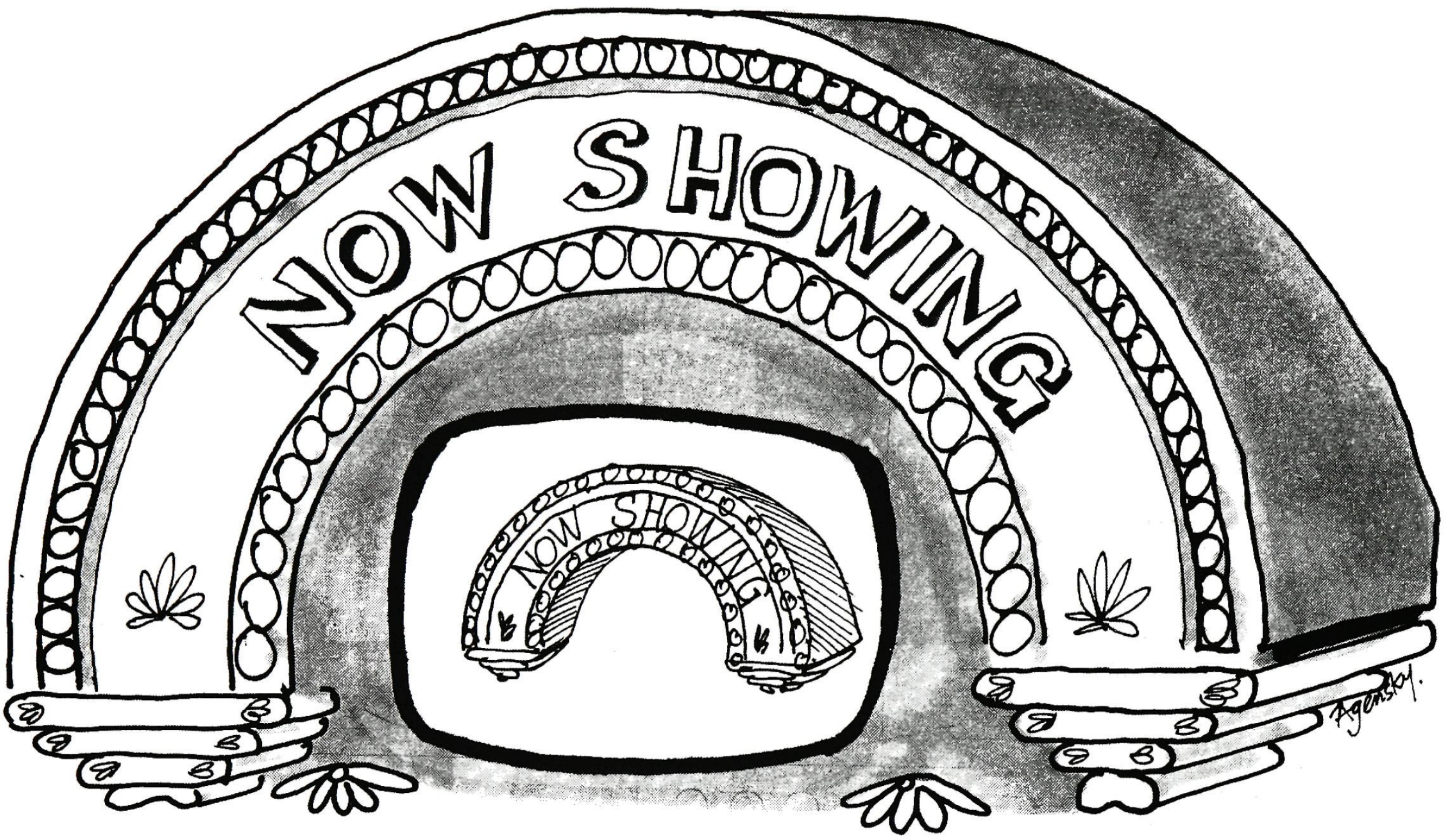

The Big Picture

by Hugh H. Edmunds

Although the history of Pay TV goes back to even pre-World War II days, it is only in the last two years or so that the spectacular eruption of Pay TV in the U.S. and the subsequent interest of the Canadian cable operators brought the issue to a head in our country. In all of this our program producers, particularly the filmmakers, sense a large new market in Pay TV. The multimillion-dollar question for our policy makers is how Pay TV might best be introduced into Canada to the advantage of our indigenous program producers, the Canadian consumer, and with the least destructive consequences to our existing broadcasting system.

