, IPTV) to reach potential consumers with their linear TV offers. Commercial linear TV distribution agreements encompass a very wide variety of models, most of which are in no way 'neutral' – absent regulation aside, they generally involve a balance between the value that platform operators place on having specific TV content on their platform, the value that broadcasters place on being able to reach the platform's subscribers, and the costs associated with the infrastructure required (for example, network bandwidth, electronic programme guide (EPG) software, etc).

Carriage fees (paid by content providers to network operators) or retransmission fees (paid by pay-TV operators to content providers) often are not only a matter of market forces – they are also influenced by 'must carry' and 'must offer' obligations, as well as other laws and regulation that determine or influence what either side can charge the other. In many cases, this combination of market value and regulation has led to 'settlement-free' carriage, but in recent years there has been pressure to increase retransmission fees paid by pay-TV operators to broadcasters on both sides of the Atlantic (in the USA and selected European countries) as well as to eliminate the regulated 'technical platform' charges that broadcasters pay platform operators (for example, in Germany and the UK).

Net neutrality and traditional TV carriage models are relevant to connected TV

Similar situations and debates are beginning to arise in multiple areas of the connected-TV value chain, where many new deals are being struck to support the fast pace of innovation in connected TV.

For regulators and policymakers, this raises some important questions relating to economic models, the impact on consumers, and policy objectives. For example, if connected-TV platforms can charge content providers unlimited fees in return for including their 'apps' in their devices, this might affect content providers' margins – for content providers that have a duty to commission and pre-finance audio-visual content (for example, the public service broadcasters in the EU), this might translate into reduced funding for producing original content. Conversely, if content providers can charge platforms, this may reduce innovation incentives for the latter. Consumers may also be affected – if commercial disagreements lead to key content being unavailable on some platforms, consumer choice (and, potentially, media plurality) is reduced. If 'blackouts' result from disagreements about content (rather than commercial factors), then this would raise concerns about freedom of expression.

These issues call for careful study by regulators and policy makers, to ensure that the objectives of audio-visual policy remain achievable in a converged environment. (In the EU, these objectives include: sustainable investment in, and pre-financing of, original content; supporting cultural and linguistic policies; and protecting vulnerable people from harmful content.)

The traditionally separate policy debates are becoming increasingly interlinked

Several policy issues cut across these three contexts (Internet access, pay TV and connected TV), including content producers' access to consumers; consumers' access to content; content prominence; media plurality; the bargaining power of platforms compared with content providers; and investment in content, networks and platform innovation. These issues touch on the traditionally separate policy areas of Internet, telecoms, media policy and industrial policy, and involve questions of economics, technology and culture. And increasingly, they are all interlinked.

Analysys Mason has worked with governments and regulators as well as industry players and investors involved in offering media services, to help them understand these issues and develop their responses. Please contact David Abecassis or Nico Flores if you would like to know more.
