Submission by Free TV Australia

Department of Communications

SBS Advertising Flexibility - Regulation Impact Statement

10 March 2015

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EXECUTIVE SUMMARY

- Free TV Australia is strongly opposed to any moves to allow the SBS to increase its advertising (either generally, or in prime time) or to incorporate product placement in its programming.
- Commercial broadcasters should not be required to subsidise funding cuts to a government-funded broadcaster. Free TV members pay extremely high licence fees on top of Australian corporate taxes. Unlike SBS they are also subject to increasingly onerous Australian content obligations.
- At the same time the sector is facing unprecedented competition for advertising dollars, structural change and a challenging advertising market. All commercial broadcasters have undertaken rigorous cost out programs in recent years to address these market factors and SBS should not be immune from those pressures.
- Despite the material impact on the Australian television advertising market, there has been no consultation with affected parties and SBS's analysis of its revenue projections has not been released for scrutiny.
- Any new revenues derived by the SBS will come at the expense of commercial broadcasters because the free-to-air television advertising pie is finite. The RIS recognises this.
- However, the RIS seriously underestimates the impact of the proposed changes. The RIS cites a lower four year impact figure supplied by SBS ($28.5 million), rather than the higher number suggested by the government's own efficiency report ($100 million).
- Independent modelling commissioned by Free TV, using actual SBS revenue data, has found that the likely impact on the Australian television advertising market is at least $148 million over four years.
- While the overall minutes per day on SBS will not change, the Managing Director of SBS has stated that 60-70% of their television advertising revenue is earned in prime time.[1] Free TV cannot understand how SBS will only achieve an additional $28.5 million over four years with twice the prime time inventory under the recommended Option 2 - particularly as the Managing Director has said he intends to hire more sales staff to add firepower to SBS's selling ability.[2]
- The inevitable revenue loss to commercial FTA broadcasters will come at the expense of the Australian production sector. Only 10% of SBS's schedule is Australian programming with 90% of SBS' schedule made up of foreign acquisitions.[3] Given this measure is intended to make up a government funding shortfall it is unlikely that SBS' proportion of foreign acquisitions versus Australian commissions will change. In contrast, Free TV

[1] Evidence of Mr Michael Ebeid to Senate Estimates (Environment and Communications Legislation Committee), Parliament of Australia, Canberra, 24 February 2015, pp 61.
[2] Evidence of Mr Michael Ebeid to Senate Estimates (Environment and Communications Legislation Committee), Parliament of Australia, Canberra, 24 February 2015, pp 61.
[3] Evidence of Mr Michael Ebeid to Senate Estimates (Environment and Communications Legislation Committee), Parliament of Australia, Canberra, 24 February 2015, pp 63-64.

broadcasters satisfy heavy Australian content obligations and spent over $1.54 billion on Australian content in 2013/4.

- Option 2 will put SBS on an almost equal footing with commercial broadcasters in prime time because, unlike commercial FTAs, SBS's advertising limits do not include program promotions. If SBS broadcasts four minutes of program promotions per hour[4] it will have 84 minutes of "non-program matter" in prime time. This contrasts with 78 minutes of "non-program matter" permitted on commercial free-to-air television. This proposal effectively allows SBS to become Australia's fourth commercial broadcaster. SBS is also not subject to many of the advertising restrictions contained in the Commercial Television Industry Code of Practice.

[4] Robin, Myriam "Ad hock: SBS have no trouble selling prime time" *Crikey* 3 March 2015

Introduction

Free TV represents all of Australia's commercial free-to-air television broadcasters. At no cost to the public, our members provide fifteen channels of content across a broad range of genres, as well as rich online and mobile offerings. The value of commercial free-to-air television to the Australian public remains high. On any given day, free-to-air television is watched by more than 13.5 million Australians.

The figures which form the basis of the proposed options in the *SBS Advertising Flexibility - Regulation Impact Statement* (RIS) are incorrect. This means that the true impact of the proposed amendments is not reflected in the RIS. The RIS also fails to consider the consequential impact of the proposed amendments on the Australian screen production sector.

Commercial free-to-air broadcasters are the major investors in Australian content spending a record $1.54 billion in 2013/14 and employing over fifteen thousand Australians, directly and indirectly.

Free TV Australia is strongly opposed to any moves to allow the SBS to increase its advertising, as proposed in Options 2 and 3 of the RIS. Option 1, involving no change, is the only option in the RIS which is supported by Free TV.

In relation to Option 2, Free TV is opposed to any increase in advertising during prime time, even if this involves moving advertising from another time of day. The SBS already receives hundreds of millions of dollars in funding from taxpayers. This should not be supplemented by additional advertising revenue (including from product placement) from an already fragmenting advertising market.

