Australian Government

Australian Communications and Media Authority

researchacma
Evidence that informs

Attachment C

Economic analysis of regional commercial television broadcasters

Broadcasting Services (Material of Local Significance – Regional Aggregated Commercial Television Broadcasting Licences) Direction 2013

DECEMBER 2013

communicating
facilitating
regulating

Canberra
Red Building
Benjamin Offices
Chan Street
Belconnen ACT

PO Box 78
Belconnen ACT 2616

T +61 2 6219 5555
F +61 2 6219 5353

Melbourne
Level 32
Melbourne Central Tower
360 Elizabeth Street
Melbourne VIC

PO Box 13112
Law Courts
Melbourne VIC 8010

T +61 3 9963 6800
F +61 3 9963 6899

Sydney
Level 5
The Bay Centre
65 Pirrama Road
Pyrmont NSW

PO Box Q500
Queen Victoria Building
NSW 1230

T +61 2 9334 7700
1800 226 667
F +61 2 9334 7799

Contents

Contents (Continued)

Executive summary

Background to the investigation

The Australian Communications and Media Authority (ACMA) has been directed to review the operation and effectiveness of section 43A of the *Broadcasting Services Act 1992* (the Act), which relates to the provision of local content by regional commercial television broadcasters ('regional broadcasters').[1]

This report examines the economic circumstances facing regional broadcasters operating in regional Australia (regional broadcasters) and the costs of extending the provision of local content requirements to the additional regional areas (that is, any area that is not defined as a metropolitan area under Schedule 4 of the Act).[2] This report does not seek to quantify the benefits from extending local content requirements or the economic circumstances of other providers of local content.

History of local content requirements

Between 1989 and 1992, a number of regional areas that had received television services from monopoly providers were aggregated into four larger areas: regional Queensland, northern New South Wales, southern New South Wales and regional Victoria. Driving this aggregation was the desire to provide three commercial television services to the majority of regional Australia enabling commercial television in regional areas to be comparable to capital cities. The aggregation also encouraged robust competition between regional broadcasters while also creating larger and more viable regional television markets.

In 2002, section 43A of the Act was introduced to require that the ACMA ensures there is a licence condition in force that requires regional broadcasters in specified regional aggregated licence areas to broadcast minimum levels of material of local significance (local content) to each local area in the licence area. The section specifies that the regional aggregated commercial television licence areas are:

- Northern New South Wales
- Southern New South Wales
- Regional Victoria
- Eastern Victoria
- Western Victoria
- Regional Queensland.

[1] The Minister for Broadband, Communications and the Digital Economy issued the ACMA with the Broadcasting Services (Material of Local Significance – Regional Aggregated Commercial Television Broadcasting Licences) Direction 2013 to examine the operation and effectiveness of section 43A of the *Broadcasting Services Act 1992* (BSA).

[2] Schedule 4 of the Act defines a metropolitan licence area as a licence area in which is situated the General Post Office of the capital city of New South Wales, Victoria, Queensland, Western Australia or South Australia. It does not include the licence area of a commercial television broadcasting licence allocated under section 38c of the Act.

In 2007 local content obligations were extended to include Tasmania. All other regional licence areas do not currently have local content obligations.[3]

Economic circumstances of regional broadcasters

To understand the economic circumstances faced by regional broadcasters, the ACMA analysed the financial returns submitted by broadcasters over the last five years to determine their licence fees, and a report prepared by PricewaterhouseCoopers (PwC) in 2013 that examined the economic circumstances of broadcasters.[4]

Trends in revenue, costs and profitability of regional commercial television broadcasters

The PwC report found that over the next five years, two key influences are likely to shape how regional Australians access and consume content:

> increasing speed of fixed internet connections

> continued proliferation of smart devices and supporting high speed broadband networks.

The provision of higher speed access to the internet in regional Australia will present opportunities and threats to regional broadcasters. The opportunities include lower costs in producing content and advertising on new platforms. The threats include lower advertising revenues as viewers consume content provided by other providers.

PwC also notes about the television industry:[5]

> the overall trend of revenue for the free-to-air television industry since 2005–06 has been negative in real terms[6], reflecting the structural shift in the market for advertising towards the internet and macroeconomic shocks (for example, the global financial crisis)

> the commercial television industry has significantly reduced costs in real terms since 2008–09 and this cost cutting has enabled it to maintain profitability in the face of falling revenue

> the global financial crisis has had a smaller negative impact on profits for regional broadcasters compared to their metropolitan counterparts, but the revenue of regional broadcasters has not recovered for all regional broadcasters since the global financial crisis.

Profitability, risk and financial outlook of regional broadcasters

Over the period 2007–08 to 2011–12, the return on assets of most regional broadcasters was approximately five per cent. This level of return is more consistent with low-risk investments (for example, cash, Australian bonds, etc.), than a regional broadcaster, which is exposed to higher levels of financial risk.

The major regional broadcasters also have high levels of debt. In 2011–12, the level of debt was 53 per cent of assets, and nine times annual earnings. This makes regional broadcasting a riskier investment, as the business has to repay debts before it can provide a return to equity holders.

---

[3] For a table outlining all of the licence areas, please refer to **Appendix A.**

[4] PwC, *Economic analysis of programming requirements on broadcasters*, Report for the ACMA, September 2013, pp. 38, 40, 44–45.

[5] loc. cit.

[6] In other words revenue has grown at a rate less than the level of inflation.

In terms of the future outlook for profitability, the commercial television broadcasting industry is entering a challenging environment with:

> advertising revenues for the television industry forecast to fall (when factoring out inflation) and substitutes (for example, online provision of audiovisual content) becoming more readily available[7]

> the cost of acquiring content appears not to be falling[8]; with limits to what regional broadcasters are able to do to reduce other costs, such as labour, given past cost cutting.

Profitability of the three industry segments

The regional television broadcasting industry can be divided into three broad segments, and the economic circumstance of each is outlined below:

1. **Major regional broadcasters** (WIN Corporation, Prime Media Group and Southern Cross Austereo)—the major regional broadcasters' profitability is low and comparable with the return of risk-free investments like cash management accounts. However unlike cash management accounts, the level of financial risk of the major regional broadcasters is high. Over the period examined, cost cutting (mainly labour costs) has sustained profitability in the face of declining revenues on average.[9] However, there are natural limits to the scope for further labour cost reductions; which vary from broadcaster to broadcaster.
2. **Subsidiaries of the metropolitan broadcasters** (regional subsidiaries of Nine Network and Seven Network)—the combined profitability of these two broadcasters is similar to the major regional broadcasters. While the subsidiaries appear to be exposed to less financial risk than the major regional broadcasters, their profitability is still low given their level of financial risk.
3. **Other regional broadcasters** (Imparja and joint ventures between the regional broadcasters which commenced after 2000)—the economic circumstances of these broadcasters are the most challenging of the three broad segments. The profitability throughout the five-year period for most of these broadcasters has been negative.

Cost of extending local content requirements to other regional areas

The ACMA estimated the cost of extending local content obligations to all regional licence areas for the three broad groups of regional broadcasters, namely major regional broadcasters, subsidiaries of the metropolitan broadcasters and other regional broadcasters.

The ACMA used two different methods and data sources to estimate the cost:

> Under the first method, the ACMA estimated the cost based on the historical differences in major regional broadcasters' costs between licence areas with local content requirements to licence areas without local content requirements. The first

[7] PwC, *Report for the ACMA*, September 2013, op. cit., p. 29.

[8] See for example L. Sinclair, 'Seven re-signs with regional affiliate Prime', *The Australian*, 11 October 2013, <www.theaustralian.com.au/media/seven-re-signs-with-regional-affiliate-prime/story-e6frg996-1226738131873>, accessed 18 October 2013; N. Tabakoff, 'WIN Corp boss Bruce Gordon opens door to merger with Nine Network or Network Ten', *The Australian*, 10 June 2013, <www.theaustralian.com.au/media/broadcast/win-corp-boss-bruce-gordon-opens-door-to-merger-with-nine-or-ten/story-fna045gd-1226660984829#>, accessed on: 4 November 2013; and D. Davidson, 'Ten, Southern Cross Media ink new affiliation agreement', *The Australian*, 26 July 2013, <www.theaustralian.com.au/media/broadcast/ten-southern-cross-media-ink-new-affiliation-agreement/story-fna045gd-1226686392013#mm-premium>, accessed 4 November 2013.

[9] As measured in real (2012) dollars. The trend relating to revenues and costs has not been uniform with the level of decline varying amongst broadcasters.

method used the data in broadcasters' television activity statements (TASs) to the ACMA.

- Under the second method, the ACMA estimated the cost of providing local content via news updates based on data submitted by most of the established regional broadcasters as part of this inquiry, on their current costs of delivering local content. Meeting local content obligations by news updates is considerably cheaper than meeting it by news bulletins, and therefore this provides a conservative cost estimate.

The results are outlined below.

1. **Major regional broadcasters** (WIN, Prime and Southern Cross Austereo)—applying the first method, the ACMA estimates that extending the local content requirement to all licence areas covered by the major regional broadcasters would increase costs by $0.7 million per annum per broadcaster (on average in 2011–12 dollars), reducing profitability by around one per cent.

   Applying the second method, the ACMA estimates that extending the local content requirement to all licence areas covered by the major regional broadcasters would cost on average $9.6 million per broadcaster in the first year, with annual ongoing costs of $0.7 million thereafter. This compares with profitability per broadcaster of around $51 million in 2011–12. The high cost in the first year reflects the capital costs of meeting local content requirements, and the estimate assumes these are incurred and fully amortised in the first year.

   In addition to this impact on costs and profitability, extending local content obligations would restrict broadcasters' ability to reduce costs future by placing a floor on their costs relating to local content. Given forecast declines in advertising revenues, this increases the burden of cost cutting on other areas of broadcasters' operations, restricting the programming they can offer viewers, and their ability to compete with other content providers (such as Pay TV).

2. **Subsidiaries of the metropolitan broadcasters** (regional subsidiaries of Nine Network and Seven Network)—all of the licence areas served by the subsidiaries of the metropolitan broadcasters are subject to local content requirements, with the exception of Darwin and parts of Regional Queensland[10]. However, in these licence areas, the broadcasters provide local content. Therefore, extending the local content obligations to all regional licence areas would have little effect on the costs and the profitability of these broadcasters. That being said, like the major regional broadcasters, local content obligations could restrict the broadcasters' ability to reduce costs into the future.

3. **Other regional broadcasters** (Imparja and joint ventures between the regional broadcasters)—the first method could not be applied as not all of the other regional broadcasters operated through a period pre-dating the imposition of local content obligations.

   Using the second method, the ACMA estimates that extending the local content requirement to all licence areas covered by the other regional broadcasters would cost on average $5.8 million per broadcaster in the first year, with annual ongoing costs of $400,000. The high cost in the first year reflects the capital costs of meeting local content requirements, and the estimate assumes these are incurred and fully amortised in the first year.

   These cost increases would threaten the long term viability of these broadcasters, who on average have made losses in each of the last five years. In 2011–12, the average loss was $200,000 per broadcaster, and therefore the higher ongoing

[10] The local content obligation only requires licensees to provide local content to five of the seven local areas for the Regional Queensland commercial television licence area. As some broadcasters provide local content to seven local areas, the content provided to the two additional local areas is considered to be additional local content.

costs of extending the local content requirements would result in a tripling of losses.

It is also worth noting that in all of the licence areas covered by the other regional broadcasters, at least one major regional broadcaster or subsidiary of a metropolitan broadcaster is already providing local content. Therefore, the costs of extending local content obligations could outweigh the potential benefits.

If the local content obligations were extended, the most significant outlay for the major and other regional broadcasters revolves around initial start-up costs. In other words, regional broadcasters would need to spend money on equipment in order to provide local content. This money would need to be funded, all other things being equal, resulting in increased financial risk to the regional broadcasters and/or lower profitability.

It is important to note that some care should be taken with the findings in this report, as it draws heavily on data provided by the regional broadcasters on a commercial-in-confidence basis. While the ACMA provides guidance to commercial television broadcasters on how to complete the TASs and the submissions on the costs of providing local content, it does not verify the information reported by individual broadcasters, nor does it stipulate accounting standards to broadcasters. For these reasons, there may be differences in accounting practices between the broadcasters. In addition:

- most of the licensees own radio and television assets, and the ACMA has not stipulated how these revenues and expenses be split by the licensees providing the returns
- the ACMA is unable to compare all of the information provided against publically available annual reports, as not all regional broadcasters are publically listed companies and do not report revenues relating to their television activities in regional Australia as a separate item.

The ACMA has aggregated the analysis of data provided by individual regional broadcasters when assessing the economic conditions facing regional broadcasters in regional Australia in order to protect the confidentiality of data provided by individual regional broadcasters. The aggregate trends in revenues and expenses are not uniform across all regional broadcasters.

The ACMA’s methodology and calculations in this report has been peer reviewed by Frontier Economics. The peer review is included as **Attachment A** to this report.

Introduction

The ACMA has been directed to review the operation and effectiveness of section 43A of the *Broadcasting Services Act 1992* (the Act), which relates to the provision of local content by regional broadcasters. The investigation must be completed by 27 December 2013 and must include consideration of:

1. the importance of material of local significance to people living in regional areas of Australia
2. whether people living in regional areas of Australia have adequate access to material of local significance provided via commercial television broadcasting services
3. the impact on people living in regional areas of Australia of recent and significant changes (if any) to the broadcast of material of local significance
4. how access to material of local significance can be maintained and enhanced for people living in regional areas of Australia
5. whether other sources of local (or regional) information are available to people living in regional areas of Australia
6. the economic circumstances facing regional broadcasters operating in regional areas of Australia
7. Whether section 43A should be extended to apply to regional broadcasters operating in specified additional regional areas.

This report seeks to address the economic circumstances facing regional broadcasters operating in regional Australia (that is, item 6), and the costs of extending the provision of local content requirements to the additional regional areas.[11] This report does not seek to quantify the benefits from extending local content requirements.

In its approach to analysis, the ACMA has gathered information about the extent of local content being provided on commercial television in regional areas, how this content is created and the costs of providing local content on commercial television.

[11] Schedule 4 of the Act defines a metropolitan licence area as a licence area in which is situated the General Post Office of the capital city of New South Wales, Victoria, Queensland, Western Australia or South Australia. It does not include the licence area of a commercial television broadcasting licence allocated under section 38c of the Act.

Background

Between 1989 and 1992, a number of regional areas that had received television services from monopoly providers were aggregated into four larger areas—regional Queensland, northern New South Wales, southern New South Wales and regional Victoria. Driving this aggregation was the desire to provide three commercial television services to the majority of regional Australia enabling commercial television in regional areas to be comparable to capital cities. The aggregation also encouraged robust competition between regional television station operators, while also creating larger and more viable regional television markets.

In May 2002, the Australian Broadcasting Authority (ABA) — predecessor to the ACMA—allocated each of the regional broadcasters a second commercial television broadcasting licence. The additional licences have the same licence areas as the regional broadcasters' existing licence, and the regional broadcasters were required to commence the services within 12 months from the date of allocation of the licences. The regional broadcasters entered into affiliation agreements for the supply of programs or, alternatively, to broadcast a mix of programming sourced from more than one network ('cherry picking'). In 2003, the Act was further amended to refine section 38B.[12]

Following the changes to the Act an additional seven joint ventures (five terrestrial and two satellite providers) were formed.

There are currently 13 broadcasters operating in regional Australia.

[12] APH, *Communications Legislation Amendment Bill (No. 3) 2003*, Bill Digest, <www.aph.gov.au/Parliamentary_Business/Bills_Legislation/bd/bd0304/04bd003>, accessed 23 August 2013.

Table 1: Regional broadcasters operating in regional Australia

Major regional broadcasters

Broadcaster	Region (s)	Mode
Prime	Regional New South Wales, regional southern Queensland, remote and regional Western Australia and regional Victoria	Terrestrial
Southern Cross Austereo	Regional Queensland, regional New South Wales, regional South Australia, regional Victoria, Tasmania and the Spencer Gulf	Terrestrial
WIN	Regional New South Wales, regional Queensland, regional South Australia, regional Victoria, remote and regional Western Australia and Tasmania	Terrestrial

Subsidiaries of major metropolitan broadcasters

Broadcaster	Region (s)	Mode
Nine Network	Darwin and regional northern New South Wales	Terrestrial
Seven Queensland	Regional Queensland	Terrestrial

Other regional broadcasters

Broadcaster	Region (s)	Mode
Central Digital Television (owned by Southern Cross Austereo and Imparja)	Remote central and eastern Australia	Terrestrial
Darwin Digital Television (owned by Southern Cross Austereo and Nine Network Darwin)	Darwin	Terrestrial
Eastern Australia Satellite Broadcasters (owned by Imparja and Southern Cross Austereo)	Northern and south eastern Australia	Satellite
Imparja	Remote Australia	Terrestrial and Satellite
Mildura Digital Television (owned by Prime and WIN)	Mildura/Sunraysia	Terrestrial
Tasmanian Digital Television (owned by Southern Cross Austereo and WIN)	Tasmania	Terrestrial
WA Satco (owned by Prime and WIN)	Western Australia	Satellite
West Digital Television (owned by Prime and WIN)	Geraldton, Kalgoorlie and regional western Australia	Terrestrial

Source: ACMA analysis.

Local content obligations

In 2002, an investigation was carried out by the former Australian Broadcasting Authority (ABA) due to community concerns about the closure of news bureaus by Southern Cross Austereo in Canberra, Cairns, Townsville, Darwin and Alice Springs and the cutting of local news bulletins in Canberra, Newcastle and Wollongong by Prime. Subsequently, in the same year, the ABA introduced a local content licence condition for regional commercial television. In 2007, the licence condition was extended to include Tasmania.

In accordance with the Act, the Broadcasting Services (Additional Television Licence Condition) Notice 8 November 2007 (the licence condition) defines local areas for each of the aggregated television licence areas.

Table 2: Local areas by licence area[13]

Licence area	Local areas
Northern New South Wales	Central Coast Hunter Northern Rivers and Mid North Coast North West Slopes and Plains Richmond/Tweed
Regional Queensland	Capricornia Central Coast and Whitsundays Darling Downs Far North Queensland North Queensland Sunshine Coast Wide Bay
Regional Victoria	Gippsland North Central Victoria South West Victoria Upper Murray and Goulburn Valley
Southern New South Wales	Australian Capital Territory and Southern Tablelands Central Tablelands and Central West Slopes South West Slopes and East Riverina Illawarra and South Coast
Tasmania	Tasmania

Source: ACMA analysis.