Hugh H. Edmunds spent 15 years in the public and private television industry as a program director, production manager, and producer-director. Recently he completed a study of the independent production industry for English-language broadcasting in Canada on behalf of the federal Department of Communications. Currently, he is acting as a consultant to the Department of Secretary of State with respect to Pay Television. His academic work includes the teaching of production courses in television and film and seminar classes in Canadian broadcasting policy. He is associate professor of the Department of Communication Studies at the University of Windsor.

Pay TV Began as Over-The-Air "Pay Per Program"

Pay TV was originally conceived as over-the-air broadcasting of programs scrambled or made unviewable through some technical process. With the payment of a fee the home viewer could watch the unscrambled program of his choice. Tantalizing ideas of symphonies, ballets, experimental and foreign film, a whole universe of programs directed to minority tastes was the promise of the new medium. Freed from the pressure of mass audience appeal which enslaved the commercial offerings to their cost-per-thousand ratings, new high-quality programs, heretofore unobtainable, could be purchased to watch in the comfort of the home. Such was the promise of Pay TV.

This brings us to the major interest in Pay TV – money. It doesn't take a financial wizard to figure out that if only five percent of the television homes in North America pay $10.00 to see a championship heavyweight fight, the total box office would amount to nearly $40 million, or if one-fifth of the homes pay $5.00 to watch the Super Bowl, the promoter would be sharing a gross revenue of $75 million. What about first-run feature films, the Metropolitan Opera, Broadway plays, etc.?

One Rand Corporation study has projected $2 billion a year in total billings as forseeable, but it's been slow in coming.

How Pay TV Developed

Earliest actual experiments began in 1950 in the U.S. but subsided while the courts debated whether this actually constituted "broadcasting" within the meaning of the Communications Act. This resolved in 1962, the FCC (Federal Communications Commission) authorized the Hartford, Connecticut, Pay TV experiment. Via over-the-air transmission, a program selection consisting mainly of feature films plus a few sporting events was shown. In Canada, Etobicoke was the site of another experiment, but this time cable was the means of distribution and the subscribers placed coins in a box to view the programs. Both experiments were variously labelled as failures; however, a number of factors were not taken into consideration. In the Hartford case, a great deal of experimenting was done with the content and the method of metering subscriber usage which was rather awkward. In Etobicoke, the pay system called for the installation of cable for Pay TV alone, rather than Pay TV being an additional source of revenue to a cable which was already paying its way by providing a basic service of distant signals.

During the next few years in the U.S., court actions to prohibit Pay TV were brought against the FCC by the motion picture theatre owners who felt the medium threatened their livelihood and also by the conventional broadcasters who not unrealistically feared that their choicer programs would be lured away to the new medium. A shift from advertiser-supported television to consumer-supported television was in the making, and although fewer viewers might be reached, the economics were such that vastly more monies could be spent for the content. Although the U.S. theatre owners eventually lost their case, the conventional broadcasters fought doggedly for the banning or restricting of Pay TV to prevent the programs now aired for "free" being "siphoned" off leaving the consumer (with his large investment in a TV set) to watch the leftovers. California citizens at the broadcasters' behest even passed a referendum – later reversed – forbidding Pay TV in their state.

