

SOCIETY ARTISJUS HUNGARIAN BUREAU FOR THE PROTECTION OF AUTHORS'

RIGHTS

BUSINESS REPORT

ON THE YEAR ENDING ON 31 DECEMBER 2014

(all balances are indicated in thousand HUF unless otherwise specified)

1. The operational environment of Artisjus in 2014

1.1 Legal environment

As a result of the amendment of Act No. LXXVI of 1999 on Authors' Rights as of the end of 2013, the Society paid 25% of all blank carrier fees collected by Artisjus (for all groups of copyright owners concerned) to the National Cultural Fund of Hungary in 2014.

Several point of the Act on Authors' Rights were amended in the course of 2014, so for example, the relation between the Act on Authors' Rights and the Civil Code was settled in a more detailed manner, and the use of works related to the activities of the Parliament was reclassified as named use of works in public domain. Furthermore, the rules of orphan works in public domain were transformed by the legislator in accordance with the relevant EU directive. Out of the above, only the introduction of the free use of orphan works was preceded by social consultations with the participation of Artisjus. (The legislative strategic partnership agreement between Artisjus and the Minister of Justice expired at the end of the previous government term and it has not been renewed by the current government.)

Similarly to all Hungarian legal entities, our Society is equally concerned by the new Civil Code having entered into force in March 2014. Accordingly, we aligned the rules of contract violation of the tariff charts (limitation, late payment, flat rate costs of recovery) as well as the Society's Constitution and the foundation acts and regulations of the Artisjus foundations with the new Civil Code.

Within the regional regulatory environment, the most important event was the approval of EU directive 2014/26/EU on the collective administration of rights in February 2014. The implementation of the directive regulating meticulously the operation of European collective management organizations will have to be completed by the legislators of the member countries by the spring of 2016. Based on the information available at the time of the preparation of this report, the Hungarian legislator is planning to take out the rules of collective rights management from the Act on Authors' Rights in the framework of the implementation of the above directive, and regulate them in a separate act on the collective management of rights. The draft laws necessary for that are expected to be submitted to the Parliament in the autumn of 2015.

The broader operational environment of Artisjus, increasingly affecting its daily operation, is constituted by the case law of the Court of Justice of the European Union (CJEU) pertaining to authors' rights. Among the decisions made in 2014 stands out the OSA case in which the CJEU declares that the legal monopoly of collective rights management prescribed by the national law (i.e. a law according to which there can be only one CMO for a given right of a given group of right owners) does not violate any EU legislation. (Reaching a contrary conclusion earlier, the Hungarian legislator terminated the legal monopoly of Hungarian CMOs.)

In the Amazon case, the CJEU acknowledged and confirmed the system of blank carrier fees also applied in Hungary.

1.2 Evolution of our relations with authorities

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The usual comprehensive supervisory audit was carried out in 2014 as well by our supervising authority, the Hungarian Intellectual Property Office (HIPO), which examined the operation of the Society with respect to its compliance with the rules on authors' rights.

This year, the annual supervisory procedure concluded with one notice: this notice — similarly to the case of several other Hungarian collective rights management societies — pertained to the way in which the Society wished to exercise the lending right and the renting right for sound recordings (not applied in the Hungarian practice) in harmony with its registration. The Society will have to decide about compliance with the notice in the first semester of 2015; we have been consulting with the supervisory body regarding the possibilities of interpretation.

It is a significant change in the supervisory criteria — having entered into effect without legislative changes — that with the help of external advisors, HIPO set up a system of requirements in 2014 with respect to unified surveillance reports and the content of the accounting policy of collective management organizations. The implementation of the new surveillance report structure requires several months of work in the legal, financial and IT domains of Artisjus, stretching into 2015 as well, including the transformation of the underlying accounting working methods. Contrary to the annual report prescribed by the accounting acts, the surveillance report will have to be submitted by the Society every six months instead of every year.

CloudCasting Ltd., again, initiated a surveillance procedure against Artisjus at HIPO in 2014, this time concerning certain details of Artisjus's activities with respect to the collection of rights of public performance. Simultaneously, it also made a complaint about Artisjus at the Hungarian Competition Authority. Artisjus was contacted by both authorities, and based upon our detailed reply, they decided to launch neither a collective rights management surveillance, nor a competition procedure, respectively, against Artisjus.