The licence condition requires each regional broadcaster to accumulate at least 90 points of local content per week within each local area and at least 720 points of local content in each local area over a six week period (an average of 120 points per week).

Points are accumulated for local content broadcast during the following eligible periods:

> from 6:30am to midnight (inclusive) on Monday to Friday

> from 8:00am to midnight (inclusive) on Saturday and Sunday.

Points are accumulated as follows:

> news that relates directly to the local area attracts two points per minute

> other material that relates directly to the local area attracts one point per minute

> news or other material that relates directly to the licence area attracts one point per minute

> repeat material (other than community service announcements) does not attract points.

[13] Regional broadcasters are required to serve five of the seven local areas in the Regional QLD licence area and four of the five regional areas Northern NSW licence area: the affected licensees choose the local areas to be served in these licence areas. Further information is available on the ACMA's website www.acma.gov.au/Industry/Broadcast/Television/Local--regional-content/local-areas-and-licensees-local-regional-content-i-acma.

- in each six week period, 50 per cent of the points accumulated need to be attributable to material which relates directly to the local area
- in each six week period, no more than 10 per cent of points accumulated can be attributed to community service announcements.

Due to low take-up rates of digital receivers among consumers in Tasmania, the ACMA granted alternative treatment to Tasmanian Digital Television for a limited period as an interim measure. From 1 January 2008, Tasmanian Digital Television was required to meet minimum quotas comprising a minimum of 120 points per calendar year.

A separate licence condition was imposed to reflect these alternative arrangements for Tasmanian Digital Television. This treatment applied for a finite period of time, until the earlier of:

- the Saturday immediately following switch-off of analog television services in the Tasmanian licence area; or
- 31 December 2012.

Tasmanian Digital Television is now required to meet the same local content obligations as the other regional broadcasters operating in Tasmania.

Appendix A lists the level of local content provision by the regional broadcasters throughout regional Australia.

Economic circumstances facing regional broadcasters operating in regional areas of Australia

Overview

The main purpose of the analysis in this section is to highlight some key economic trends over the last five-year period of regional broadcasters' television operations.

Methodology

The analysis of the economic circumstances facing commercial television broadcasters operating in regional Australia (regional broadcasters), draws from the commercial television activity statements (TASs) provided to the ACMA by broadcasters. The ACMA's information gathering powers under subsection 205B(1) of the Act create a requirement for broadcasters to '*keep and maintain financial accounts in relation to the service or services provided under the licence* and to *make those accounts available for inspection by the ACMA or an authorised officer when requested to do so'*.[14]

The analysis in this section examines the TASs lodged by regional broadcasters from 2007–08 to 2011–12. In 2011–12, there were 54 licences and 33 licensees who lodged returns to the ACMA. The 33 licensees comprise 13 broadcasters and are grouped in the analysis as follows: [15]

- Three major regional broadcasters:
  - Prime
  - Southern Cross Austereo
  - WIN
- Eight joint venture and other regional broadcasters (other broadcasters):
  - Imparja
  - Eastern Australia Satellite Broadcasters
  - Central Digital Television
  - Darwin Digital Television
  - West Digital Television
  - Mildura Digital Television
  - Tasmanian Digital Television
  - WA Satco
- Two subsidiaries of metropolitan broadcasters:
  - Nine Network Australia operating in Darwin and Northern New South Wales
  - Seven Queensland—Regional Queensland.

[14] *Broadcasting Services Act 1992* (Cwlth), ss. 205B(1)(a) and 205B(1)(b).

[15] In some cases, the same broadcaster holds multiple licences which span multiple regions. This then collapses further when you consider one broadcaster as part of a single broadcaster. For example, Southern Cross Communications Pty Limited held licences in Eastern Victoria (Licence number 106) and Western Victoria (Licence Number 104). Southern Cross then comprises from five to seven licensees in any given year.

The TASs are reported on a per licence basis. In other words, the data has been disaggregated to a specific licence area and by licence holder. Following on from this, the analysis performed has grouped the broadcasters into 'major regional broadcasters', 'subsidiaries of metropolitan broadcasters' and 'other regional broadcasters'.

It is important to note that some care should be taken with interpreting the data derived from the data collection process. While the ACMA provides guidance to broadcasters on how to complete the TASs, it does not verify the information reported by individual broadcasters, nor does it stipulate accounting standards to broadcasters. For these reasons, there may be differences in accounting practices between the broadcasters in any one year and differences in accounting practices by a broadcaster from year-to-year. In addition:

> most of the licensees own radio and television assets, and the ACMA has not stipulated how these revenues and expenses be split by the licensees providing the returns
> the ACMA is unable to compare all of the information provided against publically available annual reports, as not all regional broadcasters are publically listed companies and do not report revenues relating to their television activities in regional Australia as a separate item.

To ensure that confidentiality of financial data is maintained, the ACMA does not report data relating to the subsidiaries of the major metropolitan broadcasters. The subsidiaries comprise three broadcasters. However, the total service revenue of two of the broadcasters is greater than 85 per cent of the total service revenue. Therefore, the ACMA considered that this is likely to reveal information which has been provided on a commercial-in-confidence basis. To avoid revealing commercially sensitive data, the ACMA has discussed the economic circumstances of the subsidiaries on a qualitative basis.

The ACMA has chosen to analyse a five-year period, from 2007–08 to 2011–12. The ACMA considers that this approach strikes a balance between several considerations, such as:

> the reduced reliability of longer dated data (for example, data prior to the 2004–05 financial year was collected by the ABA, which had different arrangements with respect to the checking of data)
> the potential impact of one-off events such as the mining boom, technology bubble, global financial crisis[16], on the reliability of the data
> sufficiency of time to observe trends
> considering a time period which is most likely to reflect current market conditions.

As there is a lag of one year with the TASs, the ACMA is only able to analyse up until 2011–12 at this point in time. All amounts discussed in this report have been converted into real (2012) dollars using the Gross Domestic Product (GDP) Implicit Price Deflator.

In conducting the analysis of the other regional broadcasters, the ACMA has only examined broadcasters which have been operating throughout the five-year period.

[16] It was decided that although 2007–08 may be affected by the global financial crisis, that including this year would mainly impact revenues observed in 2007–08 which may result in understating the downward trend than if 2006–07 or 2008–09 were selected as the starting point instead.

The main advantage of this approach is that trends relating to the five-year period are not affected by new entrants to the market.[17]

In its analysis, the ACMA has examined:

> the profitability of regional broadcasters' television activities
> sources of revenue and expenditure
> the balance sheets and elements of financial risk.

This information has been used to obtain a better understanding of the economic circumstances of the regional broadcasters and provides a relevant input into determining whether local content requirements should be extended. To support this analysis, the ACMA has also looked at previous analysis it has conducted with the Broadcaster Financial Returns data and work reported by other parties.

Present economic circumstances

Quantifying the financial performance of the regional broadcasters over the five-year period requires an analysis of profitability, which involves a consideration the difference between total service revenues and expenses. Therefore, the analysis in this section examines the average (by each grouping; major regional broadcasters, subsidiaries of metropolitan broadcasters and other broadcasters):

> total service revenues of the regional broadcasters
> total service expenditures/costs of the regional broadcasters
> television net service profits/losses before tax of the regional broadcasters.[18]

The average is calculated by summing up values across the broadcasters within a group and dividing the amount by the number of broadcasters within the group. It is important to note that a key limitation of this technique is that some of the trends for individual regional broadcasters may be lost where the change in revenues, expenses, etc for one or more of the broadcasters are large. However, this approach has been adopted to protect commercially sensitive information.

The levels of profitability are then examined by looking at profit margins and the return on assets of the regional broadcasters. The return on assets is then compared to returns for other types of investments to get an indication of how the return on assets in regional broadcasting fares when compared to other investment classes.

It should be noted at this point that this analysis focuses specifically on amounts reported in the TASs for regional Australia and does not consider all parts of the regional broadcasters' operations (for example, operations in metropolitan cities, commercial radio activities, etc.).

In order to obtain an understanding of the economic circumstances faced by regional broadcasters it is important to consider not only profitability but also levels of assets, debt and elements of financial risk. The analysis in this section analyses:

> total service assets, service liabilities and net service assets (that is, total service assets less liabilities)
> quick ratios, debt to assets and debt to earnings before interest, tax, depreciation and amortisation (EBITDA).

---

[17] This is due to entrants in the other regional broadcaster group having entered into different licence areas. However, the entrance of these broadcasters may have an impact on the revenues and profitability of the major regional broadcasters who are currently operating in the same markets as the entrants.

[18] The reported profits net off the depreciation and interest expenses incurred by the regional broadcaster.

The analysis calculates averages for regional broadcasters. As a means to gauge what is considered a high level of financial risk, the ACMA has used Standard and Poor's corporate credit rating criteria as a basis for comparison when looking at the financial ratios relating to mid to long-term financial risk.

Projected economic circumstances into the future

The analysis in this section draws on the ACMA's research on emerging trends and the economic circumstances of regional broadcasters. It analyses some of the major cost drivers for regional broadcasters; namely employee costs (the sum of salaries and wages, and employee on-costs) and the cost of acquiring content (affiliation fees) that may impact on future costs and profitability of regional broadcasters.

The analysis in this section calculates the relative change in costs (that is, index) using 2007–08 as a base year (that is, 100.00). For example, a value of 70.00 can be interpreted as expenses falling by 30 per cent since 2007–08.

The relative change in expenses is used to observe trends over the five-year period.

Emerging trends

Historically, a commercial television broadcasting licence gave its owner access to the Australian public and the right to sell that access to advertisers. Advertising timeslots were constrained in line with regulated supply of broadcasting services. Up until the year 2000, the commercial television industry's revenues grew at a faster rate than the Australian economy and commercial television broadcasters achieved financial returns well above those of other industries.[19]

PricewaterhouseCoopers (PwC) reported that television remains the predominant source of audiovisual content for Australian audiences, noting (amongst other points):[20]

> digital terrestrial television penetration is the highest of all content platforms—currently at 98 per cent of all households, compared with internet connections (80 per cent), tablets (31 per cent) and smart phones (61 per cent)

> the average daily reach of the for Free To Air (FTA) television broadcasters increased from 13 million in 2008 to 14 million in 2012. This rate of increase (a compound annual growth rate (CAGR) of 1.9 per cent) was greater than Australia's population growth (a CAGR of 1.6 per cent) over the same period

> analysis conducted by Screen Australia suggests that the introduction of the multi-channels has had a positive impact on the audience size for FTA television

> the number of subscribers to subscription television increased from 1.5 million in 2003 to 2.4 million in 2011

> recent market research suggests that watching television (and particularly FTA television) remains the most popular form of content consumption.

Present market conditions

Since 2000, alternatives to content delivery via traditional platforms (such as television, print and radio) have emerged—including the internet, subscription television, DVDs and games. These platforms have gained (and continue to gain) in popularity, attracting both new audiences and advertisers. In addition, the way that

[19] ACMA, *Commercial television industry financial trends 1978–79 to 2005–06*, ACMA report, June 2008, p. 10.

[20] PwC, *Report for the ACMA*, September 2013, op. cit., pp. 10–12.

viewers consume and engage with television content has begun to change. PwC noted the following trends:[21]

> A small (but growing) number of consumers are using personal video recorders to record scheduled programs and to consume these programs at a time that is more convenient for them. This allows consumers to skip through advertisement breaks in the programs.

> Users are starting to multi-task via a second screen (for example, laptops, computers, mobile devices) while watching television, which may reduce the influence of television advertising over time.

> There has been a small (but growing) shift to Internet Protocol Television.

> Younger generations are consuming less television while older generations are consuming more television.

PwC notes in its recent report to the ACMA, where it discusses the television industry, that:[22]

> the overall trend of revenue since 2005–06 in real terms has been negative reflecting the structural shift in the market for advertising and macroeconomic shocks (for example, the global financial crisis)

> significant declines in 2008–09 expenditures in real terms following cost cutting measures undertaken throughout the industry

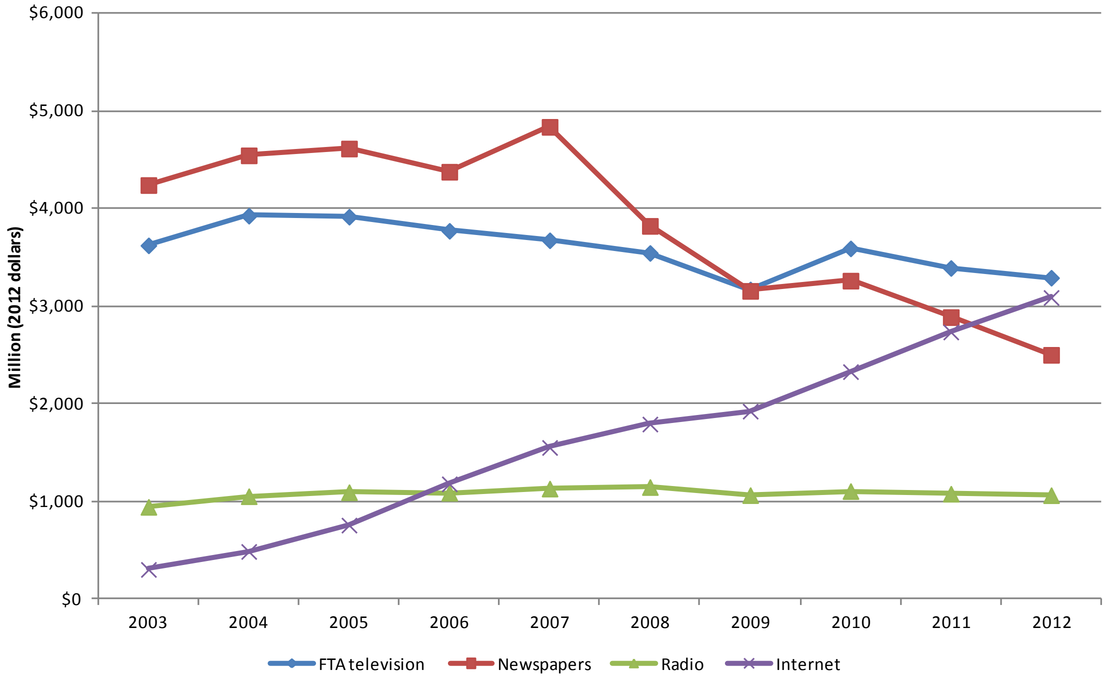
> the global financial crisis appeared to have a smaller impact on profits for regional broadcasters, although revenues appear not to have recovered as experienced by the metropolitan broadcasters

> FTA television advertising revenue appears to be trending downwards in real terms from 2004–05, while internet advertising revenue has grown unabated over the same period.

[21] ibid., pp. 12–14.

[22] ibid., pp. 38, 40 and 45.

Figure 1 Historical advertising revenue for key entertainment and media sectors, 2003–12 (2012 dollars)



Source: PwC, Report for the ACMA*, September 2013, p. 45.*

In response to the declining revenues and increasing programming costs, the commercial television broadcasters have sought to:

> reduce other costs (for example, staffing costs)

> implement strategies such as embedded advertising in order to stabilise the decline in revenues.

Influences in the next five years

Over the next five years, two key influences are likely to shape how regional Australians access and consume content:

> increasing speed of fixed internet connections

> the continued proliferation of smart devices and supporting communications networks.

In regional Australia both of these factors are likely to complement each other. It is the policy of the Australian Government to give highest priority to provide broadband to the suburbs, towns and regions with the poorest broadband services.[23] The stated goal is to provide download speeds of between 25 and 100 megabits per second by the end of 2016 and 50 to 100 megabits per second by 2019.

Provision of higher speed access to the internet will present opportunities to commercial television broadcasters (such as lower costs in producing content and advertising on new platforms) and threats (such as lower advertising revenues as viewers consume content provided by other providers).

[23] Liberal Party, *Fast. Affordable. Sooner. The Coalition's Plan for a better NBN*, Policy document, <www.liberal.org.au/fast-affordable-sooner-coalitions-plan-better-nbn>, accessed 17 September 2013.

PwC noted that while revenue for FTA television is projected to grow over the next five years, the rate of growth is unlikely to exceed inflation.[24] In other words, PwC is projecting a real decrease in revenues for television broadcasters. This view was based on the forecasts in its most recent Australian Entertainment and Media Outlook.[25]

In addition, Venture Consulting, a specialist digital, media and telecoms strategy consultancy, is projecting declining revenues for FTA television and commercial radio due to competition from online platforms.

Table 3: Forecast advertising by platform—Venture Consulting[26]

Australian Advertising Market Forecast 2012–16

Media segment	2012A	2013E	2014F	2015F	2016F
	$m	$m	$m	$m	$m
FTA	3,452	3,393	3,263	3,159	3,026
Pay TV	439	471	499	530	560
Radio	1,012	1,001	967	938	893
Newspapers	2,863	2,359	1,907	1,618	1,375
Magazine	653	523	414	347	292
Outdoor	503	516	526	542	562
Cinema	89	93	97	100	104
Online	3,343	3,928	4,572	5,361	6,251
Total	12,354	12,284	12,244	12,595	13,062

Venture Consulting, Australian Advertising Market Forecast, Annual Update—2013*, 2 September 2013, p. 2*.