The commercial free-to-air television industry is responding to challenging and uncertain market conditions by investing in new, innovative platforms and services. Channels Seven, Nine and Ten all have catch-up services: PLUS7, 9jumpin and TENplay. Most of the Free TV broadcasters have invested heavily in the development of FreeView Plus. Broadcasters are also investing in new platforms such as streaming services in the face of new competition in this sector.

In this context, any additional competition for finite advertising revenues will have an unacceptable commercial impact on Free TV members.

Overview of options in the RIS

1. Maintain status quo/no change to regulation

This Option is strongly supported by Free TV. The RIS notes that under this Option, SBS's programming, content and services are likely to be significantly impacted.

This impact will only arise if the Government proceeds to withdraw funding from the SBS. It will not arise as a result of SBS's advertising rules remaining unchanged.

2. SBS Act amended to allow advertising flexibility

Option 2 was foreshadowed by the Minister for Communications in his speech on 19 November 2014.[5]

This option is likely to result in SBS doubling its advertising time in prime time from five to ten minutes per hour.

Prime time (from 6.00pm until midnight) is the key revenue driver for all broadcasters. Up to 80% of revenue from television advertising is earned in prime time.

The RIS notes that Option 2 is the preferred option for government. Therefore, this submission principally focuses on the impacts of Option 2.

Free TV does not agree with the projected revenue figures that form the basis of the discussion around Option 2. This is detailed further below.

3. Remove all advertising restrictions on SBS

Free TV notes that Option 3 is not recommended, with the RIS indicating that it would have "an increased impact on commercial broadcasters".

Advertising changes opposed in principle

Free TV broadcasters pay a licence fee of up to 4.5% of gross revenues on top of normal corporate taxes. They are also subject to significant additional regulatory obligations, such as Australian content quotas and in the case of regional broadcasters, provision of local news services, which do not apply to the SBS.

By adopting either Options 2 or 3 to gain additional revenues for SBS, the Government will be effectively requiring commercial television broadcasters to subsidise SBS funding cuts. This amounts to a government initiated value transfer from the private sector to the Commonwealth.

For an industry that is already one of the most heavily taxed and regulated in Australia, this is an unacceptable impost and is strongly opposed on principle.

Options 2 and 3 are therefore strongly opposed by Free TV.

[5] The Hon Malcolm Turnbull MP, The future of our public broadcasters, 19 November 2014.

Problems with SBS revenue projections

1. Inconsistency

The Government's own figures on the size of the potential revenue available to the SBS as a result of the proposed changes are contradictory.

The RIS states that under Option 2, SBS will gain additional revenue of $8 – $9 million per annum (by the fourth year).

However, the Minister for Communications has previously noted that the Lewis efficiency review suggested that the SBS could raise up to $20 million per annum under Option 2.[6] The Lewis Report itself noted that these figures were conservative.[7]

Finally, the RIS itself notes that without any restrictions and based on audience share alone, SBS's television advertising revenue could represent up to five per cent of the total television industry airtime revenue – which amounts to $195 million per annum. This is an annual increase of around $145 million per year.

The disparity between the figures used by the Government in discussing these changes raises serious questions about the adequacy of the modelling on which they are based, and highlights the lack of transparency and consultation regarding the true financial impact of the proposed changes.

2. Lack of transparency

The basis on which the government has accepted the SBS revenue calculations has not been made public and the modelling behind the Lewis Report figures has been redacted.

This makes it impossible for impacted parties to interrogate these figures and participate fully in this RIS process. It is also not clear why the government has accepted the SBS modelling over that of the Lewis Report.

3. Impact on commercial broadcasters grossly underestimated

Independent modelling conducted by Anomaly, a specialist industry market research and intelligence company, indicates that SBS could earn an additional $148 million over the next four years under Option 2.[8]

This is more than a "minor impact" for commercial free-to-air television broadcasters, and is far greater than the projected additional SBS revenues of $8 to $9 million per annum (by the fourth year) cited in the RIS.

The Anomaly model has been based on:

- Actual SBS revenue figures derived from Standard Media Index (SMI) data - a proprietary industry standard measurement, that captures advertising revenue sourced from major advertising agencies;
- Expected industry growth of 1.4% over the next five years in line with the PwC *Australian Entertainment and Media Outlook 2014-2018* Compound Annual Growth Rate (CAGR) forecast;
- A gradual "fill rate" of 70%; and
- an estimated peak revenue of 80% of total revenue earned.

