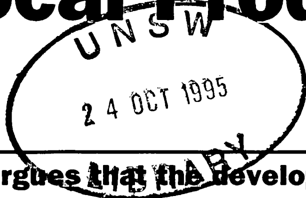
Local Production Opportunities in Pay-TV


UNSW 24 OCT 1995 LIBRARY

Jack Ford argues that the development of Australian drama for Pay TV may be stifled unless the approach taken in the ABA's Guidelines is abandoned and a more far-thinking approach adopted.

One of the objects of the Broadcasting Services Act is to promote the role of broadcasting services in developing and reflecting a sense of Australian identity, character and cultural diversity. Legislative expression for this object can be found in Section 102 of the BSA, which states:

'Each subscription television broadcasting licence is subject to the condition that, if the licensee provides a service devoted predominantly to drama programs, the licensee will, for each year of operation, ensure that at least 10% of the licensee's program expenditure for that year in relation to that service is spent on new Australian drama programs'.

A number of critical documents and pronouncements over the past 12 months have dealt with, directly or indirectly, this quota concept, both in the context of Pay TV and multi-media.

First, there was the interim report of the Broadband Services Expert Group (July 1994) which emphasised the importance of the opportunity we face in building a significant content creation industry in multi-media.

There followed the well publicised $45 million announced in Creative Nation (October 1994):

'.... for the establishment of the Australian Multi-media Enterprise to provide financing for the development and commercialisation of interactive multi-media products and services. An enterprise of this size will provide a spur to the industry at this early but critical stage of its development. It will, of course, tap only a small part of the sector's enormous potential.

The enterprise will ensure the production of Australian content by accelerating the production of high quality interactive multi-media products and services .... It will provide a platform for small Australian multi-media companies to gain a worldwide reputation as producers of innovative and high quality multi-media products and services'.

Finally, the final report (December 1994) of the BSEG referred specifically to the importance of ensuring a high level of Australian content on the networks of the future. It went on to recommend (in similar terms to section 102) that 'providers of broadband entertainment and information services be obliged to commit at least 10 per cent of their expenditure on content to new Australian content. The obligation should be reviewed by the year 2000'.

Sony has always invested in the communities in which it operates. As a total entertainment company, Sony's strategy involves program supply, equity investment in appropriate cases as well as hardware supply. All of our worldwide operations have been completely localised - from senior management to the numerous manufacturing facilities around the world that employ more than 130,000 people (Michael Schulhof, President & CEO, Sony Corporation of America, 'Staying on the Cutting Edge of the Entertainment - Electronics Industry', a speech to the Claremont Graduate School, Peter F Drucker Management Center, March 11 1995).

In Australia, Columbia TriStar is, together with Australis, TCI, Universal and Paramount (and hopefully Fox shortly) an equity partner in as well as a licensor to the two movie channels (SHOWTIME and ENCORE) being shown on the Galaxy package. Columbia is also an equity partner (and licensor), with Universal, Paramount and Australis, in another Galaxy channel, TV1, a general entertainment channel. All 3 channels, as broadcast by Galaxy, would appear to fall within the condition imposed by section 102.

Showtime, Galaxy and TV1 all recognise that their channels need to form their own identities and that this will not be achieved without a commitment to new Australian content. This commitment has got nothing to do with complying with quotas; it is commercial reality. The world is fast approaching the day when US domestic and international film revenue will be split 50/50. As music companies have done successfully for years, movie companies must continue to increase their investments in local production and talent on projects outside the US (ibid Mr Schulhof).

I am pleased to be able to inform you, in the case of TV1, of one new albeit small Australian content initiative which has just taken place. This really is new television for Australian viewers. Significantly, the opportunity is three-fold, for talent, TV1 and the venues. It is but a small example of significant opportunities which will emerge for local content on Pay TV.

To some extent these sorts of initiatives have been forced by the ban on advertising on Pay TV until July 1997. TV1 shows a number of series. Most come in the form of 23 or 46 minutes episodes. Accordingly, there is a fair amount of interstitial material required to fill in the gaps which would normally be taken by advertising.

At the same time, of course, remaining a major player in the programming software industry involves innovation, creativity, considerable expenditure and obvious risk. The major US studios each spend around U$1 billion each year on a new product. Not all of this translates into box office blockbusters.

In Australia, Pay TV is still embryonic. It will take time for local content initiatives to develop and mature.

One could be forgiven in connection with the new Australian content condition for thinking that the body responsible for implementing and monitoring it, the ABA, would be going out of its way to encourage innovation, creativity and some risk-taking so as to ensure that the potential to exploit local production opportunities will be maximised. Unfortunately, quite the reverse has happened to date with the ABA taking a position which in my view threatens significantly to stifle opportunities in Pay TV for new local production.

In May 1994 the ABA published its 'Guidelines for the Implementation of the Pay TV new Australian drama license condition'. Lest there by any doubt about the seriousness with which the ABA views these guidelines, they come up front with the warning that failure to comply with the condition can lead to penalties of up to $2 million or even suspension or cancellation of a licence.

Where then are the guidelines deficient?

First, there appears the following statement:

'As the licence condition relates to a service devoted predominantly to drama programs (ABA emphasis), only the cost of rights to programs actually broadcast by the service (my emphasis) will count toward the condition'.