Economic circumstances of the major regional broadcasters

Present economic circumstances

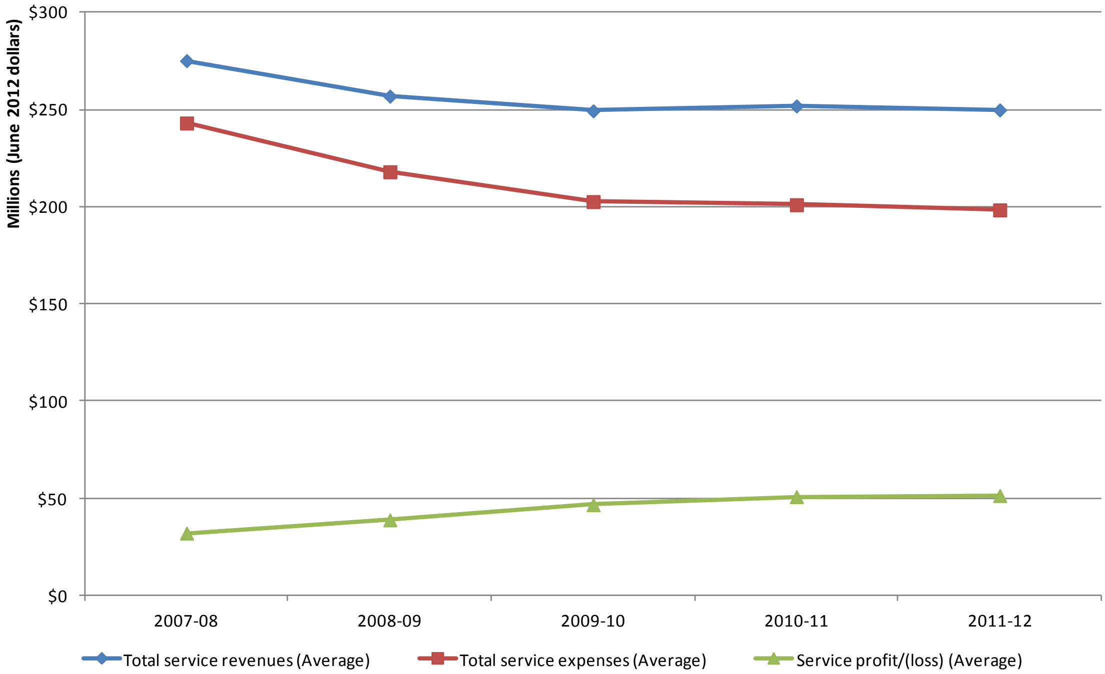
Figure 2 illustrates the major regional broadcasters' average profitability, revenues and expenses over five financial years.

[24] PwC, *Report for the ACMA*, September 2013, op. cit., p. 29.

[25] It is worth noting that operators within the commercial television broadcast industry have other sources of revenue. That being said, advertising revenues from television comprise a significant proportion of their revenues.

[26] It is not clear whether the forecast provided is in real or nominal dollars.

Figure 2: Major regional broadcasters' average revenues, expenses and profitability (2012 dollars)



Source: ACMA, Television Activity Statements 2007–08 to 2011-12 and ABS, GDP Price deflator, A2303730T.

Figure 2 illustrates that over the last five years:

> expenditures (costs) have declined at a greater rate than revenues for the major regional broadcasters resulting in an increase in profits over the five-year period in real (2012) dollars

> revenues on average have fallen for the major regional broadcasters:[27]

  > were higher in 2007–08 in part due to an election held in November 2007[28]

  > were lower in 2008–09 due to the year being having no election and being affected by downturn resulting from the global financial crisis

  > revenues slightly increased in the 2010–11 period, though this could be attributed to an election being held in August 2010.[29]

  > given that another election was held in 2013–14, it might be expected that advertising revenues may be slightly higher in that financial year.[30]

> the decline in expenses[31] in the past five financial years has been on average larger than the decline in revenues for the major regional broadcasters:

  > the decline in expenses is consistent with the Australian Bureau of Statistics' (ABS) recent survey into the film, television and digital games industries;

[27] It is worth noting that the level of decline in revenues has not been uniform across the major regional broadcasters.

[28] AEC, *Media Release 2007: Election day reminder - vote tomorrow!*, media release, 23 November 2007.

[29] In an election period commercial broadcasters receive additional advertising revenue from political parties. In addition, the commercial television code of practice permits an additional minute of advertising per hour when an election period is announced.

[30] See for example N. Tabakoff, 'Ad outlook healthy after election spike', *The Australian*, 17 September 2013, <www.theaustralian.com.au/media/ad-outlook-healthy-after-election-spike/story-e6frg996-1226720477549>, accessed 19 September.

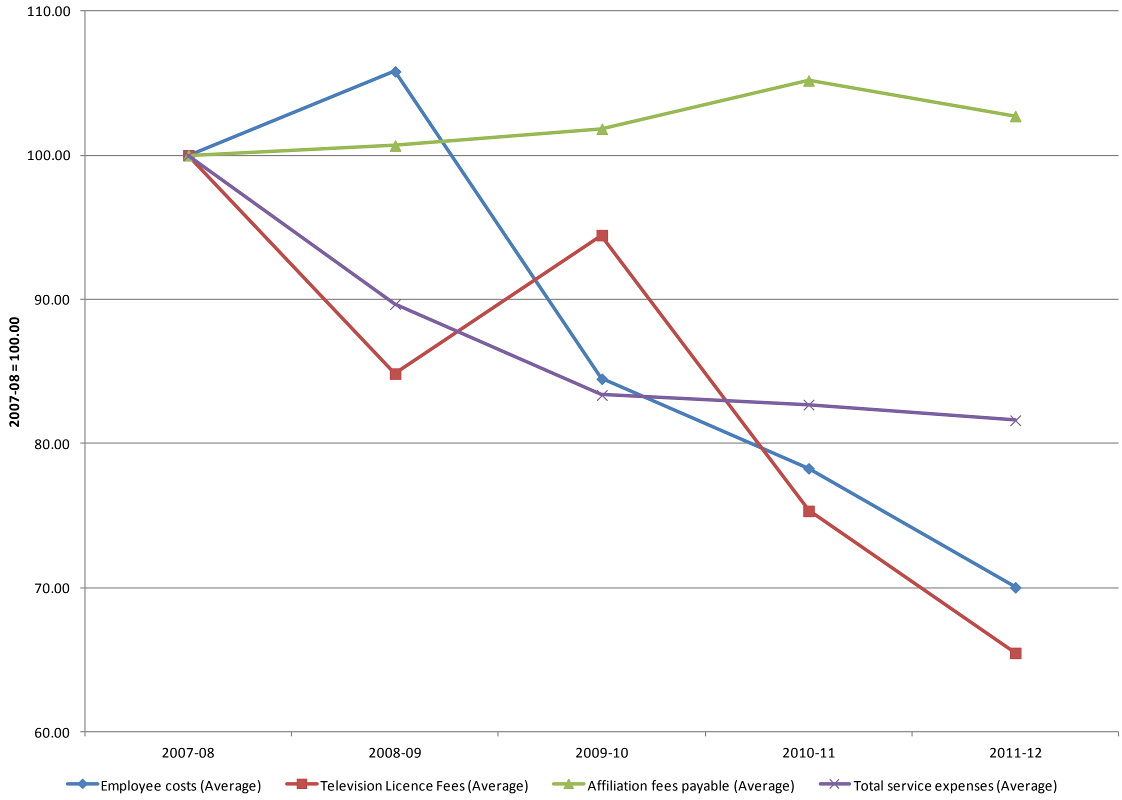
[31] It is worth noting that the level of decline in expenses has not been uniform across the major regional broadcasters.

where it found that total expenses for commercial free-to-air broadcasters have declined from 2006–07 ($3,704 million) to 2011–12 ($3,660 million)[32]

> major regional broadcasters have reported a focus on cost reduction.[33]

Figure 3 illustrates the relative changes in expenditure levels in recent years.

Figure 3 Major regional broadcasters' change in costs since 2007–08[34]



Source: ACMA analysis.

The two main areas of cost reduction have been in employee costs (salaries and wages, and employee on-costs) and television licence fees. Television licence fees fell when the former government introduced licence fee rebates for the transition to digital television.[35] Costs of acquiring content (affiliation fees) have not declined since

[32] ABS, *Film, television and digital games 2011-12*, ABS Report, 18 June 2013, accessed 19 June 2013, <www.abs.gov.au/AUSSTATS/abs@.nsf/Latestproducts/8679.0Media%20Release12011-12?opendocument&tabname=Summary&prodno=8679.0&issue=2011-12&num=&view=>, p. 6.The ABS notes that caution should be taken when making comparisons due to changes in collection years. For the 2006–07 collection, subscription television channel providers were included in production activity estimates, but excluded from the financial and employment estimates. In 2011–12, these businesses have been included in both the production activity estimates and also the financial and employment estimates.

[33] See for example Prime Media Group, *2012 Annual Report*, Annual report, 24 October 2012, pp. 3, 13; and Southern Cross Media Austereo, *Financial report for year ended 30 June 2012*, Annual report, 28 August 2012, p. 8.

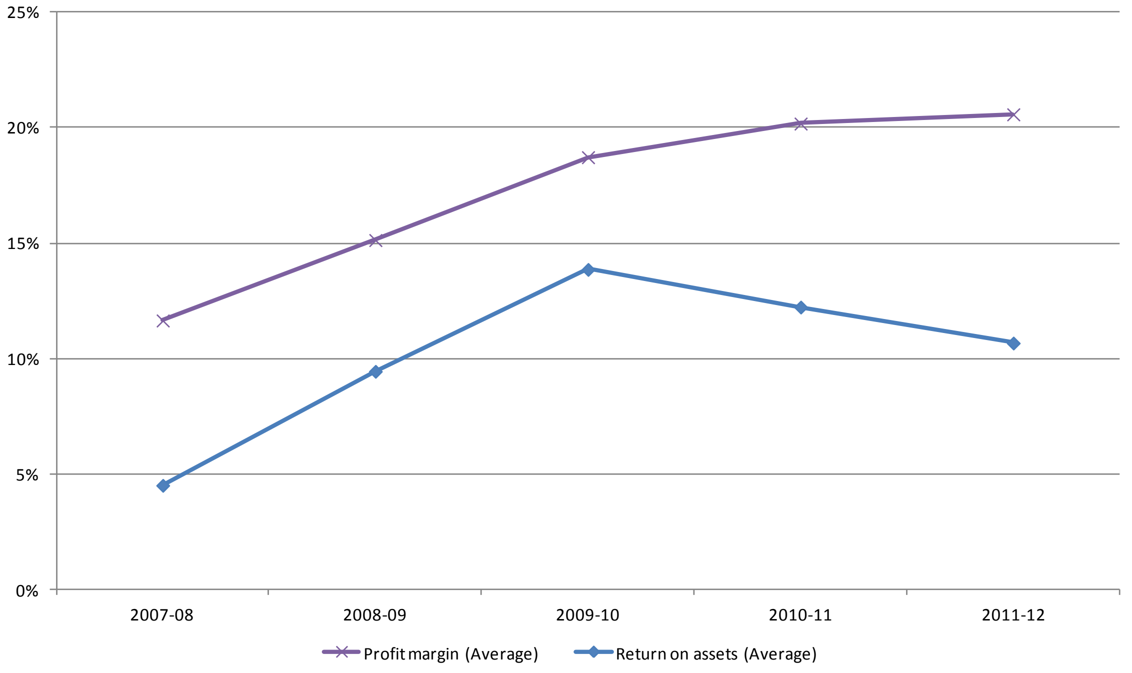
[34] Amounts were converted into 2012 dollars and then indexed against 2007–08 levels.

[35] ACMA, Broadcasting licence fee rebate, ACMA website, <www.acma.gov.au/Industry/Broadcast/Television/Licence-fees-and-charges/broadcasting-licence-fee-rebate-licence-fees-acma>, accessed 20 September 2013.

2007–08, and this trend does not appear to be abating.[36] Affiliation fees are linked closely with the costs of producing content by metropolitan broadcasters. Therefore, the scope for further cost reductions is likely to be limited for most major regional broadcasters.

Another way to consider the profitability of a market is to examine the average profit margins[37] and the average return on assets of the major regional broadcasters (see Figure 4).

Figure 4 Major regional broadcasters' average profit margins and return on assets



Source: ACMA analysis.

The ACMA observes:

> the profit margins of the major regional broadcasters increased early in the five-year period but then stabilised

> the return on assets of the major regional broadcasters increased early in the five-year period from three to five per cent but then remained around five per cent.

[36] It has been reported that one of the major regional broadcasters has renewed its affiliation with a major metropolitan network; rumoured to involve an increase affiliation fees. L. Sinclair, 'Seven re-signs with regional affiliate Prime', *The Australian*, 11 October 2013, <www.theaustralian.com.au/media/seven-re-signs-with-regional-affiliate-prime/story-e6frg996-1226738131873>, accessed 18 October 2013.

[37] Refer to the Glossary for a definition of profit margins.

The ACMA has looked at the rate of return, on a like-for-like basis[38], on different investments as a point of comparison.[39] The Australian Stock Exchange commissioned a report in June 2012 which examined rates of return on long-term investments and reported the following before-tax returns over 10 and 20-year periods to 31 December 2011:[40,41]

Table 4: Before tax (real) returns of investment classes

Investment class	10-year period
	%
Residential property investment	8.0
Australian shares	6.1
Australian bonds	6.4
Overseas shares (unhedged)	-3.1
Cash	3.8
Overseas (fully hedged)	3.7

Source: ASX and Russell Investments, Long-term investing report*, Report, June 2012, p. 1. <www.asx.com.au/documents/products/ASX_Report_2012.pdf>, accessed 23 August 2013.*

As observed in Figure 4, the average level of returns of the major regional broadcasters ranged between three and five per cent. When averaged over the five-year period, the level of return is 4.6 per cent. This is comparable to a cash investment (that is, putting your money into a cash management account at a bank), a diversified portfolio of shares, or Australian bonds. It is worth noting that:

> a cash investment is considered almost riskless as it is covered by the Australian government under the Australian Deposit Guarantee scheme[42]

> a diversified portfolio of Australian shares is likely to be considered to have a low level of risk, as by its nature it involves investments in industries across the Australian economy

> Australian bonds involve a mix of government and corporate bonds which like shares, reflect a diversified portfolio (including the Australian government) which is likely to be considered as a lower risk investment.

In contrast to these investments, money invested in a major regional broadcaster is likely to be subject to a higher level of financial risk, as the broadcasters need to service their debt before they can pay their owners. This can be confirmed by examining the average debt ratios of these businesses.

[38] Returns calculate on a net profit before tax basis.

[39] One limitation which is worth noting with this analysis is the investments and other comparisons made in this report relate to 10-year investment as opposed to a five-year investment. Currently the difference between a five-year and 10-year government bond is approximately 60 basis points. If you include this and make a slight allowance for additional compensation for the riskiness of investing by broadcasting by adding 100 basis points to the five-year return (increasing the return from 4.6 to 5.6 per cent), the return is still consistent with a lower risk investment. See RBA, F2 Capital Market Yield - Government Bonds, Statistics, <www.rba.gov.au/statistics/tables/xls/f02d.xls?accessed=2013-11-08-15-39-08>, accessed 8 November 2013.

[40] ASX and Russell Investments, *Long-term investing report*, Report, June 2012, p. 1. <www.asx.com.au/documents/products/ASX_Report_2012.pdf>.

[41] The returns for shares include capital growth and dividends.

[42] ASIC, *Banking: Managing your bank accounts*, website, <www.moneysmart.gov.au/managing-your-money/banking#guarantee>, accessed 28 October 2011.

Table 5: Major regional broadcasters' financial risk ratios

Average of Prime, Southern Cross Austereo and WIN

Financial year	Quick ratio (Current assets/ Current liabilities)	Debt/ Assets	Debt/ EBITDA
2007–08	0.3	62%	14.5
2008–09	0.9	53%	8.7
2009–10	0.4	56%	9.2
2010–11	1.3	54%	8.7
2011–12	1.4	54%	9.2

Source: ACMA analysis.

Examining the financial ratios over this five-year period (and 2007–08 is ignored due to the effect of the change of ownership for one of the major regional broadcasters[43,44]) the level of the quick ratios demonstrates that the major regional broadcasters are able to meet their short-term debt obligations. That is, in 2010–11 and 2011–12, the major broadcasters' current assets are approximately 1.3 to 1.4 times their current liabilities. However, when considering the medium to longer term obligations the level of financial risk appears to be quite prominent.

As a means to gauge what is considered a high level of financial risk, the ACMA has used Standard and Poor's corporate credit rating criteria as a basis for comparison:

> A business with a debt to earnings before interest taxes depreciation and amortisation (EBITDA) ratio exceeding six is considered highly leveraged.[45] In other words, although the major regional broadcasters' debt to EBITDA ratio has been falling over the five-year period, the average level of financial risk faced by the major regional broadcasters' television businesses is high.

> A business with a debt to asset ratio exceeding 55 per cent is considered as highly leveraged.[46] Over the five-year period, the ratio was below 55 per cent in all but two of the years. Standard and Poor's would consider this would constitute an aggressive level of financial risk.

[43] MMG, *Macquarie Media Group and Fairfax Media announce agreements to acquire the assets of Southern Cross Broadcasting*, ASX media release, 3 July 2007.

[44] The annual report notes that: ' ... management smoothly integrated the television operations with existing radio operations. Integration initiatives included the rationalisation of head office, the introduction of a unified reporting structure the co-location of national and local sales offices, and re-branding of the wider group.' MMG, *Concise financial report 30 June 2008*, Financial report, 27 August 2008.

[45] See for example Standard and Poor's, *Request For Comment: Corporate Criteria*, Request for comment, 26 June 2013, p. 37.

[46] See for example Standard and Poor's, *Corporate Ratings Criteria 2008*, Report, 26 June 2013, p. 21.

It is worth noting as a point of comparison:

- Standard and Poor's rate one particular major metropolitan broadcaster to have a credit rating of Ba2[47] (that is, equivalent of a BB rating or below investment grade debt which is BBB-).[48]
- The cost of debt for a business with a slightly better credit rating was recently benchmarked by the Australian Energy Regulator to be 4.2 per cent.[49] Therefore, one would expect that a business which is riskier than BBB rated business would be required to pay a higher rate.

This would suggest that a rate of return of 4.6 per cent would be sufficient to meet debt obligations but not much more beyond this amount. In other words, after meeting the debt obligations, not much money will be left to pay the equity holders, given the businesses are highly leveraged.

It is important to note the assessment of financial risk conducted here solely focuses on the TASs and does not take into account other parts of the business. For example, looking at the financial reports of these businesses for the year ended 30 June 2012 suggest lower levels of financial leverage.[50] These levels of gearing would suggest an intermediate level of financial risk rather than a highly leveraged business.

Overall, the analysis indicates that the levels of profitability observed would make it difficult to attract additional capital to finance the television activities of the regional broadcasters, given that the level of financial risk is much greater than a cash investment which has little or no financial risk.