[6] The Hon Malcolm Turnbull MP, The future of our public broadcasters, 19 November 2014.
[7] Peter Lewis, ABC and SBS Efficiency Study (Lewis Report), April 2014 at 84.
[8] Material sourced and analysis provided by Anomaly, an IPG Mediabrands owned company.

These calculations suggest that the RIS projections for Option 2 have significantly undervalued the impact of these changes on the advertising market.

Selling air-time is a highly specialised business, but the basic parameters are well known and understood. Free TV is confident that the Anomaly figures represent a fair projection of the possible revenue that the SBS can derive from the proposed changes at Option 2.

The figures in the RIS also do not detail the impact of the changes on particular parts of the commercial television industry, including regional broadcasters and Imparja (which will be affected significantly if there is an increase in the amount of advertising permitted on NITV).

In particular, an erosion of advertising revenues in regional areas will impact on broadcasters' continued ability to provide local news and information services.

Assumptions about advertising market are inaccurate

1. Advertising market is finite and fragmenting

The Australian advertising market is fragmenting, placing television advertising revenues under significant pressure.

Based on experience from the introduction of multi-channelling, an increase in television advertising inventory does not result in an increase in overall TV advertising revenue. In this finite and challenged market, allowing the SBS to increase its prime time advertising inventory would trigger a shift in advertising spend from the commercial networks to the SBS.

The RIS is not correct when it states that "it is not certain that any increase in SBS advertising spend will draw away revenue that would otherwise have gone to other commercial free-to-air broadcasters".

The SBS competes with commercial broadcasters for the same advertisers and audiences. A list of advertisers on the SBS (sourced from the SBS 2014 Annual Report) compared with the Nielson Adex data demonstrates that 85% of advertisers on the SBS also advertise on commercial free-to-air television.

The profile of the SBS viewing audience is similar to that of the commercial free-to-air TV audience, particularly when looking at the lucrative 25-54 year old demographic, which is the key buying audience for advertisers.

For FY13-14, 25-54's accounted for 46.8% of the commercial free-to-air audience and 41.1% of the SBS audience. During the World Cup Soccer event, 25-54's made up 48.8% of the SBS's audience.[9]

The latest PricewaterhouseCoopers analysis from the report *Australian Entertainment and Media Outlook 2014-2018* demonstrates that growth in free-to-air television advertising revenues has remained flat since 2008, and has a Compound Annual Growth Rate (CAGR) forecast of just 1.4% over the next five years, well below CPI.[10]

[9] Source: OzTAM, 5 cap cities, people 25-54, FY 13-14 (01/07/13 – 30/06/14), 2014 World Cup Soccer (12/06/14 – 13/07/14), all day 2am-2am profile, based on consolidated data.

In this environment, it is grossly misleading to suggest that either the television advertising "pie" will grow, or that the additional SBS revenue will come from a different market segment than the one in which existing broadcasters compete. Allowing the SBS to increase the amount of advertising sold in prime time can only lead to existing players receiving less of a finite revenue pool.

Further eroding the revenue of Free TV broadcasters will compromise our ability to continue investing in high quality Australian content such as news, current affairs, drama, regional content and sport, and amount to yet another tax on our revenue.

2. Prime time

The RIS suggests that Option 2 will have a "minor impact" on commercial broadcasters.

One of the reasons supporting this assertion is that the 120 minute daily advertising cap for SBS will not change.

This argument is misleading and fails to understand the operations of the television advertising market.

Up to 80% of all advertising revenue is earned in prime time. Currently the SBS is limited to 5 minutes of advertising per hour in prime time.

Under Option 2 they will be able to have 10 minutes of advertising per hour in prime time - double their current advertising inventory - so long as the overall daily limit of 120 minutes remains the same.

Any increase in advertising inventory in prime time will impact the overall market by driving down prices, as advertisers use increased supply to drive down the cost of advertising spots.

This move is particularly disruptive in a market where revenues and revenue share remain under pressure.

3. Non-program matter

The RIS also notes that the 10 minute hourly cap allowed under Option 2 "is still well below the hourly limits imposed on the commercial broadcasters under the [Code]".

However, the RIS fails to note that the definition of 'advertising' in the *Special Broadcasting Services Act 1991* (Cth) does not include program promotions.[11] This is in contrast to the Commercial Television Industry Code which captures program promotions and other items in the definition of non-program matter.[12]

If SBS broadcasts four minutes of program promotions per hour[13] it will have 84 minutes of "non-program matter" in prime time. This contrasts with 78 minutes of "non-program matter" permitted on commercial FTAs. When this additional material is taken into account, the actual amount of advertising minutes on the SBS in prime time under Option 2 will closely resemble the amount of advertising on commercial television.