As we entered the '70s the FCC hoped to resolve the arguments by issuing a set of anti-siphoning regulations designed to protect the existing programs on advertiser-supported TV (and the consumer's investment in his set) while "permitting new uses of the broadcast waves." In essence, these regulations required that a pay television operator could use only feature films younger than three years; or older than ten; or foreign films; or films for which the broadcaster had no interest. By and large, sports events shown on Pay TV could not include those currently being broadcast or special sports events such as the Olympics if they had been broadcast within the last ten years. In total, feature film and sports events were not to occupy more than 90% of the program schedule.

In spite of the huge revenue potential and with the legal problems resolved, over-the-air Pay TV, until recently, has been rather slow to develop for a number of reasons. Feasibility studies indicated that the public was not particularly interested – probably due to a general ignorance about what Pay TV was or what it could offer. Really efficient and secure (uncheatable) systems for broadcasting scrambled signals, unscrambling them, and metering the consumer's viewing of each program have only now become available. Finally, Pay TV licenses were restricted primarily to those broadcasters in large cities who were presumed to be in financial difficulties. They therefore lacked the adequate financial resources to start up and exploit the new medium.

Now that the technical problems have been solved and with the demonstrated interest of the consumer, several large companies, e.g. The Wometco Corporation, are moving in and the full impact of over-the-air and probably pay-per-program Pay TV will shortly explode on the American scene.

The Current U.S. Pay TV System

However, a variant of Pay TV which makes use of the established U.S. cable systems has surged ahead. In essence the cable subscriber gains unlimited viewing of a special channel of selected programs for a monthly fee (average $8.00) additional to the basic fee (average $7.00). This system is referred to as "pay-per-channel" and curiously in our Canadian discussions this approach has become synonymous with Pay TV, and by inference synonymous with cable.

In this context it should be noted that the development of cable systems in the United States has differed markedly from Canada. The U.S. major cities with the exception of Manhattan are not cabled. Like Canada, the extension of cable and the willingness of the consumer to subscribe, has depended on the importation of distant signals. For Canadians this has meant U.S. stations. For the U.S. consumer this has meant stations not otherwise available in the community. Of the large U.S. cities, at this time, it is only in Manhattan that there is sufficient consumer demand for cable as a means of overcoming reception problems due to industrial interference and "ghosting" to warrant the expense of a cable system. (However, newer and cheaper technologies involving multi-channel omni-directional microwave – known as MDS – transmitting the TV signals to individual buildings for internal distribution by cable, or even homes, may advance rapidly.)

The apparent plan in the United States, therefore, is for Pay TV to be distributed over the air in most major cities and by cable in the smaller centers. In Canada it is the major centers that are cabled while the smaller communities (and rural areas) are not.

How Pay-per-Channel Developed

Although most U.S. cable operators were making money, in general they were working with smaller systems and with lower ratios of homes subscribing to homes passed by cable than their Canadian counterparts. Therefore the attraction of providing other services to produce revenue, since the use of additional channels (cable can carry up to 40 channels) meant slight or negligible further cost, was very enticing.

Rapidly a number of program suppliers came into being who would either supply a "menu" of programs for a single channel or negotiate on behalf of the cable operator with the Hollywood producers for the rights to program a channel of pay television. Already a number of cable operators had had to offer a channel of feature films in addition to the distant stations in order to gain basic subscribers. Now with better product available they were able to charge an additional fee for a pay channel. In general, this amounted to $8.00 a month of which the cable operator kept approximately half and the program producers and suppliers took the rest. $4.00 a month would not pay for a cable system but as an additional revenue over and above the $7.00 subscription received for the basic service, it represented a highly profitable extra. This rather primitive Pay TV then depended on an existing cable system programming one or possibly two channels for which the viewer paid $8.00

per channel a month to view primarily six to eight new feature films per month, each repeated many times that month and the following month, plus assorted other content. Non-subscribers were prevented from viewing the pay channel by a trap (filter) placed at the connection to their home, or the signal was scrambled and pay subscribers were provided with a descrambler. On this basis less than a year ago there were a quarter million subscribers. The number now is probably close to one million, or about 1.5 percent of the TV homes in the U.S. or 10 percent of the 10 million cable homes.