The work aimed at the preparation of reference royalty notices started as early as in February 2014, and the tariff charts were submitted by the deadline of 1 September. Following the procedure conducted by HIPO, the tariff charts were approved by the Minister of Public Administration and Justice, and they were all published in the Official Journal by 1 January 2015.

2. Royalty income and administrative costs in 2014

In the year 2014, the total amount of royalties collected by Artisjus was 18,984,466 thousand HUF.

thousand HUF

	2013	2014	%
Public performance royalties	5,010,252	5,262,294	105.0
Revenue from broadcasting and cable television	3,580,366	3,953,133	110.4
<i>from which cable television revenue</i>	<i>1,398,182</i>	<i>1,498,046</i>	<i>107.1</i>
Royalties on blank carriers	5,942,217	8,866,778	149.2
Royalties on mechanical and canned music	172,452	194,272	112.7
Online	132,628	223,641	168.6
Royalties on reprography	7,767	6,156	79.3
Royalties on foreign broadcasting organizations	211,569	157,096	74.3
Royalties from abroad	270,218	321,096	118.8

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Total:	15,327,469	18,984,466	123.9
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Within that, the royalties collected on behalf of right holders represented by Artisjus amounted to 11,967,180 thousand HUF, whereas the sum collected on behalf of Hungarian collective management organizations representing other right holders and of foreign television channels represented by Artisjus was 7,017,286 thousand HUF.

	2013	%	2014	%
Those represented by Artisjus	10,058,142	65.62	11,967,180	63.04
Those represented by HUNGART, FILMJUS, EJI and MAHASZ	5,057,758	33.00	6,860,190	36.13
Foreign broadcasting organizations	211,569	1.38	157,096	0.83
Total	15,327,469	100.00	18,984,466	100.00

Based on the above, it can be stated that Artisjus successfully achieved its governing Financial Plan for the year 2014.

2.1 Live and canned music public performance market

The domain of musical public performance concluded the financial year with a sum of 105 per cent compared to the revenues of the year 2013.

This growth is relative: it should be appreciated partly in light of the revenues somewhat inferior to 100 per cent of the reference level, which occurred a couple of times over the last five-year period, and partly in the context of slight deflation. However, as a definitely positive development, we managed to increase our revenue, bringing it quite close to the historic peak revenue of the year 2008, the last year before the economic crisis. According to our analyses, the underlying reasons of this growth were not related to a single distinguished area of exploitation, but to litigation recovery, outstandingly successful in 2014, as well as to payment discipline having somewhat increased as a result of that.

Besides canned music royalties collection, in 2014, we put a great emphasis on locating live music events, thus in the course of the year, we collected rights at more events than ever before. In relation to that, we also managed to execute the most broadcasting ever collected over the year.

Despite this relatively good result, Artisjus identified important structural problems in the course of the year 2014 based on market information gathered within its own network as well as on analyses ordered from external economic experts both in the area of catering industry and commercial music exploitation. For the sake of achieving a balanced growth in the long run, Artisjus elaborated two solutions on the basis of these analyses in 2014:

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- from 2015, it reduced royalties pertaining to the catering industry in a differentiated manner, by 19-20 per cent on average (the method and distribution of differentiation were determined on the basis of the market analyses performed);
- as for the commercial sector, it experimentally introduced a package of significant discounts that users may subscribe to through professional background music providers having signed a framework agreement with Artisjus.

The effects of these two packages of measures effectively in force since the beginning of 2015, possibly leading to a temporary dip in revenues, can be first appreciated in retrospect after 3-4 quarters. Thus, also due to the deadlines of the current tariff chart approval procedure, it is in the planning phase of the tariff charts for 2017 (i.e. in the first semester of 2016) that the Society will be in the position to react to them in any way (confirmation, correction, etc.). The outcome of these measures will be most likely distorted by the special tax affecting the commercial sector as well as the effect, not yet measurable, of the closing of shops on Sunday, which has been recently introduced. Due to the increased cost level owing to the government's actions and the difficulty of foreseeing market prospects, at the end of 2014, several significant foreign-owned commercial chains decided to suspend temporarily their use of background music for sales purposes. Others terminated their activities and left the country, causing a major immediate revenue loss to Artisjus.