Expanding local content requirements may require the broadcasters to invest in further capital which will need to be financed. If the capital required to meet this obligation is raised via debt or taken from retained earnings (that is, equity in the form of cash reserves), then this increases the financial risk faced by the business. Subsequently any increase in financial risk affects a business's ability to meet debt obligations and its long-term viability.

Future influences on regional broadcasters economic circumstances

Based on current forecasts, observed trends and policy settings, the ACMA considers that the profitability levels of the major regional broadcasters are not likely to improve in the long-run, having regard to:

- the observed decline in revenues (leaving election periods aside) is likely to continue, given the pressures on advertising revenues from alternatives such as internet advertising
- content costs not declining over the last five years with limits to the ability to reduce costs for most broadcasters suggest costs are unlikely to fall in the long-run.

---

[47] Moody's, *Nine Entertainment Group Pty Ltd credit rating – Moody's*, Long Term Rating, <www.moodys.com/credit-ratings/Nine-Entertainment-Group-Pty-Ltd-credit-rating-823284829>, accessed 7 August 2013.

[48] It is also interesting to note that Standard and Poor's has recently downgraded one of the Nine Entertainment Group's secured-term loan B facilities from BB to BB-. See for example, D. Davidson, 'Nine facing a win-lose situation', *The Australian*, 6 September 2013, <www.theaustralian.com.au/media/nine-facing-a-win-lose-situation/story-e6frg996-1226712560005>, accessed 6 September 2013.

[49] AER, *Final decision: ElectraNet transmission determination 2013-14 to 2017-18*, Final decision, April 2013, p. 133. This was calculated by combining the risk-free rate for a 10-year bond (3.51 per cent) with the debt risk premium of (3.18 per cent). The forecast level of inflation of 2.5 per cent was removed to ensure that a like for like comparison was made (i.e. a real rate of return compared to real cost of debt).

[50] See Southern Cross Austereo, *Southern Cross Austereo Annual Report 2012: for year ended 30 June 2012*, Annual report, 21 September 2012, p. 31; and Prime Media Group, *Prime Media Group Annual Report 2012*, Annual Report, 24 October 2012, p. 10.

When these trends are considered together with current profitability levels and levels of financial risk, it would appear that the major regional broadcasters face a challenging economic environment into the future. It is possible that some broadcasters may have more scope than others to conduct cost cutting; increasing their ability to meet these challenges.

Economic circumstances of the metropolitan subsidiaries

Present economic circumstances

The ACMA has not reported actual figures for the metropolitan subsidiaries in order to protect commercially sensitive information, as noted in the methodology section. The profitability, revenue and expenses reflect similar trends to the major regional broadcasters:

> The profit margins remain steady throughout the period at a lower level than the major regional broadcasters. This could be due to the way the metropolitan broadcasters allocate costs to their subsidiaries or it could be due to the metropolitan broadcasters focusing on other parts of their business with respect to the cost cutting observed in the PwC report.[51]

> The level of the return on assets is consistent with the returns observed by the major regional broadcasters. However, as noted above, these levels are low when considered against other investments, the level of financial risk faced by the business and the cost of debt which is commensurate with this level of risk.

However, as the metropolitan subsidiaries only operate in a small number of markets, the overall levels of profitability, expenses and revenues are much lower than the major regional broadcasters.

That being said, the relative level of liabilities/debt to assets is much lower when compared to the major regional broadcasters. This suggests that the level of financial risk faced by the subsidiaries (if examined in isolation) is lower that the major regional broadcasters. The data provided is subject to how assets and liabilities are allocated by their parent owners and also generally any assessment of creditworthiness would consider the parent business.

Economic circumstances into the future

For the subsidiaries of the major metropolitan broadcasters, it is likely that these regional broadcasters will face the same challenges which were identified for the major regional broadcasters. One differentiating factor is the lower level of financial risk reflected in the balance sheets of these businesses. This may mean that the subsidiaries of the major metropolitan broadcasters may have greater flexibility to adjust their finances in order to meet the challenges relating to increasing costs.

Economic circumstances of the other regional broadcasters

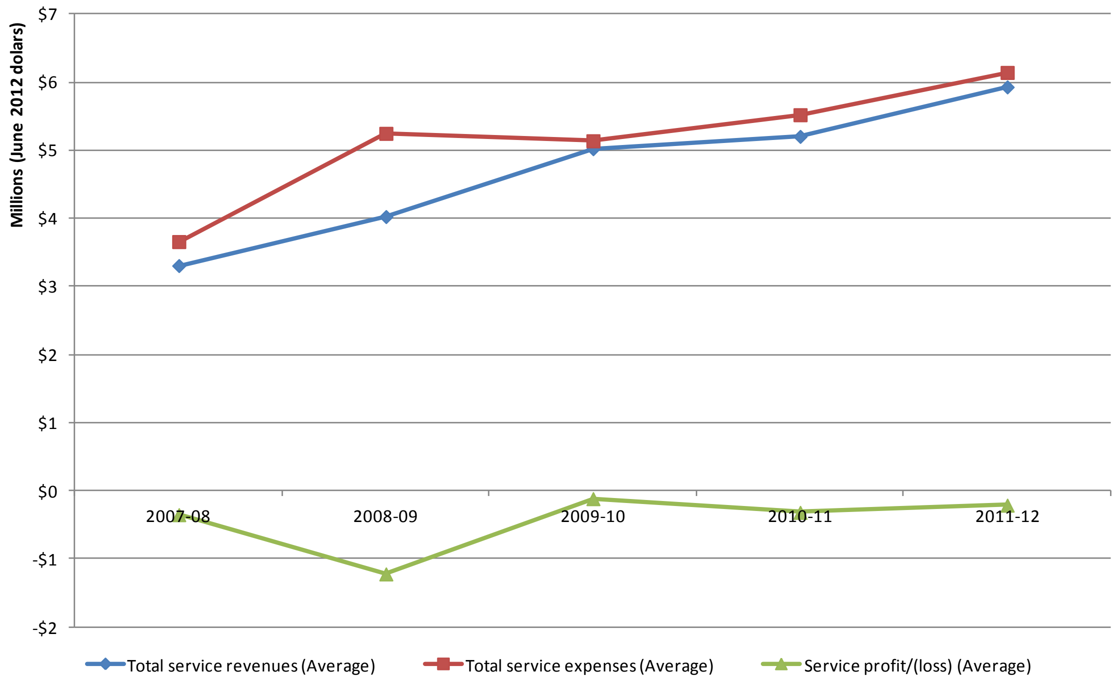
Present economic circumstances

In contrast to the major regional broadcasters and the metropolitan subsidiaries, the other regional broadcasters' profitability has been negative throughout the five-year period. This is despite a significant increase in revenues over the last five years. However, this may be due to the broadcasters receiving other funding sources such as government funding.

[51] PwC, *Report for the ACMA*, September 2013, op. cit., p. 38.

In addition, it would appear that expenses have been increasing considerably over the five-year period. This is consistent with these broadcasters expanding their operations within the licence area they operate. The oldest joint venture, Tasmanian Digital Television, entered the market in 2003, while most other ventures only commenced operating in more recent years.

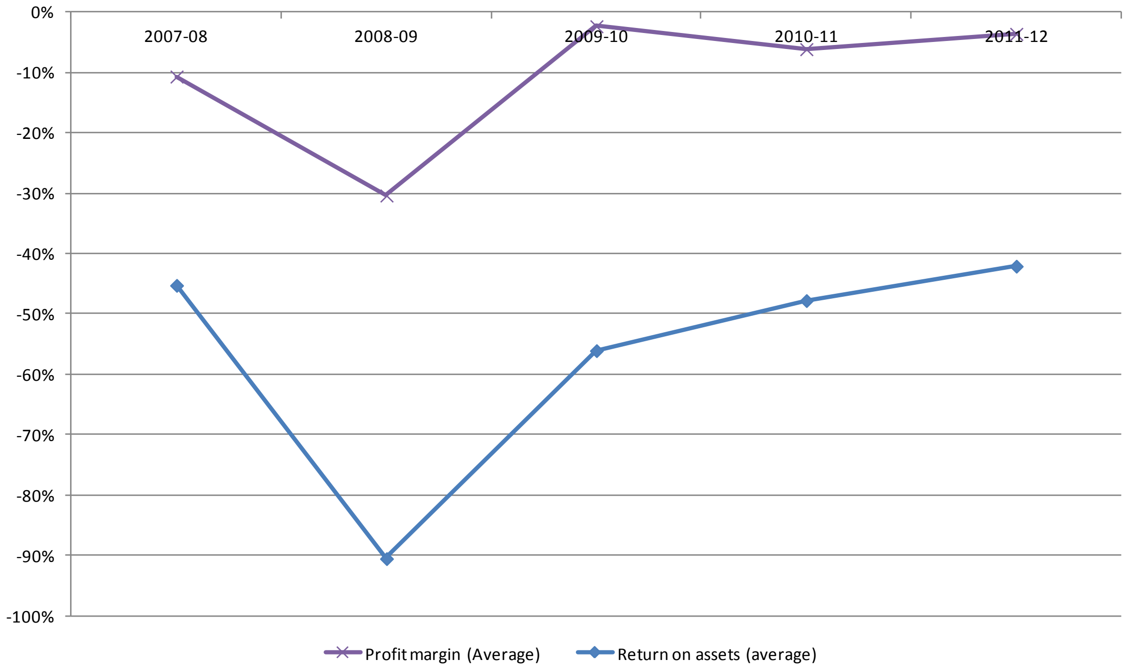
Figure 5: Other regional broadcasters' average profitability



Source: ACMA, Television Activity Statements 2007-08 to 2011-12 and ABS, GDP Price deflator, A2303730T.

Figure 6 examines profit margins and the return on assets of the other regional broadcasters.

Figure 6: Other regional broadcasters' average profit margins and return on assets

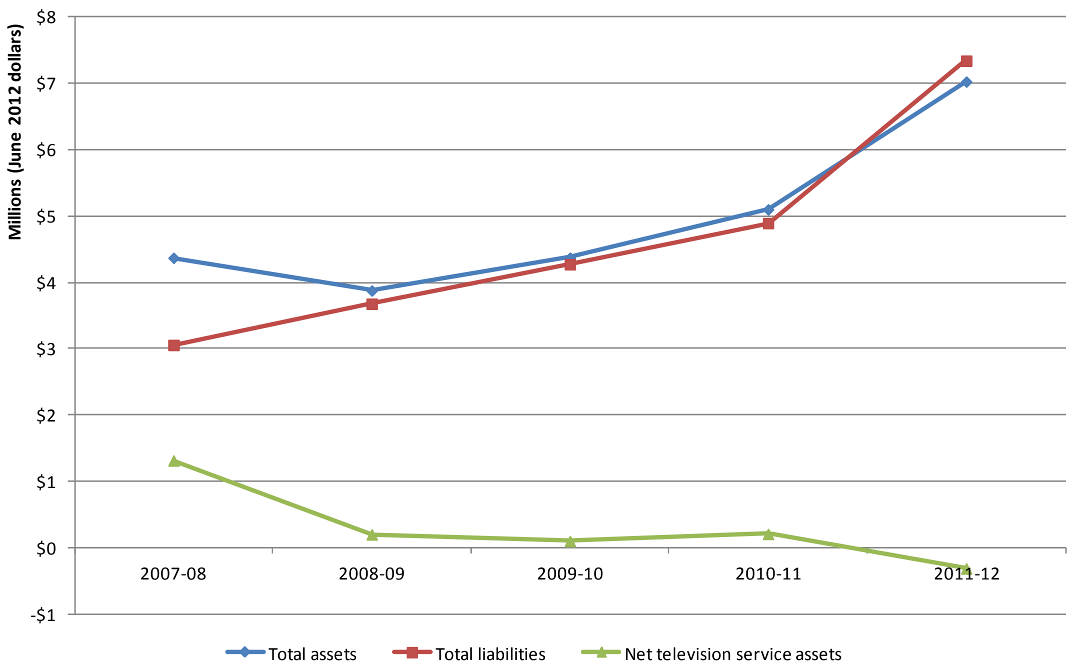


Source: ACMA analysis.

Consistent with the negative profitability observed during the period, both the profit margin and return on assets for the other regional broadcasters are negative.

Figure 7 analyses the total assets, liabilities and net television service assets of the other regional broadcasters.

Figure 7: Other regional broadcasters' average total assets, liabilities and net television service assets



Source: ACMA, Television Activity Statements 2007-08 to 2011-12 and ABS, GDP Price deflator, A2303730T.

As noted above, these broadcasters are relatively new and are going through a process of establishing themselves. Therefore, these businesses are largely reliant on funding from either their owners (that is, debt borrowed from established regional broadcasters) or government funding and are therefore operating largely on debt. This results in the net television service assets staying at low levels and being slightly negative in 2011–12 (that is, the joint ventures' assets cannot cover the debt owed). Given the high levels of debt relative to assets. However, it is standard practice for the purposes of considering financial risk to consider the support parent companies provide when making an assessment about factors such as financial risk and credit worthiness.[52,53] If the parent companies are considered supportive, then the financial risk associated with these businesses would reflect the financial risk of their owners. These businesses are generally owned by the major regional broadcasters.

Economic circumstances into the future

Based on current forecasts, observed trends and policy settings, the profitability levels of the other broadcasters are highly uncertain. The ACMA considers that the other broadcasters are likely to face similar challenges as those experienced by the regional broadcasters (that is, declining advertising revenues).

Key findings

When examining the economic circumstances faced by regional broadcasters there are a number of key points worth highlighting, including:

> the commercial television broadcasting industry is operating within a challenging environment with:
  > advertising revenues falling and substitutes (for example, online provision of audiovisual content) becoming more readily available
  > the cost of acquiring content reportedly not falling[54]; with limits to what regional broadcasters are able to do to reduce their other costs.
> the economic circumstances of the regional broadcasting industry could be split into three broad groups when considering economic circumstances, these are:
  1. **Major regional broadcasters** (WIN Corporation, Prime Media Group and Southern Cross Austereo)—the major regional broadcasters' profitability is low and comparable with the return of risk-free investments like cash management accounts. However unlike cash management accounts, the level of financial risk of the major regional broadcasters is high. Over the period examined, cost cutting (mainly labour costs) has sustained profitability in the face of declining revenues on average.[55] However, there are natural limits to the scope for further labour cost reductions; which vary from broadcaster to broadcaster.
  2. **Subsidiaries of the metropolitan broadcasters** (regional subsidiaries of Nine Network and Seven Network)—the combined profitability of these two broadcasters is similar to the major regional broadcasters. While the subsidiaries appear to be exposed to less financial risk than the major regional broadcasters, their profitability is still low given their level of financial risk.

[52] See for example Moody's, *Moody's revises Optus' rating to negative from stable*, announcement, 15 August 2012, <www.moodys.com/research/Moodys-revises-Optus-rating-to-negative-from-stable--PR_253082>, accessed 23 September 2013.

[53] It is worth noting that Imparja's position with respect to financial risk compared to most regional broadcasters is strong; with low levels of debt relative to the assets it owns. However, it is also worth noting that its profitability levels are similar to the joint ventures.

[54] See for example L. Sinclair, 'Seven re-signs with regional affiliate Prime', The Australian, 11 October 2013, <www.theaustralian.com.au/media/seven-re-signs-with-regional-affiliate-prime/story-e6frg996-1226738131873>, accessed 18 October 2013.

[55] As measured in real (2012) dollars. The trend relating to revenues and costs has not been uniform with the level of decline varying amongst broadcasters.

3. **Other regional broadcasters** (Imparja and joint ventures between the regional broadcasters which commenced after 2000)—the economic circumstances of these broadcasters are the most challenging of the three broad segments. The profitability throughout the five-year period for most of these broadcasters has been negative.

Cost of extending section 43A requirements to other regional areas

Overview

The purpose of this chapter is to:

> examine the potential costs of extending the local content obligations to other regional licence areas

> examine the impact on the profitability of the regional broadcasters.

Methodology

The ACMA has been directed by the minister to consider whether section 43A should be extended to apply to commercial television broadcasters operating in specified additional regional areas. Forming a view on extending local content requirements requires a consideration of the costs and benefits of making a regulatory change.

One of the main inputs into determining whether extending local content obligations to other regional licence areas would be a net benefit to society (which is covered in the ACMA's inquiry report and not this report) is the cost it would have on regional broadcasters.

The ACMA estimated the cost of extending local content obligations to all regional licence areas for the three broad groups of regional broadcasters, namely major regional broadcasters, subsidiaries of the metropolitan broadcasters and other regional broadcasters.

The ACMA used two different methods and data sources to estimate the cost:

> Under the first method, the ACMA estimated the cost based on the historical differences in major regional broadcasters' costs between licence areas with local content requirements and licence areas without local content requirements. This method used the data in broadcasters' TASs to the ACMA from 1999–2000 to 2011–12.

> Under the second method, the ACMA estimated the cost per broadcaster per licence area of providing local content via news updates based on data submitted by most of the established regional broadcasters as part of this inquiry. This cost per broadcaster per licence area was then applied to the number of licence areas where no local content was being provided to establish the total additional cost of extending the obligations to all licence areas.

It is important to note that both approaches are using historical or current data to estimate the costs of extending local content obligations on an *ongoing basis*. It is possible that a number of factors could result in the cost of providing local content decreasing or increasing over time; potentially affecting the cost impact of extending local content obligations.

Estimation of the cost of extending local content obligations using historical data (first method)

This analysis examined whether the introduction of local content obligations led to an increase in costs for the regional broadcasters; and had local content obligations applied to all licence areas, how much higher the ongoing costs of regional broadcasters would be.

The analysis in this section draws on the historical TAS data:

- Covering a period where local content obligations were introduced in 2003–04[56] in response to station closures which occurred from 1999 to 2001.[57]
- For the three major regional broadcasters. The analysis was based on the cost of the three major regional broadcasters. To protect commercially sensitive information, this analysis was not conducted for the subsidiaries of the major metropolitan broadcasters. Other regional broadcasters are not included in this analysis as they either did not operate for the entire period or did not have operations in locations where local content obligations were introduced. Therefore, the ACMA would caution against using the percentages calculated in this section to either the subsidiaries of the metropolitan broadcasters or the other broadcasters.