Current Programming

The actual content of the pay channel varies from location to location depending on whether the cable operator makes his own arrangements for the programs, whether the operator subscribes to a service, or whether the operator belongs to a chain of cable systems which has worked out its own package of programs, or whether a program supplier has leased a channel from the cable operator and supplies the programs for that channel. The largest supplier of programs is Home Box Office of New York, a Time-Life Inc. subsidiary, which has pioneered in the use of satellite transmission to distribute 12 hours of programs each day to about 40 locations. At the time of this writing, Home Box Office is estimated to have half a million subscribers or half of the cable homes which subscribe to a pay service in the U.S. The subscriber receives not only fairly recent feature films such as **Farewell My Lovely, Rollerball, Swept Away,** etc., but specially produced programs like **The Bette Midler Show, Les Folies Bergère,** and uncensored comedians in performance "on location." Home Box Office has also carried via satellite from Europe the non-televised tennis matches at Wimbeldon and many league games of the NBA and the National Soccer League which were not otherwise televised. They have also been experimental in the use of rather *avant-garde* film as indicated by their purchase of content from the Independent Cinema Artists and Producers Association.

The other major program supplier is Telemation Program Services which distributes its feature films and other programs via video-cassette. This company acts rather more like a film booker than an actual program supplier since it usually negotiates with the film producer for the rights for use in a particular market and the cable operator himself signs the contract with the film producer. In this way a much more flexible "menu" may be offered by the local cable operator, taking into account particular community tastes. In all cases the program suppliers have avoided any X-rated films, probably because it is a sensitive and untested issue and the pay-per-channel approach doesn't lend itself to control of content by the parent in the home. There is some evidence that those cable systems using Telemation Program Services achieve higher penetrations of pay television subscribers than does Home Box Office.

It should be pointed out, however, that all figures are changing rapidly. Pay TV in the U.S. is only in its preliminary exploitation stage and any assumptions or projections based solely on this current U.S. model which take for granted that it is either the only one, the ideal one, or the future one, should be highly suspect. It has just happened that a correct mix of program content, cost of available programs, consumer interest and willingness to pay the required cost, technological costs, and cable already in location have come together into an economically viable system. For Home Box Office, using the sophisticated satellite delivery system, this has meant huge start-up costs and it is probably only now turning the corner. It is safe to say that this will not be the final model in the U.S. (but more of that later).

What does all this mean for...?

As late as the beginning of this year the CRTC had determined that Pay TV was premature. However, due to pressure from the cable operators and the rather hollow threat of unregulated Pay TV, it appeared in May that the federal government was about to move precipitously and superficially into this area. In happy expectation of the imminent licensing of Pay TV, the cable operators of Canada assembled in early June for their annual convention in Toronto's Four Seasons-Sheraton. The high spirits abruptly stopped when Madame Jeanne Sauvé, Minister of Communications, announced that, yes, Pay TV was imminent, but that the federal government and the CRTC were suggesting other options, even up to and including a government monopoly. CRTC chairman Harry Boyle strongly advised the cable operators to review their current proposals and submit revised ones with the transparent implication that suggestions to date were unacceptable. What reduced the convention to a state of shock gave heart to the Canadian program producers. It appeared that the federal government was adamant that at least a reasonable share of the Pay TV spoils would be directed toward development of the Canadian program production industry. Before discussing options available for Canada, it is well to note that our entire system of broadcasting is in a state of crisis. It is only now fashionable to release the figures indicating the destruction of the viewing of Canadian programs due to the proliferation of U.S. stations via cable and the increase of U.S. programs aired due to newly licensed Canadian stations. In English-speaking Canada as a whole, only one hour in three is spent viewing Canadian programs and in Toronto it is one hour in four. This hour is primarily news and sports. Even more alarming is the research which indicates that by age groups the least viewing of Canadian programs is being done by our young people. If television has the power to sell merchandise, it certainly has the power to sell an alien culture. The whole purpose of broadcasting in Canada has been undermined and the solutions are not easy.