Besides the correction of tariff charts and the preservation of the positive elements of the traditions of royalty collection, the Society wishes to intensify the flow of revenues from this domain in the future with the help of a fresh attitude, trendy sales and marketing tools and methods founded on the effect of music creating economic value, and using a differentiated communication within that milieu as well, based on the segmentation of individual user groups. The finalization and the beginning of the implementation of the internal strategy taking into consideration the methods of the relevant leading foreign CMOs as well as expert advisors' guidance seem to be feasible in 2015; its impact will most likely be effectively measurable in the medium run (2-5 years).

2.2 Broadcasting and cable television market

In 2014, the sum of royalties collected from radios, television broadcasting and cable televisions attained 110.4 per cent of the 2013 reference level. This can be mainly put down to the fact that — unlike in the previous years — all of our major partners honoured their royalty payment obligation for the given year by the deadline in the course of the year.

Towards the end of the year, the atmosphere of the *television market* was marked by the announcement of the advertisement tax. The actual impact of the latter on the revenues of Artisjus can be measured from 2015. We are still striving for signing long-term and well-balanced agreements with our biggest partners even in such modified conditions.

The royalties paid by *radio broadcasters* are still affected by the "gap" caused by the disappearance of the broadcaster of Neo Fm (earlier Sláger Radio) from the market. The second national frequency had not been distributed by the Hungarian State into commercial concession; the programme of Kossuth Radio is broadcast here as well, thus it does not produce any specific revenue of royalties.

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According to the figures of the National Media and Infocommunications Authority, there was a minor (0.3 per cent) increase on the market of *cable services* in 2014. In this area, two problems arose despite the currently well-balanced royalty collection.

- On the one hand, major objections emerged repeatedly concerning the quality and usability of the aggregated data provision constituting the basis of the royalty discount, a service supplied by the bigger cable association.
- On the other hand, with respect to the tariff charts planned for 2015 in the course of 2014, contrary to their preliminary indication in the spring, the advocacy groups of the cable service providers proposed to switch to the revenue-based royalty collection method.

In the latter topic, Artisjus — with the help of a study prepared by an external economic expert — has, so far, argued successfully for upholding the present tariff chart structure (monthly flat rate fee by household and by channel).

2.3 Blank carrier market

In the year 2014, the blank carrier revenues increased by 49.2 per cent compared to the reference value of 2013. The crucial event of this domain was the extension of the blank carrier royalties claim to tablet PCs. Part of the market expected to see a significant decline in the legitimate sales of tablets as a result of this measure by Artisjus. Contrary to that, we registered nearly 50 per cent more such appliances compared to the turnover forecast by expert estimates. In 2014, the fast consolidation of the market was noticeable: just like in the case of many other devices earlier, thanks to the identifiers (stickers, IMEI number) allowing for the identification of royalty claim and payment, the turnover of the black market dipped and the market became "whiter".

Moreover, the market of mobile phones also saw a dynamic expansion in spite of the unfavourable economic environment.

2.4 The (offline mechanical) market of the collection of rights on sound recordings

Royalties on traditional sound recordings produced a more than 10 per cent increase compared to the reference value of 2013, while the number of copies registered by Artisjus grew by 17 per cent. This result can be put down, on the one hand, to the successful termination of a litigation spanning several years, and on the other, to the growth in the number of special extension carriers. According to our expectations and hopes, the royalties of the domestic market of the publication of sound recordings can stabilize around the amount of 200 million HUF per year; there seems to be no realistic source for any kind of possible growth in this realm.

The application of the BIEM-IFPI standard contract renewed in 2013 was incorporated into the practice of Artisjus.

