The Business of Television
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Summary

1. Overview of the television industry as an ecosystem and how all the various players in the industry interact and a discussion of key issues affecting its future.

Key Takeaways

1. The "television studio" is the entity responsible for the financing, development, production, and distribution of a television production, and is typically the core rightsholder, typically controlling every facet of worldwide exploitation.
    a. Through relationships with talent and employees, the TV studio is the "factory" that churns out Television product.
    b. A TV studio is at the crux of deal making in the industry both upstream (with rightsholders and talent "service providers") and downstream (with co-producing studios and network licensees).
2. Hallmarks of "Peak TV" (Notion from FX Networks CEO)
    a. There is more volume than ever before because of networks and platforms available to consume video content.
    b. There is more fragmentation than ever before as new supply of television series (125%) has increased much more than population growth (5%)
    c. Emergence of TV blockbuster to break through the noise (higher budgets and production values)
    d. Emerging new low budget productions and growing "nichification"
3. In TV, the writer is the creatives force that drives deal making where in movies it is usually the director.
4. The portfolio of a TV Studio very much resembles a venture capital portfolio and demonstrate a "power law".
    a. Shows are very expensive to produce and for the many failures there are massively successful shows (i.e. Friends, Seinfeld, and CSI) that make up for all those losses.
    b. Another analogy to investing: in managing a studio portfolio its important to have diversification.
5. The contractual relationship between the studio and a network will be that of a license agreement, by which the studio grants specific, but limited rights and will depend on several factors:
    a. Type of network involved: whether its broadcast, cable, or digital.
    b. Type of show: whether it's a 30-minute comedy or a 60-minute drama.
    c. Type of relationship between the studio and the network (whether an affiliate or a third-party studio)
6. Mix of content on most networks consists of content acquired from third-party studios / content owners and content generated in house via an affiliated studio or acquired via license from an affiliated studio entity.
7. The business model of television as a business relies on a "dual revenue" model: direct pay (transaction and subscription fees from viewers) and advertiser supported although today most blur it as a mix of the two.

   a. The broadcast networks are freely accessible and sell ads against their content, the value of which is driven by volume and demographics of a network's viewership; Note: However, the broadcast networks now rely more on retransmission revenue.
   b. The conventional cable networks (FX and AMC) generate revenue through a combination of advertising sold against their programming and carriage fees received from cable and satellite providers which is driven by viewership and consumer demand for the network.
8. The revenue model of a network really drives how it evaluates return on investment and helps decide which shows it commissions and renews:
   a. A traditional network that relies primarily on advertising revenue that directly proportionate to ratings and viewership will like shows that appeal to the largest and "broadest" group possible.
   b. Networks like HBO or Netflix are subscription services, so the goal isn't to attract as many viewers as possible but rather to add subscribers and reduce churn. Therefore, they seek more exclusive rights and to look for a mix of series that have cultural ubiquity and "must see" status and smaller series that may not have large followings, but they are very loyal (a churn reducer).
      i. Less about show by show ratings but building a brand and creating loyalty through serving niches ("the Long Tail")
9. Larger broadcast stations opt to negotiate "retransmission consent agreements" with the MVPD's to include their stations in packages for local subscribers.
   a. Like the carriage fees paid to cable companies by MVPD's.
   b. This retrans fee is split between broadcast networks and local stations.
   c. This is becoming a bigger portion of broadcast networks revenue over time.
10. Fees filter upward in the television industry: subscribers fees → MVPD's → carriage fees → Networks → license fees → Studios
11. Carriage agreements divide available advertising time between MVPD's (who sell to local advertisers on a market by market basis) and networks (who sell to national advertisers)
12. Affiliation agreements between local broadcast stations and national networks advertising allocated between inventory tied to the broadcast network's national programming with the rest going to the local station during its self-produced or syndicated program.
13. Online video distribution represents several things all at once including the death of some classical markets (the physical home video business), providing a new medium for downstream distribution or programming, and a new frontier for original content.
14. Types of on demand video include:
   a. Subscription Video on Demand (SVOD) is a service where you pay a subscription fee to access a library of video with no limits.
   b. Advertising Supported Video on Demand (AVOD) refers to customer access to on demand content which is provided at no charge but is accompanied by advertisements either pre roll (before content) mid roll (middle of content), or post roll (after the content is complete).
   c. Transactional Video on Demand (TVOD) refers to paid access to content online with purchase and rental fees paid on a product by product basis.
      i. Electronic Sell Through (EST): permanent downloads of an episode or series like a DVD purchase.
      ii. Electronic Rental (ERT): a temporary or time limited download like an old DVD rental.

