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Where convergence exposes divergence

IMPLICATIONS OF CONVERGENCE ON BROADCAST LICENSING

Communications, media and entertainment services are converging fast, with the digitisation of content and the emergence of new delivery platforms transforming consumer choices and shifting market boundaries. In light of this, the Australian Government has recently commenced a review to consider whether policy responses are necessary in the media and communications sectors to deal with these developments. In this bulletin, we focus on the implications of convergence for existing broadcasting licensing arrangements. We conclude that convergence will challenge the traditional form of these arrangements in Australia and make it harder for the Government to use existing quota obligations to support the local content industry.

In the past, communications and entertainment services were provided through separate distribution channels. Telecommunications services were provided over copper wires; television services were provided by broadcasters using radiofrequency spectrum; and written news content was provided in printed newspapers and magazines.

Often, control over individual distribution channels conferred significant market advantages on those organisations delivering services over them. For instance, the limited amount of radiofrequency spectrum made available for television services meant that only a restricted number of television broadcasters could operate in any given geographic area.

In return for the exclusive use of dedicated radiofrequency spectrum in Australia, television and radio broadcasters are currently required to pay licence fees based on a proportion of their gross revenues. Further, the Government supports local industry by imposing local content quota obligations on broadcasters. To the extent local content is more expensive, or attracts less advertising revenue, than other content, broadcast quotas are being used to subsidise local industry indirectly.

CONVERGENCE IS CHANGING MARKET BOUNDARIES

In March 2011, the Australian Government commenced a "convergence review". In a discussion document released by the Department of Broadband, Communications and the Digital Economy (DBCDE), it observed that:

> *The development of digital broadcasting, data compression and internet-based technologies, coupled with improved infrastructure capability, means that content and services that were previously constrained to one delivery channel can now be delivered over many different platforms.*
>
> *This phenomenon is known as **convergence**.*

Digitisation means there is now a common way to deliver many alternative types of content to consumers. Where previously consumers received their news, video entertainment and telecommunications via different delivery platforms (i.e. print, television and telecommunications networks), all of these services can now be provided over a single delivery platform (e.g. broadband internet). This means that a number of services previously provided in distinct markets are increasingly becoming complements in both demand and supply.

At the same time, the combination of digitisation and increased capacity on broadband networks mean that traditional delivery platforms now face competition from the internet as an alternative (or substitute) distribution platform.

Convergence is also challenging traditional commercial models for television broadcasters, who are increasingly facing competition to provide video content from online service and content providers. There is already evidence available to suggest the average time spent viewing free-to-air (FTA) and pay TV is in decline, while the amount of broadband data downloaded is increasing.

Further, viewers are no longer restricted only to watching content when it is scheduled by FTA broadcasters. Consumers can now download content whenever and wherever they want, and watch it at times of their choosing. Further, consumers may be downloading – perhaps illegally – programs over the internet before they are broadcast locally. This reduces the importance of broadcast scheduling and the ability to sell high-value timeslots to advertisers seeking to target consumers at particular times of the day.

THE THREAT TO EXISTING BROADCAST LICENCE ARRANGEMENTS

From a public policy perspective, convergence has the potential to undermine revenue collection and the support of local content under existing broadcast licensing arrangements. Licence fees from commercial radio and television broadcasters are estimated as a proportion of gross revenue, which is mainly derived from advertising. In recent years, the total amount of revenue raised from radio and television broadcast licenses has ranged between $258.6 and $286.8 million per annum[1]. As consumers substitute away from viewing content via television towards viewing content online, however, online advertising will become relatively more attractive to advertisers. In turn, this will reduce the revenue earned by FTA television broadcasters, and the revenue base upon which commercial broadcast licence fees are estimated.

The internet also creates challenges for Government attempts to support the local content industry. While the Government presently imposes local content quotas as part of broadcast licensing arrangements, it is much harder to impose such quotas on online content because consumers are increasingly able to download from anywhere in the world. This contrasts with traditional platforms where broadcasters could control what viewing options consumers faced by controlling the delivery and scheduling of programs. In this instance, the emergence of a substitute platform that works on a "pull" basis (whereby consumers pull content towards themselves) creates difficulties for local content quotas that presently rely on "push" distribution platforms (whereby broadcasters have control over what content is delivered to consumers). At the same time, the erosion of broadcasters' revenue bases reduces their capacity to subsidise the development and broadcasting of local content.

CONVERGENCE REQUIRES A FRESH APPROACH

From an economic perspective, a key change delivered by convergence is the creation of substitution possibilities that previously did not exist.

An important principal in economics is that the existence of substitute products and competition can drive out market inefficiencies. In this instance, convergence is undermining the degree of market power once held by those who controlled distribution platforms when separate services could only be provided over dedicated distribution networks. In turn, this is challenging the ability of the Government to maintain existing licencing arrangements that rely on a lack of competition between alternative platforms. The competition created by convergence is, therefore, forcing changes to existing licencing arrangements.

Economics is well placed to help consider policy issues associated with substitute services and behaviours. It suggests that social welfare will often be harmed where market features or Government policies distort economic activity. Distortions can be created when alternative activities are treated inconsistently. For instance, where taxation is applied to income earned from one economic activity but not another, such policies can distort economic behaviour away from the taxed to the untaxed activity.

This could happen where income earned from advertising on FTA television is subject to licence fees, but income earned from advertising on the internet is not. Distortions can also be created when one use of radiofrequency spectrum is paid for via license fees that vary with revenue (as is the case for broadcast television), while another is allocated via auctions that do not vary with revenue (as in mobile telecommunications for example).

Similarly, applying content quotas to one way of receiving content (e.g. television broadcasting) but not another (e.g. online services) can distort consumer choices between receiving content over different platforms.

Where possible, the Government should seek to ensure that licensing arrangements do not distort economic activity in this way, or favour one way for consumers to receive content over another. To achieve this, the Government may consider alternative arrangements such as those used in other overseas jurisdictions. Rather than obliging a growing number of disparate content providers to broadcast local content, the Government could directly subsidise the production of local content if it thought this was necessary. It could then consider ways to fund such subsidies transparently through non-distortionary means. One option may be via general taxation revenue. Other options may include a more targeted industry tax. For instance, in the United Kingdom and a number of other European jurisdictions, consumers pay a licence fee to own a television to fund the provision of public broadcasting services. In a converged world, the imposition of a "screen tax" – where a levy is charged on the sale of any device capable of receiving digitised content – could similarly be set to cover the cost of subsidising local content.

CONCLUSION

The Australian Government's convergence review is likely to lead to changes in broadcast licensing arrangements. We believe that the Government's focus should be on improving economic efficiency by determining the optimal level of revenue that should be raised from a converged dissemination industry, removing taxation distortions between content disseminators, and increasing transparency around the costs of providing local content.

Doing so, however, may not be easy. Such reforms will create winners and losers in a number of different industries, from FTA, pay-TV and radio broadcasting to media & content and broadband internet providers. In the absence of clear Government leadership in this area, there may be little convergence between these parties on the appropriate policy framework.

NOTES

1 Australian Communications and Media Authority (ACMA), Annual Report 2009-10, at p. 71. The Government has agreed, however, to make licence fees subject to rebate arrangements that will lead to substantial reductions in licence fees for the 2010 and 2011 calendar years.

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