A Positive Role?

The question, then, is whether Pay TV, although unlikely to fragment the existing audience very much, can be directed toward redressing the balance through some positive role. A recent study by the author and colleagues into the independent production industry for English-language broadcast in Canada has demonstrated, rather conclusively, that our entire broadcasting system is structured against the independent producer. The broadcasters own their own production facilities, the means of distribution, and control the exhibition of programs. This is not dissimilar to the plight of feature film in Canada where foreign producers control the distribution companies and the Canadian theatres. Very simply, the current system has no incentive to make use of independent production. The other problem, of course, is whether either the existing broadcasters or independent producers can make programs that Canadians would want to watch. In the U.S., advertiser-supported television for the current year can pay $300,000 for a prime-time one hour program. This is not to say that the viewer gets what he wants, but the viewer gets what can be made most "audience-attractive" for $300,000. In order to compete with other producers, the producer spends virtually all this amount in production costs, hoping to reap a profit in later syndication or in foreign sales, which in the case of Canada means a $4-6,000 return (that is, as long as we remain a seller's market).

Only a tenth of the U.S. population

A Canadian-produced program must not exceed approximately $15,000 a half-hour to pay its way, since we are one-tenth of the U.S. size. However, if the economic base for program production moves from the advertiser-supported to consumer-supported as in Pay TV, would this mean the funding of programs Canadian in origin but with the sophistication and production values found in conventional U.S. product? Could we then make programs Canadians would want to watch? Ultimately Pay TV is much more program-oriented than our current systems, particularly on a pay-per-program basis. Our existing system has been saddled with immense expenditures for extension of services, and investment in plant, distribution and transmitters. Although we have refused to permit substandard technology and have applied rigorous qualitative technical standards, we make no such demands on the content. We do set a quantitative standard on the amount of Canadian content on over-the-air broadcasting but leave it to the broadcaster to determine the qualitative standards. On the whole, we install first-class hardware to distribute second-class content.

The federal government (for pragmatic rather than cultural reasons) seems to be demanding far greater participation by Canadians in the production of broadcast and film programs using our creative and other resources, particularly if export dollars are involved. By simply applying the existing U.S. model for Pay TV to Canada, it is rapidly apparent that the bonanza of dollars for Canadian programs is simply not there. Madame Sauvé, in her address to the cable operators, conservatively projected thirteen and a half million dollars for Canadian programs annually at some future time, or roughly the price of two Hollywood feature films per year. This projection was based on 35% of the existing cable subscribers electing to pay another $8.00 a month for pay television of which 15% would go to Canadian program production. This 15% of gross Pay TV revenues is the figure suggested by the Canadian cable operators and represents what they feel they can afford if given pay television. It probably also represents the amount we could underpay the American supplier for his feature films if a single organization were to buy for all the cable systems in Canada. If judiciously applied, this thirteen and a half million dollars would be very useful to the independent program industry, particularly as seed money for feature film production. The independent production industry study mentioned before did indicate that when our independent producers were funded sufficiently well to meet reasonable production costs, they showed good indications of international sales and profits. The other 85% of the $8.00 a month would then go to the cable operators to cover the costs of selling the service, installing the necessary technology, billing and collecting, and acquiring the U.S. programs, with a profit left over.

Who cares?

With the advent of Pay TV a flurry of studies of the Pay TV problem have been set in motion in Canada during the last six months. The CRTC, The Department of Communications, and the Department of the Secretary of State are all much concerned. So are some of the provinces. The cable operators and the over-the-air broadcasters, including the CBC, are bidding for their role in Pay TV. So are the independent program producers and the filmmakers. It is assumed that there will be no public hearing, but that the CRTC, upon receipt of the various submissions, will make a decision concerning the *modus operandi* and then call for applications. At this time the governmental departments are in some disarray. Each is convincing their minister that they alone know how Pay TV should be introduced and that the other department is hopelessly uninformed. In reality, everyone is pretty confused.