15. “Standalone” rights are those given to a service that is inherently streaming based (i.e. Netflix or Amazon) whereas “Companion” rights are granted to traditional network licensees who want to provide their customers both web based and linear streams.
16. The new streaming video providers (Netflix, Amazon, and Hulu) look at lot like the prominent cable networks (AMC, FX) that rose two decades before and build the franchise on second-run syndicated content that appeared in the theatres or on television.
17. Tax credits have a huge impact on television today in various areas such as: where show is produced, how it is produced, how much it is produced for, and whether it makes sense to produce it at all.
18. Copyright: often described as a “bundle of rights” whose divisibility is only limited by the availability of markets and the creativity of lawyers.
    a. Foundation of distribution and profit-making strategy of television studios.
    b. *The goal of a studio is to sell the same product over and over to as many buyers as possible into order to recoup its investment and eventually make a profit on the series.*
    c. A studio uses the divisibility of its copyrights to maximize revenue across media, territory, and time.
19. Secondary medium for most television shows referred to as syndication. This market is robust for:
    a. Half hour shows as they are easier to schedule.
    b. Episodic, non-serialized comedies (easier to follow and enjoy).
    c. Shows that originally aired on broadcast TV (as they are known).
    d. Have at least 100 episodes.
20. Most content licenses define a limited exhibition territory, so the same show can be sold multiple times on a territory by territory basis.
21. The most important markets for international rights include the United Kingdom and Germany and Canada, France, Spain, and Australia are also economically significant.
    a. US Broadcast network series usually most significant.
22. In every territory and media, a successful TV show can be licensed over and over again making a long-tail of revenue for studios with significant libraries.
    a. Helps subsidize losses for taking risks elsewhere.
23. The studio controls a variety of “allied and ancillary” rights such as soundtrack and music publishing rights. This also includes licensing and merchandising rights.
    a. Not many series make a ton of money here but the ones that do generate lots in ancillary revenue.
    b. Agreements generally structured as copyright and trademark licenses with a defined scope (i.e. licensed product categories), exclusivity, territory, and time.
    c. Royalties typically range from 5 – 15% depending on product category and desirability of the intellectual property.
24. Copyrights protect creative works that are tangibly recorded and enjoy these rights:
    a. To copy or reproduce the copyrighted work.
    b. To prepare derivative works based on the copyrighted work.
    c. To distribute the copyrighted work.
    d. To publicly perform or display the copyrighted work.
25. A trademark is a limited property right in a particular work, phrase, or symbol used to identify an individual or company as the source of a product or service.
26. Rights deals are another form made with individuals of sometimes true stories, etc.