[11] Section 45(3), *Special Broadcasting Services Act 1991*.
[12] See Clause 5.4 of the Commercial Television Industry Code of Practice.
[13] Robin, Myriam "Ad hock: SBS have no trouble selling prime time" *Crikey* 3 March 2015

4. Share

In discussing Option 2, the RIS states that the impact on commercial broadcasters will be shared equally, so the proposal is unlikely to result in a significant loss in revenue to any individual network.

This is an overly simplistic consideration of the advertising market.

In particular, the RIS does not consider the impact of the proposed changes on Imparja (who will be particularly impacted if increased advertising is permitted on NITV), or regional broadcasters.

This approach also fails to consider the variations in revenue share for metropolitan broadcasters that result from a particular broadcaster having a very strong programming slate, or a popular sporting event.

Impact of proposed changes go beyond revenues

There are many flow-on impacts of the proposed changes beyond the direct impact on commercial free-to-air revenues.

1. Detrimental impact on Australian screen production sector

A loss of revenues for commercial free-to-air broadcasters will undermine their major contribution to the production of expensive Australian content across a range of genres including, news, sport, drama and children's programs.

Commercial free-to-air broadcasters are subject to extensive obligations to produce Australian content, including specific requirements for first release Australian drama, documentary and children's programs. This is in addition to the 55% transmission quota for Australian content, which applies to Free TV members' primary channels.

Regional commercial television broadcasters also face an additional financial impost as a result of the licence condition that requires the delivery of local content to regional areas in parts of Australia.

The cost of meeting these obligations has increased substantially, with broadcasters now devoting approximately 79% of their total programming expenditure to Australian content.[14]

Each year Screen Australia reports that commercial broadcasters are the leading underwriters of Australian drama, contributing more than any other source to the TV drama slate.[15]

The SBS does not have any comparable obligations, despite government funding of over $267 million in 2013/14.[16]

At a Senate Estimates hearing in February 2015, Managing Director Michael Ebeid noted that only about 10% of the SBS schedule was local Australian content, and

[14] Australian content expenditure figures compiled by Free TV. See: http://www.freetv.com.au/SiteMedia/W3SVC751/Uploads/Documents/RECORD_1.54_BILLION_DOLLAR_COMMITMENT_TO_FREE_AUSSIE_CONTENT.pdf

[15] See, for example, Screen Australia Drama Report – Production of feature films and TV drama in Australia 2013/4 at page 14

[16] SBS, Annual Report 2014 at 70.

that that SBS was “pretty much out of drama”, because Australian drama was very expensive to produce.[17]

Because this measure is only about making up a shortfall in funding from the Government, there is no reason to believe that the amount SBS spends on commissioning Australian content will change.

However, a loss of revenue as a result of the proposed changes will impact on commercial broadcasters’ ability to continue to fund Australian content. This will have flow on effects to the Australian independent production industry, which relies heavily on the investment from the commercial free-to-air television sector. It could also cost jobs around the country as broadcasters are forced to reduce costs to meet revenue shortfalls.

2. SBS will become a fourth commercial network

In 2013 there was bi-partisan support for changes to the *Broadcasting Services Act 1992* to prevent the allocation of a fourth commercial television broadcasting licence.[18]

Free TV members are deeply concerned that the proposal to increase prime time advertising on the SBS equates to the introduction of a fourth commercial television broadcasting network by stealth. As noted above, the preferred option in the RIS will see SBS broadcasting 84 minutes of non-programming matter in prime time compared to 78 minutes under the Free TV commercial Television Code of Practice.

Increased advertising, particularly integrated advertising, means that SBS will skew its programming and focus more toward mainstream programming and sports, to appeal to advertisers and sponsors. This is contrary to its Charter-defined function to “*educate and entertain all Australians*.”

The SBS plays an important role in the community, but it is already government-funded. Furthermore, the hybrid model, which allows the SBS to derive advertising and sponsorship revenue, was never intended to place them on an equal footing with commercial television broadcasters. This principle should not be modified further.

Product placement

The RIS indicates that legislative change to allow product placement is to provide “clarity” on the issue.

For the reasons set out above, Free TV is strongly opposed to any legislative change that would allow the SBS to increase advertising of any kind, including product placement.

[17] Evidence of Mr Michael Ebeid to Senate Estimates (Environment and Communications Legislation Committee), Parliament of Australia, Canberra, 24 February 2015, pp 63-64.

[18] Section 37A of the *Broadcasting Services Act 1992*