The analysis in this section compares:

1. The level of expenses in licence areas with local content obligations in the period prior to the introduction of local content obligations (1999–2000 to 2003–04), to the period after the obligations were imposed (2003–04 onwards). If the trends in the costs changes between these periods then it could be argued that local content obligations had an impact on the major regional broadcasters' costs.
2. The change in average expenses by broadcaster in licence areas with local content obligations, to licence areas without local content obligations. To do this, the ACMA calculated the change in the labour and capital expenses from 2003–04 (when local content obligations were introduced) to 2011–12. This approach was used to estimate the additional cost of extending local content obligations to major regional broadcasters.

Refer to **Appendix B** for a detailed description of the methodology.

An advantage of using historical data (that is, the first method in the methodology section) is that it allows the ACMA to observe expense data over a long period of time rather than costs observed at a single point in time (that is, the second method in the methodology section).

That being said, there are some key limitations with the first method such as:

- The data cannot provide estimates for meeting local content obligations using different approaches (for example, news updates and news bulletins) as the major broadcasters use a mix of approaches from licence area to licence area. This could mean that the cost estimated under the first method understates or overstates the additional annual cost of extending local content obligations to the major regional broadcasters. Therefore, some caution should be taken when making any conclusions on the basis of historical data.
- The analysis implicitly assumes that the difference in the growth of costs between the two groups of licence areas, namely areas with local content obligations and areas without, is attributed to the difference in local content obligations applying over the period examined. However, it is quite possible that another unrelated factor could have explained the differential.
- As this analysis relies on the TAS data, the same limitations relating to the analysis of the economic circumstances applies to the analysis in this section. While the

[56] ABA, *Broadcasting Services (Additional Television Licence Condition) Notice 7 April 2003*, ABA Notice, 7 April 2003.

[57] News bureaux in Canberra, Cairns, Townsville, Darwin and Alice Springs were closed by Southern Cross Broadcasting (Australia) Limited in November 2001. This followed similar closures by Prime Television Ltd in Canberra, Newcastle and Wollongong in June 2001. See ABA, *Adequacy of local news and information programs on commercial television services in Regional Queensland, Northern NSW, Southern NSW and Regional Victoria (aggregated markets A, B, C and D)*, ABA report, August 2002, p. 9.

ACMA provides guidance to broadcasters on how to complete the TASs, it does not verify the information reported by individual broadcasters, nor does it stipulate accounting standards to broadcasters. Other limitations of the TAS data are discussed in the Methodology section of the chapter which examines the Economic circumstances facing regional broadcasters operating in regional areas of Australia.

> The analysis is sensitive to the years the changes in cost are analysed against. For example, if you calculate the growth rate in costs based on the last five years, then the trend in costs is reversed. That being said, it is appropriate to consider costs over the full nine-year period of the analysis. This is because the initial up-front costs of meeting local content obligations are likely to represent a substantial element in the costs of extending local content obligations. A shorter, five-year, period of analysis would not capture the impact of these initial up-front costs, which were likely to have been incurred close to when the existing local content obligations came into effect in 2003–04.

> It is possible that the major regional broadcasters may have increased their expenditures relating to local content obligations in advance of the licence obligations being put in place, in which case the method underestimates the cost of local content obligations. However, this is likely to have varied on a broadcaster-by-broadcaster basis as some of the broadcasters may have not needed to alter their behaviour when the local content obligations were imposed. Therefore, the ACMA chose to compare costs starting from 2003–04, rather than conducting a complex broadcaster-by-broadcaster analysis.

It is possible that econometric analysis may have captured some of these effects. However, this approach would present its own challenges such as controlling for differences between licence areas, news models (bulletins and updates) and other factors over a relatively short time period. Therefore, it was decided that a simpler approach be used; with the limitations being acknowledged.

Costs of extending local content obligations using data obtained from submissions provided by regional broadcasters in 2013 (second method)

The analysis in this section draws upon submissions received from most of the established regional broadcasters. The ACMA estimated the cost to broadcasters of extending local content obligations to all licence areas (see **Appendix C**). The method assumes that the local content obligations are met using cheaper news updates rather than news bulletins, and therefore reflects a conservative estimate of meeting the obligation.

The analysis in this section draws upon data provided by five regional broadcasters, in response to a questionnaire issued by the ACMA in July 2013. Data was received from major regional broadcasters, the subsidiaries of the metropolitan broadcasters and the other regional broadcasters. The ACMA used this data to derive the minimum cost of meeting local content requirements in a medium sized local area (see **Appendix C**). This cost per local area was then used to derive the costs per region and per broadcaster of extending the local content obligation to all areas.

The key strengths of this approach are:

> The ACMA received submissions from a mix of broadcasters (at least one regional broadcaster from the three categories analysed in the economic circumstances of regional broadcasters chapter of this report). This allowed the ACMA to confirm that the costs specifically relating to the delivery of local content were similar irrespective of the type of broadcaster.

> The submissions also provided costs for different methods of providing local content (for example, news bulletin supplemented by news updates) and their cost estimates are outlined in **Appendix C** of this report.

Some key limitations with this approach are:

> The data does not cover all of the regional broadcasters which operate within Australia.
> The data examines a single point in time. That being said, the data is likely to be more current than the analysis of the historical data.
> The ACMA has taken a best endeavours approach to ensure that the information provided by regional broadcasters is accurate. However, as with the data submitted in the TASs, the information provided has not been audited. In addition, there may be differences in the approach taken to allocating the costs of delivering local content. Further limitations with the data are discussed in **Appendix C** of this report.
> The estimates relating to the initial costs of providing local content have been derived from two submissions and are one of the main cost components in this analysis. In addition, the regions where these broadcasters currently do not provide local content to are quite large. Therefore, it is possible that the initial costs might be overstated. That being said, whether this component results in a high cost to the broadcasters largely depends on the period this amount is amortised over. The longer the period of time, the smaller effect it has on ongoing costs. The term over which this cost should be amortised over was not been provided by the two regional broadcasters who provided this estimate.
> It is assumed in this analysis that if regional broadcasters are currently delivering local content in regions without content obligations, they could meet the local content obligations without needing to change their level of local content. Therefore, the ACMA has made a conservative estimate of the cost of meeting local content obligations. If this is not the case, then the costs of meeting local content obligations would have to be adjusted upward, having reference to analysis conducted in **Appendix C** of this report.
> One of the main impacts of extending and maintaining local content obligations for broadcasters, which cannot be estimated with this modelling approach, is it limits the regional broadcasters' ability to reduce costs by reducing or ceasing to deliver local content such as by shutting down news services. Therefore, being required to provide local content may result in:
    > higher costs when compared to providing other cheaper content
    > forgone revenue[58] from not being able to air a more popular program or advertisement.

In the tables below, the higher costs and forgone revenue are referred to as 'loss in flexibility' and 'introduces opportunity costs' respectively.

Costs of extending local content obligations for major regional broadcasters

As noted in the methodology section, the ACMA has developed estimates of extending local content obligations for the major regional broadcasters using two approaches:

> Under the first method, the ACMA estimated the cost based on the differences between licence areas with local content requirements to licence areas without local content requirements. This first method used the data in broadcasters' TASs to the ACMA.

[58] The forgone revenue is calculated as the difference in revenue between airing the two different types of content (for example, the news bulletin and the program it replaces, or the advertisement and the news update).

> Under the second method, the ACMA estimated the cost of providing local content via news updates based on data submitted by most of the established regional broadcasters as part of this inquiry.

Estimation of the cost of extending local content obligations using historical data

Figure 8 looks at expenses data from 1999–2000 (prior to the closure of several local stations) to 2011–12 to see whether local content obligations had an effect on major regional broadcasters' costs. The graph groups expenses into two categories for regional broadcasters that are likely to be affected by local content obligations, these are:

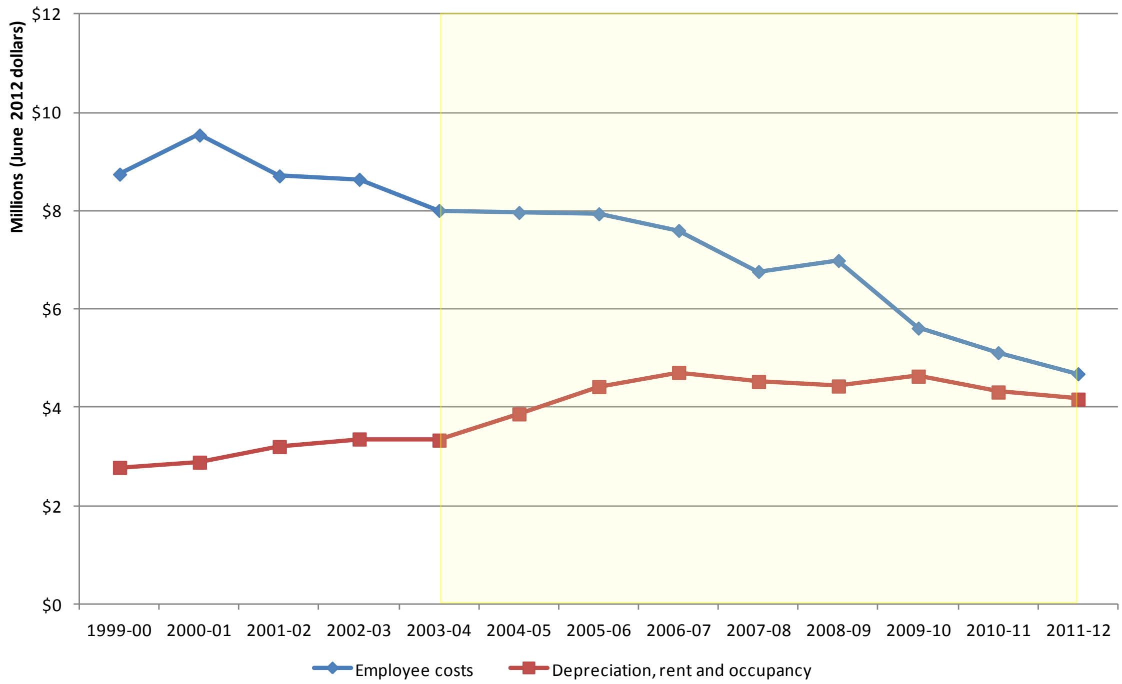
> employee costs—comprising salaries and wages expense, and employee on-costs

> depreciation, rent and occupancy expenses.

Other expenses, such as affiliation fees and licence fees have been excluded as these are not expected to be affected by the local content obligations.

The period shaded in yellow represents the financial year where local content obligations were introduced.

Figure 8: Major regional broadcasters—average expenses by broadcaster per region—regions with local content obligations

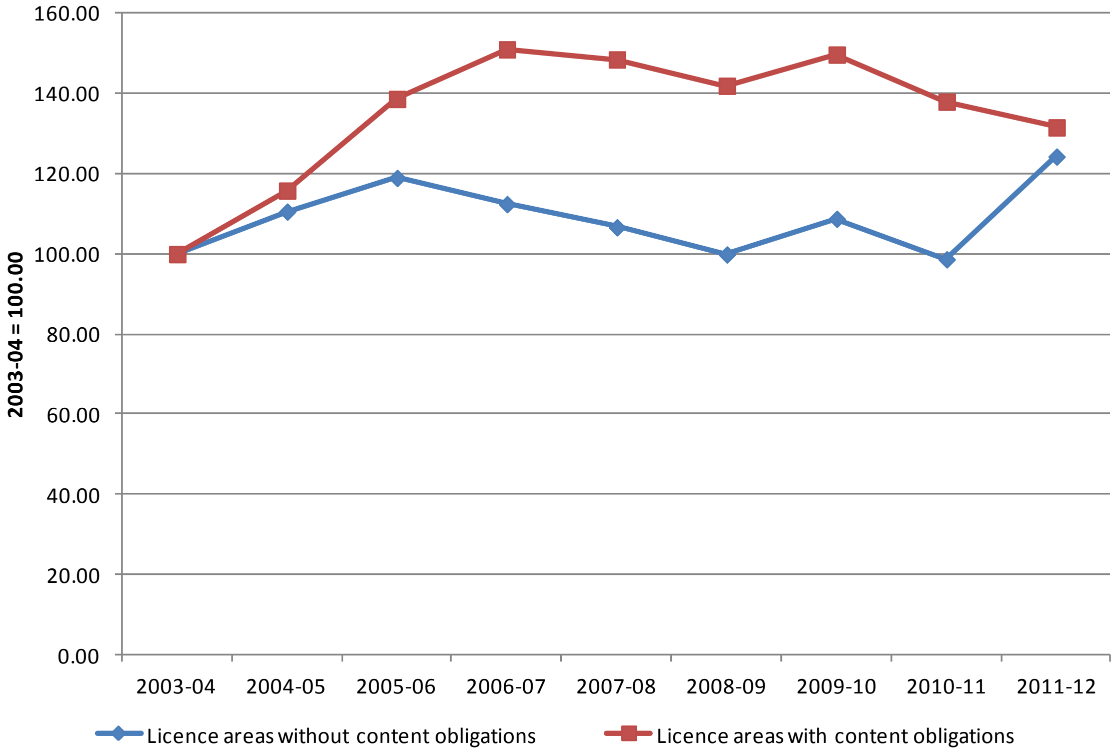


Source: ACMA, Television Activity Statements 1999-00 to 2011-12 and ABS, GDP Price deflator, A2303730T.

If you were to examine the expenses from 1999–2000 to 2011–12, it would appear that the introduction of local content obligation may have led to an initial shock in the initial years (that is, 2003–04 to 2005–06). Whether this shock led to a material difference between licence areas with local content obligations and without local content obligations can be examined by looking at data from 2003–04 to 2011–12.

Figure 9 illustrates that over the period in which local content obligations have been in place, the growth in depreciation, rent and occupancy costs has been slightly greater in licence areas where local content obligations have applied. In other words, if licence obligations had applied across all licence areas, costs relating to depreciation, rent and occupancy costs may have been slightly higher.

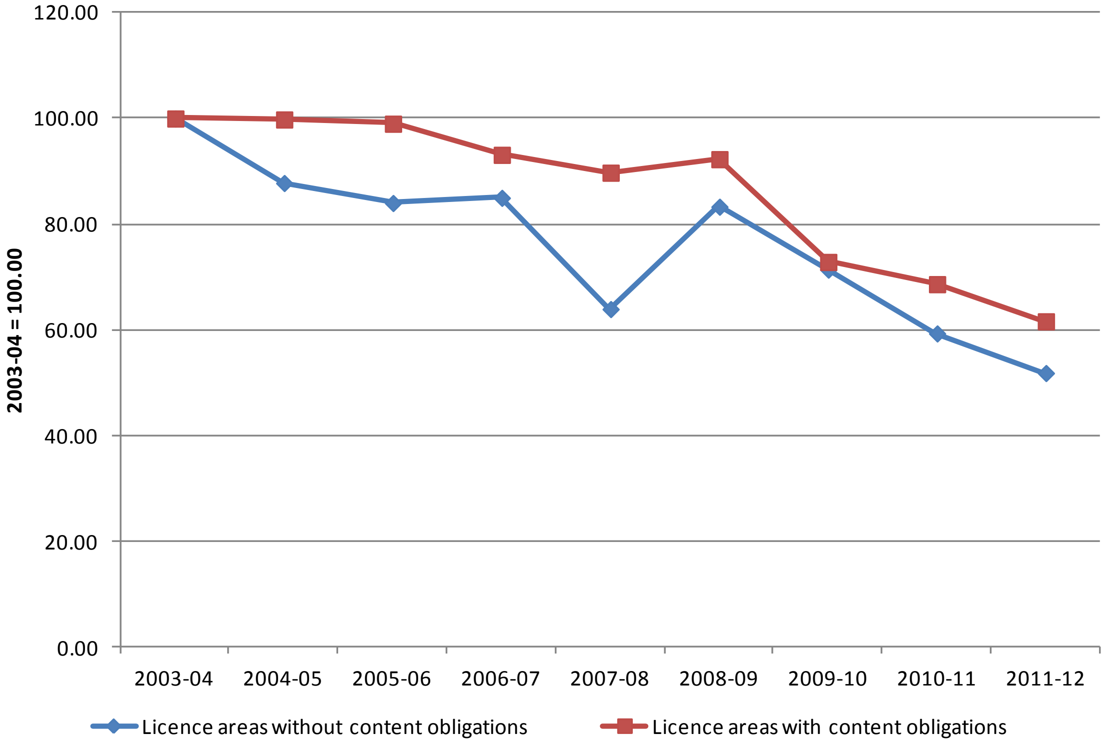
Figure 9: Change in depreciation, rent and occupancy costs—major regional broadcasters—change in costs since 2003–04



Source: ACMA analysis.

Figure 10 illustrates that employee costs have fallen less rapidly in regions with local content obligations compared to licence areas without the obligation, over the same period. What this suggests is that if local content obligations had applied to all licence areas, then employee costs may have been slightly higher.

Figure 10: Change in employee costs—major regional broadcasters—change in costs since 2003–04



Source: ACMA analysis.

Table 6 uses the differential in growth rates between regions with local content obligations to those without local content obligations to estimate how much higher the major regional broadcasters' expenses would have been had local content obligations applied across all regions. For a detailed explanation of the methodology used, refer to **Appendix B** of this report.

Table 6: Estimate of the cost of extending local content obligations to all licence areas for major regional broadcasters

	Depreciation, rent and occupancy costs	Employee costs	Combined costs[59]
Difference in cost growth[60] (A)	7.28%	9.78%	N/A
Average cost per broadcaster in regions without local content obligations (B)	$3,106,069	$4,447,052	$7,553,121
Average additional cost per broadcaster had local content obligations applied (A x B = C)	$226,179	$434,726	$660,905
Total average cost if obligation is extended (B + C)	$3,332,248	$4,881,778	$8,214,026

Source: ACMA analysis.

If you assume the difference in the change in expenses in licence areas since 2003–04 was solely due to local content obligations, then:

> Depreciation, rent and occupancy costs would have been 7.28 per cent higher in regions where local content obligations did not apply. This represents an additional cost of approximately $226,000 per annum on average per major regional broadcaster—increasing the cost per annum across licence areas without local content obligations from $3.1 million to $3.3 million per annum.