2.5 Online music market

In 2014, for the first time in the history of Artisjus, revenues from online sources exceeded the royalties received from the sales of physical sound recordings, and they amounted to 168.6 per cent of the 2013 reference level. The market, which is becoming increasingly concentrated, continues to be dominated by international service providers, while Hungarian companies are mostly present in the video-on-

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demand (VOD) market. Due to the quickly changing business models and repertoire withdrawals, the invoicing of royalties can only be generated through a longer development process in the case of streaming services demanding a high-standard preliminary (!) administration, whereas an average play generates as few as 0.20-0.24 HUF (!) of royalties, and according to our data, only about 25-30 per cent of plays are, in fact, works represented and registered by Artisjus. It is the strategic aim of Artisjus to profit from the tools developed in the Armonia cooperation established with our membership in this domain, which are expected to become ready for use in 2015.

2.6 Administrative costs

In the year 2014, the administrative costs deducted by Artisjus effectively for its operation (i.e. excluding the obligatory payment of healthcare contribution after copyright) amounted to 17.32 per cent, that is, they remained at the usual rate.

	<u>2013</u>	<u>2014</u>
Net sales revenue:	16,157,443	18,832,448
Administrative costs of the distribution of royalties carried over to the year following the year concerned	-	*1,012,473
Standard administrative costs for the year concerned	2,560,071	3,175,547
Administrative costs of the distribution of royalties collected in the year prior to the year concerned	829,974	860,456
Total administrative costs	3,390,045	4,036,003
Adjusted net sales revenue	15,327,469	18,984,465
Authors' healthcare contribution	716,915	748,380
Operational administrative costs	2,673,130	3,287,623
Total administrative costs in proportion to net sales revenue	20.98%	21.43%
Operational administrative costs in proportion to corrected sales revenue	17.44%	17.32%

* In the previous years, this sum was included in the net sales revenue.

3. Relations with members and right holders, communication

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The society membership of Artisjus continued to grow in 2014: the Society had 1,994 members on 31 December 2014. At the same time, the number of non-society members entrusting Artisjus with the collective administration of their rights was 12,536.

Our two flagships for the authors are the Authors' Customer Service (ACS) and the Authors' Information System (AIS). Both of them proceeded according to their usual orientation; only minor developments, changes and trainings were necessary in 2014.

Regarding the "Dal+Szerző" (Song+Composer) blog, the most significant change of the year 2014 — besides the new, more professional and more user-friendly design — is that a music journalist entrusted with this specific task was nominated as the blog's editor-in-chief, so besides Artisjus's own contents, topical musical industry related contents are also continuously made available on the site, which fill a gap in Hungarian in certain cases.

In 2014, we launched our Twitter channel; for the moment, only as a sounding board for the blog entries.

The programme series entitled "Interactive Musical Alarm" (IZÉ), which replaced Artisjus Authors' Academy from 2013, continued last year as well. Moreover, from May, it was organized as a major event in Akvárium Klub featuring the following topics:

- January: Musical sponsorship
- February: Royalties and other revenues
- March: Radio airplay
- April: Music export
- May: Composing with producers
- June: Music trends & YouTube (VOLT "jubilee" special edition)
- September: Festival crisis communication, Fluor and the social media
- October: Mary Popkids — empowerment, new clips
- December: Cseh Tamás Programme, Music in the stores

The dialogues were then completed, giving birth to our publication entitled "IZÉ — Artisjus Zeneipari Kézikönyv" (Artisjus Handbook on Music Industry).

Following the traditions of the past 5 years, Artisjus attended the biggest music industry event of Hungary, Budapest Music Expo (earlier called "Hangfoglalás") in 2014 as well. The Artisjus booth attracted more visitors than ever: our colleagues offered a continuous customer service for authors during the entire event. What is more, on each of the three days, we also invited the administrators of EJI and MAHASZ to visit our booth for one hour so that musicians could take care of all their copyright issues at the same place. Besides that, the colleagues of the Authors' Customer Service gave professional presentations about the rights management work performed by Artisjus, and guest speakers were also invited on behalf of the National Cultural Fund.

In 2014, our Society launched a new publication series entitled "Artisjus füzetek" (Artisjus Booklets). In these thematic information booklets, we answer those questions that authors address to our Society on a daily basis. We systematized all those pieces of information in a concise and clear manner that all music creators will encounter sooner or later in their career. The booklets made their debut at the Budapest Music Expo and were met with great enthusiasm.