The policy-makers sense an opportunity to do something for Canadian broadcasting and for the Canadian program producer. However, as they burrow into the information and the statistics and the cost figures and the proliferation of hardware, they are staring at a medium which will probably send $2.00 to the Hollywood producer for every dollar spent on Canadian content, with little promise of markedly assisting the goals of broadcasting in Canada. Such questions as how much money can be extracted from the system for a Canadian production and how this money can be distributed to program producers have not been satisfactorily solved. At present the cable operators suggest 15% of gross revenue which would be $13.5 million based on 35% of cable homes subscribing to Pay TV. The private broadcasters offer 15% of gross revenue plus 40% of pre-tax profits which in the case of 45% penetration means close to $20 million. However, $8 million would be spent within the broadcasters' own operations, with $5 million for "Pay TV and Culture" and $7 million for Canadian feature films. The best government projections implying a government agency seem to be in the area of $20 million and none of the above seem to provide incentives to producers in the sense that the producer profits directly on the quality of his work. What is lacking is a real sense of Canadian programs, and those who make them, being the dynamic heart of the system. It is simply perpetuating the real control of those who own the hardware and the delivery system in a medium where there should be very direct interaction between those who really buy the programs – the consumers, and those who make them – the producers. Part of the problem lies in slavishly accepting the current U.S. system and simply modifying it for Canadian application.

Two basic errors

Two basic but probably erroneous assumptions appear to be conditioning our current strategies. The first is that Pay TV is synonymous with cable and the second is that pay-per-channel viewing is more advantageous in Canada than pay-per-program. Let's deal with the first.

Over-the-air and Cable Pay TV

Although the past history of over-the-air subscription television in the U.S. has been very spotty and checkered, it is only recently that serious financial concerns have entered the picture and competition for licenses in the major cities has commenced. In the view of the FCC, over-the-air pay television is now on its way. Two or three years from now it may well eclipse cable-pay in number of subscribers. Four licenses have been granted and 16 more applications are pending. The technology for unscrambling the program and charging for its viewing is costly (in the order of $100 per home), but over-the-air distribution of the TV signal is very much cheaper than cable. The objection that radio frequencies for television signals are in short supply doesn't hold up. Although there are areas in Canada where it would be difficult to create a new UHF allocation, it would not be impossible, nor would the conversion of some of the existing UHF transmitters to pay be inconceivable. Other than these areas, there is a wealth of spectrum space available. Not only can over-the-air broadcast extend Pay TV to the less settled areas, it could also provide something akin to the basic service now supplied by cable to the urban areas, helping to equalize services and possibly aiding in offsetting the continual migration to larger centres. Over-the-air Pay TV could also serve our urban centers as it will in the American major cities if it becomes impossible to arrive at some agreement with the cable operators. The financial damage done to the broadcasters in Canada by cable might to some extent be redressed through the granting of over-the-air Pay TV licenses. It is curious how few broadcasters have pursued this option.

Pay-per-channel vs Pay-per-program

With regard to the second assumption that the pay-per-channel strategy is better than pay-per-program, the following arguments are usually raised. The technology for pay-per-program is much more sophisticated and therefore more expensive than pay-per-channel which indicates a greater capital investment in hardware is required using money that should be available for programs; that the technologies are not properly operational; and that since Canadians do not seem anxious to watch Canadian programs they certainly wouldn't pay for the privilege. The technical cost arguments have some truth. Without going into too much detail concerning the various technologies, the security of a pay-per-channel system depends on three options: placing a trap at the home of every non-subscriber so that they cannot watch the pay channel, placing a descrambler in the homes of those that do subscribe and putting a scrambled signal on the system; or using one of the midband channels (A, B, C, D, etc.) requiring the rental of a converter (which amounts to a very insecure system in Canada). Present trends would indicate that although the traps are relatively cheap initially they have to be installed at all non-subscribers' homes and they are rather easily defeated, a practice becoming more prevalent. The unsophisticated descrambler has a number of weaknesses depending on the method used. The converter system has no application in our major cities which need converters in any case. There is a considerable expense involved in all of these and a poor or insecure system would have to be replaced.