> Employee costs would have been 9.78 per cent higher in regions where local content obligations did not apply. This represents an additional cost of approximately $435,000 per annum on average per major regional broadcaster—increasing the cost per annum across licence areas without local content obligations from $4.5 million to $4.9 million per annum.

When you combine the two effects, this would have resulted in an additional cost of approximately $661,000 per annum on average per major regional broadcaster. This would have lead to the combined costs increasing from $7.6 million to $8.2 million per annum. It is worth noting the average service profit per broadcaster in 2011–12 was $51.4 million, and therefore the additional cost of $661,000 (assuming revenues are held constant) would represent approximately a one per cent reduction in service profits.

Costs of extending local content obligations using data obtained from submissions provided by regional broadcasters

In addition to examining the historical TAS data, the ACMA sought information from regional broadcasters on the costs of delivering local content. The cost information has been used to develop estimates of the cost of extending local content obligations.

Table 7 summarises the types of local content being provided by the major regional broadcasters. A detailed table is found in **Appendix A** of this report.

[59] Combined costs are calculated by adding depreciation, rent and occupancy costs with employee costs.
[60] This represents the difference in growth levels between regions with local content obligations to regions without local content obligations (2003–04 to 2011–12). For example, employee costs fell by 9.78 per cent less in regions with local content obligations than in regions without local content obligations over a nine-year period.

Table 7: Impact of extending local content obligations—major regional broadcasters

Broadcaster	Content obligation	Type of local content delivered	Licence areas	Impact on broadcaster
Prime	Yes	Bulletin & updates	> Southern NSW > Northern NSW > Regional Vic.	None
	No	Bulletin & updates	> Western Australia	Reduces flexibility and introduces opportunity costs
	No	None	> Mildura/ > Sunraysia	Increases costs, reduces flexibility and introduces opportunity costs
Southern Cross Austereo	Yes	Updates	> Southern NSW > Northern NSW > Regional Qld > Regional Vic.	None
	Yes	Bulletin	> Tasmania	None
	No	Updates	> Northern Territory > Remote Central & Eastern Australia > Regional Qld[61]	Reduces flexibility and introduces opportunity costs
	No	Bulletin	> Spencer Gulf > Broken Hill[62]	Reduces flexibility and introduces opportunity costs
	No	None	> Mount Isa > Spencer Gulf > Broken Hill[63]	Increases costs, reduces flexibility and introduces opportunity costs
WIN	Yes	Bulletin & updates	> Southern NSW > Regional Qld > Regional Vic. > Tasmania	None
	No	Bulletin & updates	> Regional Qld[64] > Mildura/ > Sunraysia	Reduces flexibility and introduces opportunity costs
	No	None	> Western Australia > Mount Gambier/South East > Riverland	Increases costs, reduces flexibility and introduces opportunity costs

Source: ACMA analysis.

Table 7 shows that there are six licence areas where no local content is being provided by at least one of the major regional broadcasters, these are:

[61] The local content obligation only requires licensees to provide local content for five of the seven local areas for the Regional Queensland commercial television licence area. As this broadcaster provides local content to seven local areas – two local areas are considered to be additional local content.

[62] Southern Cross operates channels 7, 9 and 10 in the Broken Hill/Spencer Gulf licence area. Only channel 7 provides local content.

[63] Southern Cross operates channels 7, 9 and 10 in the Broken Hill/Spencer Gulf licence area. Only channel 7 provides local content.

[64] The local content obligation only requires licensees to provide local content for five of the seven local areas for the Regional Queensland commercial television licence area. As this broadcaster provides local content to seven local areas – two local areas are considered to be additional local content.

> small licence areas—Mildura/Sunraysia and Mount Isa
> medium licence areas—Spencer Gulf, Mount Gambier/South East and Riverlands
> large licence areas—Western Australia.

Therefore extending local content obligations to these areas would increase costs for broadcasters. The size of the licence area (which is determined by the number of local areas within it) affects the magnitude of the initial costs incurred in providing local content. The number of local areas within each licence area affects the magnitude of the ongoing costs of delivering local content.

Using the average costs described in **Appendix C** of this report, the ACMA estimated the additional costs of meeting local content obligations on a per local area basis. Table 8 outlines different cost estimates of different sized licence areas, using the assumptions discussed in **Appendix C** of the report, where:

> a small licence area has one small local area
> a medium licence area has three medium-sized local areas
> a large licence area has four large licence areas.

Table 8: Additional costs of meeting local content obligations per licence area

Cost item	Small	Medium	Large
	$m	$m	$m
News updates			
Initial cost	3.4	4.9	6.4
Ongoing costs—annual cost	0.1	0.6	1.2

Source: ACMA analysis.

Table 9 provides estimates of the increase in costs per major regional broadcaster if local content obligations were extended to all licence areas.

The analysis in Table 9 assumes:

> local content obligations are extended across regional Australia
> the major regional broadcasters deliver the local content via 60 minutes of news updates per week[65]
> there would be an initial start-up cost[66] in each licence area where new local content would be required due to the extension of local content obligations
> in the licence areas where local content is provided it assumed no further ongoing costs are required
> the ongoing and initial, one-off costs will vary according to the size of the licence area described above.

[65] If you assume that the major regional broadcasters would implement news bulletins then the ongoing costs are likely to be five to six times higher.
[66] Regional broadcasters were asked to report on costs relating to establishing infrastructure where none is currently available in a licence area. In addition to these costs, regional broadcasters were asked to report any additional start up (capital) costs.

Table 9: Estimate of additional costs resulting from the extension of local content requirements using updates by major broadcaster

Broadcaster	Number of licence areas requiring additional local content	Number of local areas requiring additional content	Initial costs per broadcaster	Ongoing cost per broadcaster
			$m	$m
Prime	1	1	3.4	0.2
Southern Cross Austereo	3	3	10.2	0.6
WIN	3	6	13.2	1.2
Average per broadcaster	2.3	3.3	8.9	0.7

Source: ACMA analysis.

The ACMA has averaged the three broadcasters to obtain an understanding of how the additional costs might relate to the overall profitability of the businesses. A cost of $9.6 million in the first year (that is, combining $8.9 million with the $0.7 million ongoing cost) represents approximately a 17 per cent reduction in cash flows on average for each of the major broadcasters. If you assume that the $8.9 will be raised through borrowing funds, then the $0.7 million represents approximately a one per cent reduction in services profits on average per major regional broadcaster.

In addition to this impact on costs and profitability, extending local content obligations would restrict broadcasters' ability to reduce costs into the future. Given forecast declines in advertising revenues, this increases the burden of cost cutting on other areas of broadcasters' operations, restricting the programming they can offer viewers, and their ability to compete with other content providers (such as Pay TV).

Costs of extending local content obligations for the subsidiaries of the metropolitan broadcasters

Table 10 summarises the types of local content being provided by the subsidiaries of the metropolitan broadcasters. A detailed table is found in **Appendix A** of this report.

Table 10: Impact of extending local content obligations—metropolitan subsidiaries

Broadcaster	Content obligation	Type of local content delivered	Licence areas	Impact on broadcaster
Nine Network (Nine Darwin)	No	Bulletin & updates	> Northern Territory	Reduces flexibility and introduces opportunity costs
Nine Network (Newcastle Broadcast Network)	Yes	Bulletin & updates	> Northern NSW	None
	No	Bulletin & updates	> Northern NSW[67]	
Seven Queensland	Yes	Bulletin	> Regional Qld	None
	No	Bulletin & updates	> Regional Qld[68]	Reduces flexibility and introduces opportunity costs

Source: ACMA analysis.

Table 10 highlights that the main effect of extending local content obligations on the subsidiaries of the metropolitan broadcasters is to create a floor on the broadcasters' ability to reduce costs relating to delivering local content in two licence areas (Darwin and Regional Queensland) in the future.

Unlike the major regional broadcasters, the subsidiaries of the metropolitan broadcasters currently provide local content. Therefore, if local content obligations were extended, they would not incur additional ongoing costs or start-up costs. Therefore, extending the local content obligations to all regional licence areas would have little effect on the profitability of these broadcasters but may have implications for the businesses in the long-run resulting from losses in flexibility in reducing operating costs.

Costs of extending local content obligations for the other regional broadcasters

Table 11 summarises information the ACMA collated to obtain a snapshot of the types of local content being provided by the other regional broadcasters. A detailed table is found in **Appendix A** of this report.

[67] The local content obligation only requires licensees to provide local content for four of the five local areas for the Northern New South Wales commercial television licence area. As this broadcaster provides local content to five local areas – one local area is considered to be additional local content.

[68] The local content obligation only requires licensees to provide local content for five of the seven local areas for the Regional Queensland commercial television licence area. As this broadcaster provides local content to seven local areas – two local areas are considered to be additional local content.

Table 11: Impact of extending local content obligations—other regional broadcasters

Broadcaster	Content obligation	Type of local content delivered	Licence areas	Impact on broadcaster
Central Digital Television	No	None	> Mount Isa, > Remote Central & Eastern Australia	Increases costs, reduces flexibility and introduces opportunity costs
Darwin Digital Television	No	None	> Northern Territory	Increases costs, reduces flexibility and introduces opportunity costs
Eastern Australia Satellite Broadcasters	No	None	> Northern Australia > South East Australia	Increases costs, reduces flexibility and introduces opportunity costs
Imparja	No	Updates	> Remote Central & Eastern Australia	Reduces flexibility and introduces opportunity costs
Mildura Digital Television	No	None	> Mildura/ > Sunraysia	Increases costs, reduces flexibility and introduces opportunity costs
Tasmanian Digital Television	Yes	Updates	> Tasmania	None
WA Satco	No	None	> Western Australia	Increases costs, reduces flexibility and introduces opportunity costs
West Digital Television	No	Bulletin & updates	> Western Australia	Reduces flexibility and introduces opportunity costs

Source: ACMA analysis.

Table 11 shows that a majority of the other regional broadcasters do not currently provide local content. If local content obligations were to be extended to these broadcasters, this would impose significant additional costs for all but three of the regional broadcasters.

If it is assumed that local content obligations are applied across regional Australia, then each of the other regional broadcasters could face the following additional costs:

Table 13: Local content provided—cost estimate of extending local content requirements using updates

Broadcaster	Number of licence areas requiring additional local content	Number of local areas requiring additional content	Initial costs per broadcaster	Ongoing cost per broadcaster
			$m	$m
Central Digital	2	2	6.8	0.4
Darwin Digital	1	1	3.4	0.2
Eastern Australia Satellite Broadcasters	2	2	6.8	0.4
Mildura Digital	1	1	3.4	0.2
WA Satco	1	4	6.4	0.8
Average per broadcaster	1.4	2	5.4	0.4

Source: ACMA analysis.

Table 13 provides estimates of the costs of meeting the local content obligations. The ACMA has averaged the five broadcasters to obtain an understanding of how the additional costs might relate to the overall profitability of the businesses. A cost of $5.8 million in the first year would increase the average loss observed in 2011–12 from $0.2 million to $6 million. If you assume that the initial set up cost of $5.4 million will be raised through borrowing funds and not affect profitability, then the $0.4 million increase in ongoing costs represents approximately a tripling of annual losses.

The capital cost of $5.4 million per broadcaster would require a large injection of funds for the other regional broadcasters. This large increase in the capital base would have to be funded putting further strain on the financial risks associated with these businesses. These estimates indicate that the extension of local content obligations could result in the other regional broadcasters ceasing to operate or requiring further subsidies to continue operating.

Finally, it is worth noting that in all of the licence areas covered by the other regional broadcasters, at least one major regional broadcaster or subsidiary of a metropolitan broadcaster is currently providing local content. Therefore, the costs of extending local content obligations could outweigh the potential benefits.

Key findings

The ACMA observes that the costs of extending local content obligations would affect the different groups of the regional broadcasters as follows:

1. **Major regional broadcasters** (WIN, Prime and Southern Cross Austereo)—applying the first method, the ACMA estimates that extending the local content requirement to all licence areas covered by the major regional broadcasters would increase costs by $0.7 million per annum per broadcaster (on average in 2011–12 dollars), reducing profitability by around one per cent.

   Applying the second method, the ACMA estimates that extending the local content requirement to all licence areas covered by the major regional broadcasters would cost on average $9.6 million per broadcaster in the first year, with annual ongoing costs of $0.7 million thereafter. This compares with profitability per broadcaster of around $51 million in 2011–12. The high cost in the first year reflects the capital costs of meeting local content requirements, and the estimate assumes these are incurred and fully amortised in the first year.

   In addition to this impact on costs and profitability, extending local content obligations would restrict broadcasters' ability to reduce costs into the future by placing a floor on their costs relating to local content. Given forecast declines in advertising revenues, this increases the burden of cost cutting on other areas of broadcasters' operations, restricting the programming they can offer viewers, and their ability to compete with other content providers (such as Pay TV).

2. **Subsidiaries of the metropolitan broadcasters** (regional subsidiaries of Nine Network and Seven Network)—all of the licence areas served by the subsidiaries of the metropolitan broadcasters are subject to local content requirements, with the exception of Darwin and parts of Regional Queensland.[69] However, in these licence areas, the broadcasters provide local content. Therefore, extending the local content obligations to all regional licence areas would have little effect on the costs and the profitability of these broadcasters. That being said, like the major regional broadcasters, local content obligations could restrict the broadcasters' ability to reduce costs into the future.

[69] The local content obligation only requires licensees to provide local content to five of the seven local areas for the Regional Queensland commercial television licence area. As some broadcasters provide local content to seven local areas, the content provided to the two additional local areas is considered to be additional local content.

3. **Other regional broadcasters** (Imparja and joint ventures between the regional broadcasters)—the first method could not be applied as not all of the other regional broadcasters operated through a period pre-dating the imposition of local content obligations.

   Using the second method, the ACMA estimates that extending the local content requirement to all licence areas covered by the other regional broadcasters would cost on average $5.8 million per broadcaster in the first year, with annual ongoing costs of $400,000. The high cost in the first year reflects the capital costs of meeting local content requirements, and the estimate assumes these are incurred and fully amortised in the first year.

   These cost increases would threaten the long term viability of these broadcasters, who on average have made losses in each of the last five years. In 2011–12, the average loss was $200,000 per broadcaster, and therefore the higher ongoing costs of extending the local content requirements would result in a tripling of losses.

   It is also worth noting that in all of the licence areas covered by the other regional broadcasters, at least one major regional broadcaster or subsidiary of a metropolitan broadcaster is already providing local content. Therefore, the costs of extending local content obligations could outweigh the potential benefits.

Whether these impacts are realised will largely depend on how local content obligations are extended. For example, if local content obligations are:

> Extended to all of regional Australia and to all regional broadcasters, then the other regional broadcasters would experience the highest amount of additional costs in order to comply with the local content obligations. This option may affect the viability of other regional broadcasters.

> Extended to all regional broadcasters in specific regional markets (for example, Mildura/Sunraysia, Mount Gambier), then the impact on costs to broadcasters would vary depending on whether all of the broadcasters operating within the region were already providing local content.

> Extended across all licence areas with obligations imposed on licensees owned by the major regional broadcasters only, then the costs of meeting the local content obligation are likely to have a small impact on profitability in the short-term (that is, about one per cent of net profits). However, this may restrict the ability of the regional broadcasters to reduce costs into the future.

.

Appendix A—Level of local content provided[70]

The ACMA has collated the most common types of local content being provided by regional broadcasters when meeting the regulatory local content obligation. The purpose of this appendix is to provide a snapshot of the local content types being provided by regional broadcasters.

Table A1 Licence areas with regulatory local content obligation

LICENCE AREA	LOCAL AREA	CALLSIGN/LICENSEE	NEWS BULLETIN (Mon to Fri)	NEWS BULLETIN (Sat to Sun)	NEWS UPDATES (Mon to Fri)	CSAs[71]	OTHER
Southern NSW	**Central Tableland & Central Western Slopes**	CTC/ Australian Capital Television Pty Ltd (Southern Cross Austereo)			✓	✓	
		CBN/ Prime Television (Southern) Pty Ltd	✓		✓	✓	✓
		WIN/ WIN Television NSW Pty Ltd	✓		✓	✓	✓[72]
	ACT & Southern tablelands	CTC/ Australian Capital Television Pty Ltd (Southern Cross Austereo)			✓	✓	
		CBN/ Prime Television (Southern) Pty Ltd			✓	✓	✓
		WIN/ WIN Television NSW Pty Ltd	✓		✓	✓	✓
	South Western Slopes & Eastern Riverina	CTC/ Australian Capital Television Pty Ltd (Southern Cross Austereo)			✓	✓	
		CBN/ Prime Television (Southern) Pty Ltd	✓		✓	✓	✓

[70] A number of regional commercial television broadcasters broadcast content that may be considered material of local significance (local content) for the purposes of the licence condition but have not been captured in this appendix. Additional material not identified may include weather, sport or stock updates, weekend news updates or programs/episodes which contain local content, such as sporting or lifestyle programs. Data is current as at November 2013.

[71] Although most broadcasters generally broadcast community service announcements (CSA's), not all count them towards meeting their local content obligations.

[72] WIN also broadcasts programs across all licence areas of regional Australia, wherein certain episodes may meet local content obligations, such as *Alive & Cooking* and *Fishing Australia*. WIN also broadcasts annual programming events such as *Gympie Muster* and other region specific programming.

LICENCE AREA	LOCAL AREA	CALLSIGN/LICENSEE	NEWS BULLETIN (Mon to Fri)	NEWS BULLETIN (Sat to Sun)	NEWS UPDATES (Mon to Fri)	CSAs[71]	OTHER
		WIN/ WIN Television NSW Pty Ltd	✓[73]		✓	✓	✓
	Illawarra & South Coast	CTC/Australian Capital Television Pty Ltd (Southern Cross Austereo)			✓	✓	
		CBN/ Prime Television (Southern) Pty Ltd			✓	✓	✓
		WIN/ WIN Television NSW Pty Ltd	✓		✓	✓	✓
Northern NSW	**Richmond/Tweed**	NBN/ NBN Ltd (Nine Network)[74]	✓	✓	✓	✓	✓
		NRN/ Northern Rivers Television Pty Ltd (Southern Cross Austereo)			✓	✓	
		NEN/ Prime Television (Northern) Pty Ltd	✓		✓	✓	✓
	North West Slopes & Plains	NBN/ NBN Ltd (Nine Network)	✓	✓	✓	✓	✓
		NRN—Northern Rivers Television Pty Ltd (Southern Cross Austereo)			✓	✓	
		NEN—Prime Television (Northern) Pty Ltd	✓		✓	✓	✓
	Northern Rivers & Mid North coast	NBN/ NBN Ltd (Nine Network)	✓	✓	✓	✓	✓
		NRN/ Northern Rivers Television Pty Ltd (Southern Cross Austereo)			✓	✓	
		NEN/ Prime Television (Northern) Pty Ltd	✓		✓	✓	✓
	Hunter	NBN/ NBN Ltd (Nine Network)	✓	✓	✓	✓	✓

[73] Included in this news bulletin are two stories per day from licence area Griffith and MIA, a licence area not subject to local content obligations.