27. Studios obtain these rights with an option / purchase agreement, an agreement by which the buyer obtains the exclusive rights for a period of time to purchase certain specified rights on pre-negotiated terms.
    a. Option fee typically runs around 10% of the negotiated purchase price.
28. In addition to the purchase price, royalty, the seller of the television rights with received a share of the “back end” or contingent compensation from the series.
    a. Usually runs between 1.5-5% of the MAGR (Modified Adjusted Gross Receipts) with it typically being 2.5%
29. Every option / purchase agreement must specify the rights that are being optioned, and therefore subject to purchase by the studio.
    a. Studios like to start are 100% and work their way down.
    b. Smaller producers and studios may settle for acquiring only specified rights (“all motion picture and television rights”)
30. Authors often seek to reserve merchandising rights in their works, and in particular, rightsholders for science fiction, fantasy, and other genre titles tend to fight hard to reserve or at least freeze potentially lucrative video game rights.
    a. Studios try to resist it and they can be sub-divided further.
31. Major negotiation takes place around the theatrical feature film rights and live stage rights which have significant value.
32. When parties cannot agree on the reserve or grant of a “right” they may choose to freeze the rights.
33. Rightsholders’ will often negotiate to have the rights revert back over a specified period of time.
34. A lot of popular scripted series originated in other geographies: (The Office in The UK and Homeland based on an Israeli series). In addition, Married With Children was updated for some local geographies.
35. *A studio usually acquires both theatrical and television rights without having a clear plan on which ones they will exploit.*
36. Writers prefer short-term deals for professional flexibility and the right to re-negotiate their contracts.
    a. This is often how shows become more expensive in the out-years and Netflix has cancelled some show after two seasons for this reason.
37. Digital services such as Netflix and Amazon have paid top dollar to lure talent and need to pay top dollar to offset contingent compensation due to the scope of rights, they desire for their business models.
    a. They are basically buying across all media, territories, and time
38. Contingent compensation (profit participation or backend) is a key component of numerous agreements with key creative talent and rightsholders behind a television series.
    a. This represents the talents chance to share in the upside of a series; this is very similar to employees receiving equity in a company versus just salary.
    b. Most studios employ a rigid policy of not allocating more than 35% of the MAGR to the backend with the range going from 30-40%.
    c. A typical 35% backend pool would be allocated as follows: 2.5% to the underlying IP, 2.5% to the pilot director, 15% to the writers / creators, and 15% to non-writing producers.
39. The variables that drive the backend include all the revenues from series exploitation and expenses incurred by the studio in all aspects for production, marketing, and distribution.
40. Gross Receipts – Distribution Fees – Distribution Expenses – Overhead – Interest – Cost of Production – Third Party Profit Participations = MAGR

   a. <u>Gross Receipts:</u> refers to all revenue received by or credited to a studio from its exploitation of a TV series and rights therein from all sources.
      i. Home video royalty only 20% and studios moved that in house to capture the sub-distributors margin; this could begin to happen now with content creators bypassing the MVPDs to go DTC (i.e. HBO)
      ii. The majority of studios consider licensing to OTT streaming as television revenues but TVOD and EST they still consider home video (at the reduce royalty rate of 20%)
   b. <u>Distribution fee:</u> A defined % of revenue received form nearly all sources which the studio retains as compensation for its time, effort, overhead, and other resources in the distribution process.
      i. These fees generally range from 10-25% with 15% being the most common and 10% being A-level.
      ii. These fees are usually waived on revenues received in the initial domestic license For a TV series usually because not much effort was expended in the first place without the deal from the initial TV network.
   c. <u>Distribution Expenses:</u> studios reimburse themselves off the top for all actual expenses incurred in the process of distribution.
      i. Advertising and marketing
      ii. Costs for subtitling or dubbing of foreign versions
      iii. The expense of duplicating and transporting physical materials to licensees; clearance fees that have not otherwise been accounted for as production costs
      iv. Residuals and reuse fees payable to talent pursuant to applicable union collective bargaining agreements
      v. Costs of enforcement (including intellectual property and audit litigation)
   d. <u>Overhead charge:</u> a charge that ranges from 10-15% and it based on the cost of production and meant to compensate the studio for in house salaries, offices, and overhead used in the studio production business.
   e. <u>Interest charge:</u> an expense on the actual expenses incurred by the studio and is calculated before production costs but after (gross receipts – distribution fees / expenses – overhead)
   f. <u>Series cost of production:</u> actual out of pocket expenses incurred by the studio.
   g. Frequent disagreements about how to handle tax incentives
41. <u>First Look Deal:</u> agreements by which talent gives studio an exclusive first opportunity to develop or produce projects owned by others.
42. <u>Co-production agreement:</u> agreement between two studios that agree to jointly own, finance and produce a series. They typically arise in the following scenarios:
   a. When two different studios control separate elements (rights and talent)
   b. Often one studio is affiliated with the commissioning network.
      i. <u>Note:</u> Hulu now requesting this role.
43. <u>Initial Network License Agreement:</u> the deal under which a television series is first commissioned and exhibited by an American licensee.
   a. A television studio makes money by using the divisibility of its copyrights to maximize revenue across <u>media</u>, <u>territory</u>, and <u>time</u>, so the goal of a studio in negotiating a network license agreement is to grant the network as <u>few rights</u>, in as <u>few territories</u>, for a <u>brief a term</u>, and for as much money as possible, retaining for itself as much freedom as possible to further license the same series to additional licensees across various platforms, countries, and time windows.