In other words, no credit will be allowed for research and development. With respect, this in my view is an indefensible position taken by the ABA. How are you going to get creative and historically risky expenditure on new Australian drama in a new medium if there is no credit available for R&D? Both Creative Nation and the BSEG final report recognised the importance not only of R&D itself but also of encouraging it. The BSEG report stated that:

'R&D is extremely important in bringing new products to market, and is also essential in developing the skills and knowledge needed by our organisations if they are to introduce and adapt foreign technologies and products intelligently. Further, Australia's strengths in R&D provide important pointers to areas of opportunity'.

Creative Nation was in the following terms:

'The creation of multi-media product from an initial concept is difficult and risky. For every successful multi-media title, probably another 2 to 3 never make it out of the prototype stage and another 2 fail to bring in appropriate returns at market. A combination of good title selection, sound management, effective marketing and distribution and access to suitable finance is required. This can be especially difficult for enterprises starting out'.

Finally on this aspect, there is a curious but in my view inexplicable nexus drawn by the ABA between its no R&D credit position and the drama service concept. This seems to contemplate that R&D would be available for non-drama channels but not for drama channels.

Secondly, the ABA has introduced the concept of 'residual value' which is defined to mean the difference between the price paid for program rights and the price of the rights on-sold. What the ABA says is that where Pay TV rights acquired by a licensee are sold to somebody else, only the residual value should be included in program expenditure. What this means is that if a licensee actually succeeds in producing so good an Australian program that it is on-sold in another territory or medium, such that for example the effective price paid for the program is recouped in full, the licensee would be given no credit for that particular program and, even worse, if the entire 10 per cent had in that case been spent on a single product which became a blockbuster, the licensee would, under the ABA's Guidelines, risk losing its licence.

The third difficulty arises from the ABA's treatment of what it calls 'jointly acquired program rights'. What the ABA says is that if program rights are acquired in a bundle with, say, an intention to broadcast some but not others, there is potential to realise significant savings over purchasing rights individually and therefore the value of the Pay TV rights should be reduced in proportion to the saving achieved for the joint rights. With respect, that proposition simply ignores commercial reality. Programs are typically bought and sold in packages, which can include a mix of programs in terms of their broadcast quality. No one in the industry, however, would dispute that prices paid for such packages are other than genuine market prices. Why should licensees be artificially penalised by being forced in effect to reduce those prices below their market value? In any event, if this part of the guidelines was to be enforced, who is to say in some definitive manner what the discounted figure should be? Presumably this would necessitate some sort of independent expert, thereby leading to, in my view, unnecessary expense and administrative burdens.

The fourth difficulty is really the result of the first 3. In my view, the Guidelines are so deficient that if the ABA made a decision or purported to take some action in relation to a licensee in reliance on the Guidelines, the decision or action would readily be set aside by the Federal Court.

Might I offer the following solution, conscious that the Guidelines state the ABA's expectation that 'there will be a need for further consultation about the implementation of the new Australian drama condition as the industry develops'. My solution involves a 7 point plan as follows:

1. Abandon the present guidelines completely. They are unworkable and, if implemented in their present form, will stifle local content opportunities.

2. Full credit must be allowed for R&D. Recognise that expenditure will be incurred on products which won't get past the drawing board, let alone onto a screen. Do not insist that a program must be broadcast to obtain a credit.

3. Encourage innovation and creativity through the production of quality programs. If programs are on-sold so that expenditure is recouped or profits are made, don't penalise licensees.

4. Leave market forces to determine what value is to be ascribed to the program purchase rights. Don't create artificial prices and discounts.

5. Pay TV in Australia will be characterised in its early years by expenditure substantially exceeding revenue. Sections 102 and 215 were enacted in October 1992. Section 215 requires the Minister to review before July 1997 the operation of the Australian drama Pay TV condition, with the possibility of increasing it to 20 per cent. The difficulty is that it is now mid-1995 and Pay TV is only just kicking off and subscriber numbers are small. The present review, even if it takes place near its sunset, will happen after only a very short period of full scale Pay TV operations. First, there is a real question in my view whether or not a review at that time could honestly achieve very much because the industry will be still very much in its infancy. Secondly, because of that fact, raising quotas at the time would undoubtedly have significant adverse effects on licensees. At the very least, the review date should be extended.

6. The 150 percent tax concession for R&D should be extended to expenditure on new Australian drama. The BSEG group's final report supports such an extension in the context of multi-media (page 81). There is no reason in my view why this concession should not be extended to Pay TV operators, particularly in the early years.

7. Likewise, again following a recommendation of the BSEG group (page 84), withholding tax on royalties should be eliminated.

In conclusion, success for Pay TV in Australia means success for Australia and Australians. New substantial companies like Australis are creating lots of new jobs and companies like Australis and Sony are investing lots of capital as well. The 3 new channels I mentioned earlier will also create job opportunities. I've already said that movie companies must increase their investments in local production and that involves creative and innovative thinking. Let's have our regulators thinking likewise.

Jack Ford, Vice President & Managing Director, Columbia TriStar International Television, A Sony Pictures Entertainment Company

The article is an edited version of a paper presented to the Cable & Satellite Television Conference in Sydney in May 1995.