[74] The local content obligation only requires licensees to provide local content for four of the five local areas for the Northern New South Wales commercial television licence area. The broadcaster is not required to provide local content to this local area – this is considered to be additional local content.

LICENCE AREA	LOCAL AREA	CALLSIGN/LICENSEE	NEWS BULLETIN (Mon to Fri)	NEWS BULLETIN (Sat to Sun)	NEWS UPDATES (Mon to Fri)	CSAs[71]	OTHER
		NRN/ Northern Rivers Television Pty Ltd (Southern Cross Austereo)			✓	✓	
		NEN/ Prime Television (Northern) Pty Ltd			✓	✓	✓
	Central Coast	NBN/ NBN Ltd (Nine Network)	✓	✓	✓	✓	✓
Regional Queensland	**Far North Queensland**	RTQ/ WIN Television Qld Pty Ltd	✓		✓	✓	✓
		STQ/ Channel Seven Queensland Pty Ltd	✓			✓	✓
		TNQ/ Regional Television Pty Limited (Southern Cross Austereo)			✓	✓	
	North Queensland	RTQ/ WIN Television Qld Pty Ltd	✓		✓	✓	✓
		STQ/ Channel Seven Queensland Pty Ltd	✓			✓	✓
		TNQ/ Regional Television Pty Limited (Southern Cross Austereo)			✓	✓	
	Central Coast & Whitsundays	RTQ / Win Television Qld Pty Ltd[75]	✓		✓	✓	✓
		STQ/ Channel Seven Queensland Pty Ltd	✓		✓	✓	✓
		TNQ/ Regional Television Pty Limited (Southern Cross Austereo)			✓	✓	

[75] The local content obligation only requires licensees to provide local content for five of the seven local areas for the Regional Queensland commercial television licence area. The broadcaster is not required to provide local content to this local area – this is considered to be additional local content.

LICENCE AREA	LOCAL AREA	CALLSIGN/LICENSEE	NEWS BULLETIN (Mon to Fri)	NEWS BULLETIN (Sat to Sun)	NEWS UPDATES (Mon to Fri)	CSAs[71]	OTHER
	Capricornia	RTQ/ WIN Television Qld Pty Ltd	✓		✓	✓	✓
		STQ/ Channel Seven Queensland Pty Ltd[76]	✓		✓	✓	✓
		TNQ/ Regional Television Pty Limited (Southern Cross Austereo)			✓	✓	
	Wide Bay	RTQ/ WIN Television Qld Pty Ltd[77]	✓		✓	✓	✓
		STQ/ Channel Seven Queensland Pty Ltd	✓		✓	✓	✓
		TNQ/ Regional Television Pty Limited (Southern Cross Austereo)[78]			✓	✓	
	Sunshine Coast	RTQ/ WIN Television Qld Pty Ltd	✓		✓	✓	✓
		STQ/ Channel Seven Queensland Pty Ltd	✓		✓	✓	✓
		TNQ/ Regional Television Pty Limited (Southern Cross Austereo)[79]			✓	✓	
	Darling Downs	RTQ/ WIN Television Qld Pty Ltd	✓		✓	✓	✓
		STQ/ Channel Seven Queensland Pty Ltd[80]				✓	✓

[76] ibid.
[77] ibid.
[78] ibid
[79] ibid
[80] ibid.

LICENCE AREA	LOCAL AREA	CALLSIGN/LICENSEE	NEWS BULLETIN (Mon to Fri)	NEWS BULLETIN (Sat to Sun)	NEWS UPDATES (Mon to Fri)	CSAs[71]	OTHER
		TNQ/ Regional Television Pty Limited (Southern Cross Austereo)			✓	✓	
Regional Victoria	**Goulburn Valley & Upper Murray**	AMV/ Prime Television (Victoria) Pty Ltd	✓		✓	✓	✓
		GLV/ Southern Cross Communications Pty Limited	✓		✓	✓	
		VTV/ WIN Television Vic Pty Ltd	✓		✓	✓	✓
	North Central Victoria	AMV/ Prime Television (Victoria) Pty Ltd			✓	✓	✓
		BCV/ Southern Cross Communications Pty Limited			✓	✓	
		VTV/ WIN Television Vic Pty Ltd	✓		✓	✓	
	South West Victoria	AMV/ Prime Television (Victoria) Pty Ltd			✓	✓	✓
		BCV/ Southern Cross Communications Pty Limited			✓	✓	
		VTV/ WIN Television Vic Pty Ltd	✓		✓	✓	✓
	Gippsland	AMV/ Prime Television (Victoria) Pty Ltd			✓	✓	✓
		GLV/ Southern Cross Communications Pty Limited			✓	✓	
		VTV/ WIN Television Vic Pty Ltd	✓		✓	✓	✓
Tasmania	**Tasmania**	TNT/ Southern Cross Television Pty Ltd	✓	✓			
		TVT/ WIN Television Tas Pty Ltd	✓	✓	✓	✓	✓

LICENCE AREA	LOCAL AREA	CALLSIGN/LICENSEE	NEWS BULLETIN (Mon to Fri)	NEWS BULLETIN (Sat to Sun)	NEWS UPDATES (Mon to Fri)	CSAs[71]	OTHER
		TDT /Tasmanian Digital Television Ltd (Southern Cross Austereo and WIN joint venture)			✓	✓	

Table A2 Licence areas with no regulatory local content obligation, where local content is being provided.

LICENCE AREA	LOCAL AREA	CALLSIGN/LICENSEE	NEWS BULLETIN (Mon to Fri)	NEWS BULLETIN (Sat to Sun)	NEWS UPDATES (Mon to Fri)	CSAs	OTHER
Western Australia	**Kalgoorlie**	VEW/ Mid-Western Television Pty Ltd (Golden West Network—Prime) / VDW— West Digital Television (Prime and WIN joint venture)	✓		✓	✓	✓
	South West & Great Southern	SSW/ Golden West Network Pty Limited (Prime) SDW/ West Digital Television (Prime and WIN joint venture)	✓		✓	✓	✓
	Geraldton	GTW /Geraldton Telecasters Pty Ltd (Prime) GDW/ West Digital Television (Prime and WIN joint venture)	✓		✓	✓	✓
	Western Zone	WAW/ Golden West Satellite Communications Pty Ltd (Prime) WDW/ West Digital Television (Prime and WIN joint venture)	✓		✓	✓	✓
Northern Territory	**Darwin**	TND/ Regional Television Pty Limited (Southern Cross Austereo)			✓		
Remote Central and Eastern Australia	**Remote Central and Eastern Australia**	IMP/ Imparja Television Pty Ltd			✓	✓	✓[81]
		QQQ/ Regional Television Pty Limited (Southern Cross Austereo)			✓		
Regional Victoria	**Mildura/Sunraysia**	STV/ WIN Television Mildura Pty Ltd	✓		✓	✓	✓

[81] Imparja's other programming include, for example, Indigenous programs such as *Nganamapa Anwernekehne*, *Yamba's Playtime* and *Outback Tracks*, as well as sporting events like the *Intrust Super Cup*. Imparja also broadcasts weather, stock and sport updates.

LICENCE AREA	LOCAL AREA	CALLSIGN/LICENSEE	NEWS BULLETIN (Mon to Fri)	NEWS BULLETIN (Sat to Sun)	NEWS UPDATES (Mon to Fri)	CSAs	OTHER
Spencer Gulf/ Broken Hill	**Spencer Gulf/ Broken Hill**	GTS/ Spencer Gulf Telecasters Pty Limited/ BKN/ Broken Hill Television Pty Limited (Southern Cross Austereo)	✓[82]				

[82] This is news bulletin is a combined service for both Spencer Gulf and Broken Hill.

Table A3 Regional broadcasters that do not provide local content, with no obligation to do so.[83]

NETWORK	CALLSIGN/LICENSEE	LICENCE AREA
Southern Cross Austereo	IDQ/Central Digital Television Pty Ltd	Mount ISA (Queensland)
Southern Cross Austereo	ITQ/Regional Television Pty Limited	Mount ISA (Queensland)
Southern Cross Austereo	VAN/Eastern Australia Satellite Broadcasters Pty Ltd (Network Ten and Seven Network joint venture)	Northern Australia
Southern Cross Austereo	VAS/Eastern Australia Satellite Broadcasters Pty Ltd (Network Ten and Seven Network joint venture)	South East Australia
Southern Cross Austereo	CDT/Central Digital Television Pty Limited	Remote Central & Eastern Australia
Southern Cross Austereo	BDN/Broken Hill television Pty Limited	Broken Hill (New South Wales)
Southern Cross Austereo	SCN /Broken Hill Television Pty Limited	Broken Hill (New South Wales)
Southern Cross Austereo	SGS/Spencer Gulf Telecasters Pty Limited	Spencer Gulf (South Australia)
Southern Cross Austereo	DTD/Darwin Digital Television Pty Limited	Darwin (Northern Territory)
WIN Television	WIN Television WA Pty Ltd	Remote and regional Western Australia (Western Australia)
WIN Television	WIN Television SA Pty Ltd	Mount Gambier/South East/Riverland (South Australia)
Prime	PTV/Prime Television (Victoria) Pty Ltd [Mildura/Sunraysia]	Mildura/Sunraysia (Victoria/New South Wales)

[83] Under Clause 7D to Schedule 2 of the Broadcasting Services Act 1992 (BSA), certain Viewer Satellite Access Television (VAST) services are required to broadcast local news provided by regional commercial television licensees under section 43AA of the BSA. Section 43AA requires section 38C regional commercial television broadcasting licensees to make available their regional news to be carried on VAST, with some exceptions for Western Australia and regional commercial television broadcasting licensees who supply their own regional news via satellite services.

Appendix B—Methodology used to estimate costs of extending local content obligations using historical data

The purpose of this analysis is to examine what impact (if any) local content obligations had on the regional broadcasters' business models. Local content obligations were introduced in 2003–04[84] in response to station closures which occurred from 1999 to 2001.[85]

The analysis in this section draws on the historical TAS data:

> covering a period where local content obligations were introduced in 2003–04[86] in response to station closures which occurred from 1999 to 2001.[87]

> for the three major regional broadcasters. The analysis was based on the costs of the three major regional broadcasters. To protect commercially sensitive information, this analysis was not conducted for the subsidiaries of the major metropolitan broadcasters. Other regional broadcasters are not included in this analysis as they either did not operate for the entire period or did not have operations in locations where local content obligations were introduced. Therefore, the ACMA would caution against using the percentages calculated in this section to either the subsidiaries of the metropolitan broadcasters or the other broadcasters.

The analysis also examines costs of the three major regional broadcasters from 1999–2000 to 2011–12 for the licence areas where local content obligations were imposed. The ACMA has calculated the average expenditures across the major regional broadcasters by aggregating expenses which could be attributed to labour inputs (salaries and wages, and employee on-costs) and capital inputs (depreciation and amortisation, and rent and occupancy expenses).

These two broad categories were then calculated into an average licence area expense by broadcasters (that is, the total costs of each broadcaster are divided by the number of licence areas the broadcaster is operating within). The reason for taking this approach is:

> the number of licence areas which the broadcasters operate in changes over time due to changes in ownership in regional television licences

---

[84] ABA, *Broadcasting Services (Additional Television Licence Condition) Notice 7 April 2003*, ABA Notice, 7 April 2003.

[85] News bureaux in Canberra, Cairns, Townsville, Darwin and Alice Springs were closed by Southern Cross Broadcasting (Australia) Limited in November 2001. This followed similar closures by Prime Television Ltd in Canberra, Newcastle and Wollongong in June 2001.See ABA, *Adequacy of local news and information programs on commercial television services in Regional Queensland, Northern NSW, Southern NSW and Regional Victoria (aggregated markets A, B, C and D)*, ABA report, August 2002, p. 9.

[86] ABA, *Broadcasting Services (Additional Television Licence Condition) Notice 7 April 2003*, ABA Notice, 7 April 2003.

[87] News bureaux in Canberra, Cairns, Townsville, Darwin and Alice Springs were closed by Southern Cross Broadcasting (Australia) Limited in November 2001. This followed similar closures by Prime Television Ltd in Canberra, Newcastle and Wollongong in June 2001.See ABA, *Adequacy of local news and information programs on commercial television services in Regional Queensland, Northern NSW, Southern NSW and Regional Victoria (aggregated markets A, B, C and D)*, ABA report, August 2002, p. 9.

> the licence areas covered by major regional broadcasters vary in geography and population—however, this data was not available for each of the years recorded in the analysis.

Therefore, the ACMA wanted to ensure that the trends observed in the data were not being driven by changes in the number of licence areas or differences in geography between licence areas. To accomplish this, the number of licence areas from year-to-year was considered as a proxy.

The analysis compares:

1. The level of expenses in licence areas with local content obligations in the period prior to the introduction of local content obligations (1999–2000 to 2003–04), to the period after the obligations were imposed (2003–04 onwards). If the trends in the costs changes between these periods then it could be argued that local content obligations had an impact on the major regional broadcasters' costs.
2. The change in average expenses by broadcaster in licence areas with local content obligations, to licence areas without local content obligations. To do this, the ACMA calculated the change in the labour and capital expenses from 2003–04 (when local content obligations were introduced) to 2011–12. This approach was used to estimate the additional cost of extending local content obligations to major regional broadcasters.

With the second part of the analysis the ACMA has calculated how much more the major regional broadcasters would have had to spend if the local content obligations applied to all licence areas. This is done by (for both labour and capital costs):

1. Calculating the percentage change in costs (from 2003–04 to 2011–12) for licence areas **with** local content obligations. (A)
2. Calculating the percentage change in costs (from 2003–04 to 2011–12) for licence areas **without** local content obligations. (B)
3. Subtracting (B) from (A) to obtain the difference in growth rates. (C)
4. Calculating a nine-year average (2003–04 to 2011–12) of the costs by broadcaster. (D)
5. Multiplying (C) by (D) to estimate the additional ongoing cost which would have resulted if local content obligations were applied across all licence areas.

Appendix C—Local content—cost per licence area

Appendix C outlines how the ACMA developed estimates of the costs of delivering local content. The cost estimates for the delivery of news updates were then used as the basis of estimating the cost of extending local content obligations. **Annexure A** provides a detailed outline of the methodology used to obtain the estimates in **Appendix C**.

Cost of delivering local content via news bulletins

The ACMA received submissions from regional broadcasters outlining how they deliver local content via news bulletins. The approach generally involves:

> A 30 minute bulletin, which contains five to 25 minutes pertaining to the local/licence area. Most news bulletins offer about 20 minutes of local content five days a week.

> Updates throughout the day lasting about one minute, of which only 68 minutes per week contain new content.

News bulletins generally involve a news bureau being located in the licence area where news items are sourced, shot, written and edited by the local bureau staff, and supplied to the central studio for production of the program. The news updates are gathered in local areas where a local journalist scripts the required updates and submits them to a centralised news editor, which are then presented from a central location.

The average cost of delivering local content and resources required by the regional broadcasters using this delivery model on a local area basis are (assuming a range of 20 to 25 minute bulletins delivered five times a week, with one minute updates throughout the week):

> Approximately 11 to 13 staff to deliver the news bulletin at a cost of $398,000 to $498,000 per year per local area.[88]

> Approximately 1.5 staff members to deliver the news update at a cost of $144,000 per year.

This equates to annual costs on average of $542,000 (20 minutes of local content per bulletin) to $642,000 (25 minutes of local content per bulletin) per year involving 12 to 14 staff to deliver at least five bulletins per week with updates throughout the week within a local area. To estimate a cost for the licence area, you would multiply this amount by the number of local areas with unique news bulletins. For example, if three local areas are within the licence area then the cost of delivering the news bulletin and updates model is between $1.6 million and $1.9 million, using 36 to 52 staff.

The regional broadcasters which have adopted this approach generally offer local content well above the regulatory local content obligations. The local content obligation requires each regional broadcaster to accumulate at least 90 points of local content per week within each local area and at least 720 points of local content in each local area over a six week period (an average of 120 points per week). One point

[88] The ACMA calculated annual wage cost using numbers in the MEAA award for the purposes of ensuring that the number of staff does not result in wage amount that exceeds the annual cost. See MEAA, *Broadcasting and recorded entertainment award 2010*, Award, December 2012, pp. 19-20. <www.alliance.org.au/award-summaries/download-document/broadcasting-and-recorded-entertainment-award-2010>, accessed 23 August 2013.

is awarded for each minute of local content required; with the exception of local news which is awarded two points per minute broadcast. For example, offering 20 minutes of local content via a news bulletin five days a week would result in 200 points per week being awarded, which is above the 120 point requirement. This is without including the one minute updates.

Cost of delivering local content via news updates

At the other end of the spectrum of delivering local content is delivering local content through one minute updates throughout the week. The news updates are gathered in local areas where a local journalist scripts the required updates and submits them to a centralised news editor, which are then presented from a central location.

Currently the regional broadcasters using news updates to deliver local content range from providing 60 to 400 minutes[89] per week in licence areas with local content obligations. Using the scheme described above, this would equate to 120 (content on licence area) to 800 (content on local area) points being accrued per week. In some areas this would meet the 120 point weekly average requirement, while in other areas it significantly exceeds the level of content required.

The average cost of delivering local content and resources required by the regional broadcasters using this delivery model are (assuming a range of 200 to 400 minutes worth of updates delivered throughout the week):

> Approximately a cost of $194,000 (that is, 60 minutes) to $1.3 million (that is, 400 minutes) per year to deliver local content via news updates to the local area.