44. The type of network involved whether broadcast, cable or streaming significantly affect this agreement and the level of risk and reward.
    a. Capital at risk: Broadcast networks require studios put a lot of capital at risk, cable much less, and streamers almost none.
    b. Rights: Broadcast and cable leave a lot of high-value rights and windows open whereas digital platforms buy all the rights leave little economic upside for studios.
45. The size of the license fee depends on a host of factors:
    a. Desirability of the project.
    b. Budget.
    c. The scope of rights (media, territory, and time).
    d. Series term of license agreement.
    e. Extent of network's holdbacks on studios reserved rights.
46. Motivations: Studios looking to monetize a bundle of rights and networks are focused on ratings and resulting ad advertising sales to recoup its license fees and marketing costs.
47. Series budget ranges (Table 8.1)
    a. 30-minute comedy: Pilot $1-2M; $500k - $3M
        i. Most comedies fall into the $1M-$2.5M range.
    b. 60-minute drama: Pilot $5-12M; $2M - $6M
        i. Most dramas fall into $3M-$4.5M range.
48. Scripted Television operates on the deficit model meaning the initial license fee is less than the cost of production and the deficit is the studio's at-risk investment.
    a. In seasons 5 and 6, the license fee goes to 100% of the cost of production.
49. Studios who negotiate license agreements with digital platforms charge a premium based on the opportunity cost of the scope of rights desired by the digital player.
    a. Its advantageous for these players to produce their own content and not rely on outside suppliers but the competition for talent is fierce.
50. *Networks can only exploit the rights licensed to them so any change in its business model or distribution scheme can reveal rights gaps and studios make these rights expensive to fill.*
51. A co-production is a risk mitigating structure but from an affiliated studio perspective it can be economically attractive.
    a. Networks will agree to allow the studio to take risk for developing then want 50% participation to the upside.
        i. Economics show why this is so productive: if initial license fee is 50% and deficit is 50%, for 25% more, (75% v. 50%) you share in 50% of the upside.
        ii. Cable is even better given license fee is usually 75%, so for 12.5% more, you get to share in 50% of the upside.
            1. This is most likely why cable networks started up their own studios.
    b. Two primary categories of duties typically allocated: which studio leads physical production and which one controls distribution rights.
        i. Domestic market most valuable for comedies and international market for dramas.
52. *Example of economics of television series:*
    a. The per-episode cost of a series goes down as episodic orders go up because fixed costs amortized across greater number of episodes.
    b. License fees negotiated on a per episode basis so more aggregate revenue.
53. Unscripted series tend to be less successful in terms of re-runs and syndication.
54. Major studios are built to maximize the value from exploiting retained downstream rights and must find lucrative hits to balance out unsuccessful projects.

    a. Studio is like a VC or investment portfolio.

55. Market fragmentation has reduced viewership and advertising revenue.
    a. Networks trying to limit license fee commitments and will renew middling performers rather than bear expense of creating something new.
    b. That said, ballooning budgets keep happening to stand out in the marketplace.
56. MVPDs have consolidated to have more leverage in carriage negotiations and retransmission consents.
57. Consolidation will force a lot of changes in how media companies manage risk and seek upside.
    a. Digital players rights hungry purchases are lower margin and cap upside which means les mega hits for studios.
    b. Media conglomerates curb investment in niche cable networks because they can't get distribution should the bundle fall apart?
58. Launching an over-the-top services requires huge investment in content, infrastructure, and marketing, and the companies who have successful have been:
    a. First-mover advantage (Netflix)
    b. Industry affiliate subsidization (Hulu, via its ownership structure),
    c. Massive deployable resources and complementary lines of business (Amazon and Apple)

What I got out of it

1. A good understanding the television ecosystem and the various agreements that make the industry go as well as the economics of the entertainment ecosystem.
2. A networks business model really determines what kind of shows it wants to order and what scope of rights it desires.
    a. Broad versus narrow rights: Netflix / Amazon versus Broadcast / Cable
    b. Broad appeal versus niche: Broadcast / Cable (for advertising $) versus Netflix Amazon (more niche) as a tool to add subscribers and / or reduce churn

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