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The following parts of the series published in 2014 (as well as more recent ones) are available at the Artisjus Authors' Customer Service and on the "Dal+Szerző" blog:

- 1) Facts about Artisjus
- 2) The first steps at Artisjus
- 3) Musical arrangements
- 4) Authors' Information System (AIS)

Press communication is also one of our priority areas. It is probably here that the positive effect of our persistent and continuous efforts over the years can be felt the most: last year did not only feel to be the most productive one, but it produced the most positive balance so far in this realm in terms of figures as well. Today press communication is no longer mainly about repelling various attacks and misunderstandings, but about conveying our own important messages according to a planned schedule.

We reinforced our presence in the ProArt communication; last year, for the first time, we became the co-organizers (in cooperation with EJI and MAHASZ) of the second edition of the Music Hungary conference considered to be the biggest professional conference of the Hungarian music industry.

In 2014, we sent altogether 35 authors' newsletters to the authors of Artisjus, which meant a total of 10,929 addressees at the end of the year.

4. Distribution and documentation

The distribution of royalties collected in 2013 was carried out according to the previously indicated deadlines and the royalties were paid accordingly. The year 2014 was the first time that as a new distribution type, canned music ("individually distributed canned music") royalties were distributed for specific music plays logged on the spot by an electronic device. Also, it was the first year that as a result of a litigation successfully won in 2013, the complex task of the ad-hoc distribution of blank carrier fees paid retroactively for the financial years of 2007-2010 was executed.

The amendments of the Distribution Regulation are presented to the General Assembly by the Executive Board. The work of the Executive Board was enhanced actively by the Distribution Working Group in 2014 as well.

Changes in the Distribution Regulation in 2014:

- minor modifications were made related to financial and accounting requirements and pertaining to the correction of the wording of the text;
- regarding broadcasting royalties, the weighted coefficients by rate will be applied above a total time of 40,000 seconds instead of the previous total time of 31,500 seconds in the case of specific music plays;
- the Society approved a Royalty Prepayment Regulation as an appendix to the Distribution Regulation about the conditions regarding advance payments on royalties;
- the Society created a possibility in the Distribution Regulation for the ad-hoc distribution of blank carrier fees collected retroactively;
- the criterion was introduced that no work announcement is valid without the submission of a copy of the work;

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- the royalties on the sound recording of a piece transcribed without authorization will have to be distributed by the original author (abolishment of the former 6-month "grace period" following the registration of the publication for obtaining the authorization);
- the procedural rules of legal disputes related to the author's dividend and music publisher's dividend were clarified;
- concert distribution: the Regulation put off the distribution deadline of the communication of the programme presented from the end of the year to 31 January of the next year;
- the degression key of radio and television signal airplays was reduced from 1/8 to 1/6;
- the distribution of royalties of webcasting and on-demand was clarified;
- the time intervals of point-based distribution types were modified.

5. Social and cultural activities

In harmony with the governing legal frameworks from 2012, Artisjus is only entitled to provide allowances (through its foundations: Artisjus Music Foundation and Artisjus Literary Foundation) as a supplement to pension or as a social benefit for persons in need. The amounts deducted for cultural purposes were transferred by Artisjus to the National Cultural Fund in 2014 as well.

6. International environment

Artisjus continues to take part in the work of the global confederation of rights management organizations (CISAC) and the European regional organization (GESAC) as a member of the board of both bodies. The representatives of our individual professional fields participate actively in the international professional information exchange of collective management organizations. In 2014 again, Artisjus hosted the international seminars and trainings organized by the European regional directorate of CISAC/BIEM. Furthermore, it was also the venue of celebration for the 10th anniversary of the regional office.

7. Miscellaneous issues

The Society pursues no research and development.

The Society has a single business location (1016 Budapest, Mészáros utca 15-17.). Moreover, it has local offices in the following towns:

- Debrecen
- Győr
- Miskolc
- Pécs
- Szeged
- Zalaegerszeg

On 31 December 2014, the Society had 156 full-time employees of which 141 persons had an open-ended contract and 15 a fixed-term contract.

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The Society has projected a net royalty income of 12,139,370 thousand HUF (without VAT and standard administrative costs) for the year 2015.

16 April 2015, Budapest



Dr. András Szinger
Director General