> Approximately one to 12 staff members to deliver the news update.

It is worth pointing out:

> That where regional broadcasters are required to provide local content in a geographically large region, say for example northern Western Australia, then it is more likely that three staff members would be required to obtain news from across the region; with costs reflected somewhere in the middle of this range being more applicable.

> The number of staff required to produce local content under the news updates as a standalone service (up to 12 staff) compared to the number of staff allocated to news updates under the news bulletin approach (that is, 1.5 staff working on updates) is higher. The reason for this is that a regional broadcaster which provides news bulletins is able to allocate staff working on news bulletins to also assist with producing the news updates.

Cost of meeting minimum local content obligations

The largest cost in delivering local content is the initial cost of setting up the local news service. The ACMA received two submissions from the regional broadcasters which reported the initial costs of providing local content to additional licence areas. The average of these costs was $4.9 million per licence area per regional broadcaster. As the estimate involved two submissions covering three regional broadcasters, it is possible that this average could be overstating or understating the initial costs of delivering local content, depending on the circumstances of the regional broadcaster.

The ACMA did not have sufficient information to calculate initial (that is, set-up) costs on a local area basis. The submissions provided only noted the number of licence areas the initial costs applied to. That being said, each of the licence areas varied significantly in terms of land size and population. This informed the use of a 30 per

[89] Note this is an aggregated amount which relates to multiple local areas. For example, four local areas would receive 100 minutes of local content per week.

cent adjustment to average costs for the low and high ranges. The range stated below includes the range of initial costs reported by the regional broadcasters.

The assumed initial costs for different types of licence areas were calculated as follows:

- only one local area, low initial costs ($3.4m) are applied
- two to three local areas, medium initial costs ($4.9m) are applied
- four or more local areas, high initial costs ($6.4m) are applied.

Using the data received from submissions provided by the regional broadcasters, the ACMA estimated the costs per licence area of delivering local content through 60 news updates delivered throughout the week containing one minute of local content on average. This is assumed to be the lowest cost option of meeting local content obligations, as the data received consistently reported it to be lower in ongoing costs than using news bulletins.

The costs in **Appendix C** have been used to estimate the additional costs regional broadcasters would face if local content obligations were extended across regional Australia. Table C1 provides a range of estimates for the annual ongoing costs of delivering local content, depending on the size of the local area.

Table C1 Ongoing costs of meeting local content obligations by size of the local area

Cost item	Small	Medium	Large
	$m	$m	$m
News updates			
Ongoing costs—annual cost	0.1	0.2	0.3

Source: ACMA analysis.

The ACMA has made an allowance of 30 per cent on the average ongoing costs per 60 minutes of news updates per local area to account for the fact that local areas differ in size. This has been informed by the data provided by the regional broadcasters. The low scenario represents a 30 per cent reduction from the average and the high scenario represents a 30 per cent increase.

Table C2 outlines different costs estimates of different sized licence areas, using the assumptions outlined above on the initial costs and annual ongoing costs of delivering local content, where:

- a small licence area has one small local area
- a medium licence area has three medium sized local areas
- a large licence area has four large local areas.

Table C2 Summary of current costs for meeting local content conditions by licence area

Cost item	Small	Medium	Large
	$m	$m	$m
News updates			
Initial cost	3.4	4.9	6.4
Ongoing costs—annual cost	0.1	0.6	1.2

Source: ACMA analysis.

For example, a regional broadcaster operating in a medium sized licence area with three medium sized local areas would incur an initial cost of $4.9 million and ongoing annual costs of $0.6 million to deliver 60 minutes of news updates.

Annexure A—Methodology

To estimate the number of additional staff and costs required to deliver local content, the ACMA requested from regional broadcasters data on:

> staff numbers
> costs involved in setting up a new service (initial costs and additional capital costs)
> ongoing operational expenditure (for example, wages, rent, etc.)
> amortisation (where known)
> number of local areas covered (or alternatively number of licence areas where number of local areas was unknown)
> number of minutes related to the delivery of local content.

The ACMA notes that one of the limitations of the data provided by the regional broadcasters is that some of the regional broadcasters provided information on depreciation and amortisation while other broadcasters did not provide this information. Therefore, the ACMA chose not to make assumptions about the split between ongoing labour and capital costs in estimating the cost of delivering local content.

The ongoing cost data provided by the regional broadcasters was converted into a common unit of measurement (for example, the annual cost of delivering local content divided by the number of minutes of local content per year and by the number of local areas covered).

The staffing and cost information gathered differentiated between news bulletins, news updates and other content. The unit costs were therefore calculated for each individual regional broadcaster according to these three groupings which were then converted into averages and also examined to inform ranges (in terms of average costs and the number of minutes).

Another area which broadcasters varied was in the quantity of minutes provided for news bulletins (that is, between 20 and 25 minutes). Therefore, to estimate the costs of the different local content models being currently delivered by regional broadcasters, two different costs were estimated to reflect the differences in the number of minutes.

The cost estimates developed by the ACMA and the cost data provided has been reconciled with information from other sources, such as:

> TASs lodged by the regional broadcasters
> wages and rates quoted in public sources (such as the Awards and Agreements lodged on the Media, Entertainment and Arts Alliance (MEAA) website).

The ACMA has taken a best endeavours approach to ensure that the information provided by regional broadcasters is accurate. For example, where costs in specific licence areas were higher than other regions, the ACMA sought an explanation from the regional broadcaster for the reasons behind this.[90] However, as with the data submitted in the TASs, the information provided has not been audited. In addition,

[90] It is worth noting that the ACMA decided to remove one observation from the analysis as the costs and minutes provided did not appear to be reasonable as the number of minutes were well below other submissions and the cost of delivering the local content was well above the other submissions and one of the own submitter's numbers.

there may be differences between regional broadcasters in the approach taken to allocating the costs of delivering local content.

Glossary

Term	Description
$	Australian dollars
‘000	Thousands
ABA	The Australian Broadcasting Authority
The ACMA	The Australian Communications and Media Authority
The Act	The *Broadcasting Services Act 1992*
CAGR	Compound annual growth rate
CPI	Consumer Price Index
Debt to assets	Total liabilities as a proportion of total assets. Provides an indication of the level of financial risk associated with the business. Unlike equity where the business can reduce its dividends to the owners, in the event of a downturn of the economy, the business must continue to pay money owed to debtors.
Debt to EBITDA	Estimates a business’ debt repayment capacity. It provides an estimate of the number of years it would take to repay the debt owed in any given year given the gross profit earned in the same year. Therefore, the number represents an estimate of the number of years it would take to repay debt. The lower the ratio, the greater capacity for business to repay debt and subsequently a lower level of financial risk.
DVD	Digital Versatile Disc
Employee costs	The sum of salaries, wages and employee on-costs
EBITDA	Earnings before interest, tax, depreciation and amortisation
GFC	Global Financial Crisis
GDP	Gross Domestic Product
Imparja	Imparja Television
KPMG	Klynveld Peat Marwick Goerdeler
MEAA	Media Entertainment and Arts Alliance
Prime	Prime Media Group
Profit margin	Profits measured as a percentage of total costs/expenditure
PwC	Pricewaterhouse Coopers
Quick ratio	Ratio of current assets to current liabilities. Measures the ability of a company to use its near cash or quick assets to extinguish or retire its current liabilities immediately. This provides an indication of a business’s ability to meet short-term obligations.
RBA	Reserve Bank of Australia
Real dollars	The amounts are converted into a base year, which removes the effect of inflation from the dollar values.
Return on assets	Profits expressed as a percentage of total assets

Term	Description
TASs	Television Activity Statements—holders of commercial television broadcasting licences are required to provide a licence fee return under the *Broadcasting Services Act 1992* by 31 December each. Contained within this statement is information relating revenues, expenses, assets and liabilities.
Total Service Expenses	Total expenses incurred by the broadcaster as part of its commercial television broadcasting operations.
Total Service Revenues	Total revenues received by the broadcaster as part of its commercial television broadcasting operations.
TWS	Total Welfare Standard
VAST	Viewer Access Satellite Television
WA	Western Australia
WIN	WIN Corporation

Attachment A—Peer review—Frontier Economics

Peer review of "Economic analysis of regional commercial television broadcasters"

A NOTE FOR THE ACMA

1 Frontier Economics has been asked by the Australian Communications and Media Authority (ACMA) to undertake a peer review of the methodology and quantitative modelling analysis supporting its report titled "Economic analysis of regional commercial television broadcasters" (the ACMA report).

2 The ACMA report has two parts to it:

- First, it considers the economic circumstances currently facing commercial television broadcasting licensees operating in regional areas of Australia
- Second, it seeks to estimate the costs of extending local content requirements to other parts of regional Australia.

3 We believe the methodological approaches taken by the ACMA to considering both of these questions are broadly sensible. While the analysis has at times required the ACMA to make a number of simplifying assumptions, this is consistent with many quantitative modelling exercises. We have also reviewed the spreadsheet models relied upon by the ACMA when making the estimations contained in its report. Where we found errors in the calculations, these were minor in nature and have been corrected by the ACMA in subsequent estimations.

4 In making its estimations, we note that the ACMA has relied heavily on material and data provided to it by the regional broadcasters. In a small number of instances, the data provided by some of these broadcasters contains anomalies. We do not believe believes these anomalies are likely to inappropriately bias the results of the ACMA's analysis. We observe that the ACMA appropriately notes the limitations with the data it has relied upon when making its estimations, and we would echo these comments by the ACMA.

5 The remainder of this note sets out in more detail our findings in relation to the methodological and modelling analysis conducted by the ACMA for each of the two parts of its report referred to in para [2] above.

1. Analysis of economic circumstances

6 In order to assess the economic circumstances presently facing commercial television broadcast licensees operating in regional Australia, the ACMA looks at trends over recent years regarding revenues and costs for regional broadcasters.

Based on this, the ACMA is able to estimate trends in the return on assets for these broadcasters. This return on assets is then considered – having regard to the gearing levels of regional broadcasters – to assess the profitability of regional broadcasters.

7 Once returns over recent periods are estimated, the ACMA then considers forecasts of revenues and costs to see whether there is likely to be an improvement or worsening of economic conditions. These assessments are made for three different types of regional broadcaster – major regional broadcasters; subsidiaries of the metropolitan broadcasters; and other smaller regional broadcasters.

8 Generally speaking, this seems a sensible approach to analyse the economic circumstances presently facing regional broadcasters. We have also reviewed the estimates made by the ACMA and have found no errors in its calculations.[1] We agree with its conclusions that:

- The evidence suggests advertising revenues are falling for the industry as a whole
- Returns on assets are low for regional broadcasters relative to other available investments and the level of risk facing these broadcasters.

9 We observe, however, two factors that should be borne in mind when interpreting the results of the ACMA's analysis:

- First, the ACMA has chosen to aggregate its analysis of data provided by individual broadcasters when seeking to assess the economic conditions presently facing broadcasters in regional Australia. This is entirely appropriate in order to protect the confidentiality of data provided to it by individual broadcasters. However, it means the ACMA is unable to report in detail on the economic circumstances facing individual broadcasters. This is important because, based on the data we have peer reviewed, it does not appear that the aggregate trends in revenues and expenses are uniform across all regional broadcasters. This issue has been identified and discussed by the ACMA in the report.
- Second, the results are heavily reliant on the quality of data provided to the ACMA. The ACMA appropriately notes the potential limitations of its data throughout the report, and we would echo these concerns. One particular issue of concern relates to the allocation of common costs where

1 We note, however, that we have not been asked to review the source of the data used by the ACMA in undertaking its analysis. Our review of the ACMA's calculations has therefore been limited to reviewing whether the modelling estimations undertaken by the ACMA are consistent with the methodology set out in its report; and that there are no errors in the calculations it has undertaken. The review does not extend to assessing the validity or suitability of data relied upon by the ACMA when making its estimations.

broadcasters operate in different geographical markets; or where they provide services other than broadcast television. Where this is the case, the ACMA has no visibility over how common costs have been allocated to the provision of broadcast television services in regional areas. If common costs have not been allocated in a reasonable fashion, this may have the effect of over- or under-estimating costs in regional areas, and therefore could potentially bias estimates of profitability. There are also some unusual anomalies associated with certain data provided by particular broadcasters in the data provided to the ACMA.

2. Costs of extending local content requirements

10 The ACMA takes two approaches to estimate the cost of extending local content obligations in regional areas:

a. Analysing historical data from the Television Activity Statements (TASs) of the three major regional broadcasters from 1999-00 to 2011-12

b. Analysing submission material relating to the costs of extending local content obligations in regional areas.

11 Each of these approaches is addressed in turn below.

2.1 Analysis of historical TAS data

12 The ACMA considers TAS data in two ways to determine whether the introduction of local content obligations impacted on costs for regional broadcasters.

Consideration of total expenditures from 1999-00 to 2011-12

13 Under the first approach, the ACMA:

- Looks at expenditure levels for each of the three major regional broadcasters in each year from 1999-00 to 2011-12
- Divides this for each broadcaster by the number of regions it operated in during each year
- Averages estimates across the three broadcasters to determine average expenditure levels by employee costs; depreciation, amortisation and occupancy; and affiliation fees in each year.

14 The ACMA is then able to see whether the introduction of local content obligations had an impact on these costs. It does this by comparing average expenditure levels in the years prior to 2003-04 with the years afterwards.

15 We believe this is a reasonable first approach to considering whether the introduction of local content obligations had an effect on expenditure levels for regional broadcasters. We believe the ACMA shows appropriate caution when noting such estimates can only be high-level indicators because it doesn't seek to control for other factors that might be influencing changes in expenditures over the period. The ACMA also appropriately notes limitations that are likely to exist with the data provided in the TAS statements.

16 We have reviewed the spreadsheets and underlying calculations performed by the ACMA in support of this analysis and found no error with them.

Extrapolation of costs

17 The second part of the analysis of the TAS data involves separating license areas into those where a local content obligation applied, and those where it didn't. The ACMA then sums across all three major regional broadcasters:

- Depreciation and all forms of amortisation costs
- Rent and occupancy costs.

18 It then compares the growth rate between 2003-04 and 2011-12 for these expenditures for those license areas with a local content obligation and those without. In this regard, it finds that costs were higher in those license areas where a local content obligation applied.

19 The ACMA then sums the total of these expenditures for the 9-year period between 2003-04 and 2011-12 for those license areas where there was no local content obligation, and applies the differential growth rate estimated in para [18] above to this figure to determine what it believes might have been the additional expenses incurred in these areas if broadcasters had faced a local content obligation. These are then divided by the number of major regional broadcasters to determine an additional cost per broadcaster.

20 A similar process is followed in relation to labour costs (i.e. salaries and wages plus labour on-costs).

21 The approach used by the ACMA appears reasonable for estimating the potential impacts of the imposition of local content obligations. We have also reviewed the spreadsheet modelling and have found no errors in the calculations undertaken by the ACMA. We do agree, however, with the ACMA's observation that the analysis in this section of the report is sensitive to the period over which changes in costs are analysed. For instance, and as noted by the ACMA, if calculations are conducted over the last 5 years rather than the last 9 years, then the trends in growth rates are reversed. We agree with the ACMA that it is appropriate to consider costs over the full 9-year period of the analysis. This is because, as noted elsewhere in the report, the initial up-front costs of meeting local content obligations are likely to represent a substantial element in the costs of extending

local content obligations. A shorter, 5-year, period of analysis would not capture the impact of these initial up-front costs, which were likely to have been incurred close to when the existing local content obligations came into effect in 2003-04. Interestingly, however, the ACMA's analysis may suggest that while up-front costs make meeting local content obligations more expensive than not, the effect on ongoing annual costs is less certain.

2.2 Analysis of submission material

22 The second method used by the ACMA to estimate the costs of extending local content obligations to other regional areas involves developing a more "bottom-up" estimation of the costs of supplying local content in additional areas. To do this, the ACMA:

- First, determines the additional licence areas and local areas within which each regional broadcaster would need to provide additional local content
- Second, determines the likely costs of supplying content in these areas using a "news update" model, which involves providing 60 1-minute updates with local news content throughout the week
- Third, estimates both the upfront initial and ongoing costs of supplying local news content under this model
- Fourth, adjusts its estimates to account for a range of scenarios relating to "low cost" and "high cost" scenarios; and different amounts of cost growth rate over time.

23 This gives the ACMA a range of cost estimates within which it believes the costs of providing local content are likely to fall.

24 We would observe that the modelling results are again heavily dependant on data provided to the ACMA by regional broadcasters. In this respect, we note that:

- Certain of the data inputs provided to the ACMA lack credibility. For instance, in some cases, data provided by one broadcaster in relation to ongoing labour costs appear to be invariant to the number of staff employed in certain license areas. In other cases, there are no amortisation costs reported for one broadcaster for some license areas in certain periods. In combination, these points reduce confidence that estimates of the cost per minute per local area are reliable. The ACMA notes in its report that where anomalies were found, it went back to submitters to verify the numbers provided. The ACMA provided Frontier Economics with a summary of the responses from the regional broadcasters.
- A crucial input into the estimation of the costs of extending local content obligations is the level of up-front initial costs (estimated at $4.9 million). We understand the ACMA has been heavily reliant on the submissions of two

broadcasters on this input, and has not sought to independently model this amount itself.

25 The methodology used by the ACMA to estimate the costs of providing local content seems broadly reasonable. It does contain a number of simplifying assumptions, but this is often the case with bottom-up cost modelling exercises. We have reviewed the underlying spreadsheets and estimations made by the ACMA, and have found no errors in its calculations.

researchacma

Canberra
Red Building
Benjamin Offices
Chan Street
Belconnen ACT

PO Box 78
Belconnen ACT 2616

T +61 2 6219 5555
F +61 2 6219 5353

Melbourne
Level 32
Melbourne Central Tower
360 Elizabeth Street
Melbourne VIC

PO Box 13112
Law Courts
Melbourne VIC 8010

T +61 3 9963 6800
F +61 3 9963 6899

Sydney
Level 5
The Bay Centre
65 Pirrama Road
Pyrmont NSW

PO Box Q500
Queen Victoria Building
NSW 1230

T +61 2 9334 7700
1800 226 667
F +61 2 9334 7799

acma.gov.au