The move to pay-per-program viewing will probably take place in the not-too-distant future. Most experts agree that the consumer will probably prefer it; the available evidence indicates that gross revenues are markedly higher per subscriber; penetration will be higher, and that the program producers are becoming more militant about receiving an actual share of the box office generated by their programs. Not only does the evidence indicate that pay penetration will be higher with pay-per-program than pay-per-channel, the differential between the two will more than pay for the difference of cost due to sophistication of technology.

There are other considerable advantages to pay-per-program over pay-per-channel. The pay-per-program method is not restricted to one channel, but uses a multitude of channels. Contrary to the belief that pay-per-program would lead to the same market forces that control conventional commercial television, that is, mass audience appeal, this simply isn't the case. With a multitude of channels (since increase in number of channels is virtually without cost on a cable system), there is real evidence that a program which is bought by a total of only 2 or 3% of subscribers in all its many exposures pays its way at least for the Pay TV operator. Expert opinion also indicates this could be as low as 1%. For example, if only 5% of the cabled homes in Canada paid just $2.00 to see a Canadian production, this would amount to a gross box office of $300,000. If our pay-TV system was designed to double or triple the producer's share of this amount, the return would be very significant.

Telecinema of Columbus (Ohio) is currently programming four channels and is experimenting widely with various program contents. One interesting trend is that the less-than-blockbuster feature film is showing significant results. Features that have been unreleased, or failed to receive prime distribution, when exhibited in the home have done surprisingly well. This bodes well for Canadian feature production.

Without the constraint of limited prime time on a single channel or attempting to please everyone with a single menu of offerings over a single channel, pay-per-program offers much wider diversity of choice and interest. Curiously, it also consumes less of the viewer's time than pay-per-channel and therefore has less of an adverse affect in fragmenting audience. (This technical capability of metering the pay channels has been extended to the monitoring of all channels in 800 homes and some curious audience preferences have come to light. Of all television viewing on Sunday morning, for instance, it appears that soft pornography appeals to the greatest number of homes.)

The Program-Centered Option

How would the Canadian producers, artists, and performers fare? Probably better than in the protective wrapper of pay-per-channel. Although that seems a safe approach, the danger is that the pay-per-channel subscriber who buys the whole "package" expects very little to displease him. The pay-per-channel operator would have to play it very safe.

Conversely, while pay-per-view does demand that the producer appeal to some definite audience it need not be large. Surely the producer does have some obligation to demonstrably interest at least some segment of the population. We do expect our symphonies and ballets to show substantial other interest before granting subsidies. Within this system a formula could be devised which would greatly augment the financial returns to a Canadian producer pro-rated to some extent on the program's success. From a financial point of view it becomes a highly leveraged investment and very attractive to the investor, yet all the monies are derived from within the system without call on the public purse. This program-centered option is worth some serious study. With the inclusion of over-the-air Pay TV and use of pay-per-program charging, the potential number of subscribers and the gross revenues rise considerably above the currently suggested models and can provide considerably more money for Canadian programs. Analysis shows there is also much greater opportunity for use of local and regional programs in this system and considerable incentive for them.

It would be regrettable then, that if the United States is about to move toward over-the-air pay television and pay-per-view, we were to install a modified and soon likely to be obsolete system which probably would not offer the maximum potential returns to Canadian program production.

We must also act in the best interests of the Canadian consumer while using the introduction of Pay TV as a beginning of an overhaul of our existing broadcast system. □