Getting upfront and personal for network advertising dollars

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MENTION the term “TV industry” and people might conjure up a glamorous image of Kate Walsh and Patrick Dempsey in formal attire, splashed by klieg lights. But what really rules the profession is mathematical and dull and not sexy at all. It's those statistics known as ratings, and they're about to form the basis for a major behind-the-scenes battle.

Every network has a research department that slices and dices the numbers from Nielsen Media Research, in hopes of convincing advertisers that tens of millions are watching or, if that fails, that at least a goodly portion of high-income, highly suggestive people ages 18 to 49 are watching. TV research is about as scintillating as an Internal Revenue Service form, but these industry drones do the scut work that winds up paying for Walsh's pedicures and Dempsey's hair gel.

Right now, though, the big TV networks are on a collision course with the advertisers that subsidize their shows, including the big hits like ABC's "Grey's Anatomy," Fox's "American Idol" and NBC's "Heroes." The battle has the potential to get very ugly indeed over the next few weeks. And it's all about ratings — or, more specifically, how to measure and assign monetary values to the rapidly dwindling broadcast TV audience in our era of TiVo and the Internet.

Why should you, the average viewer, care?

Because what happens will decide how and what you watch, what devices you watch it on and how much you pay for that privilege. And although no one has all the answers, these questions are going to be decided starting now, not at some fuzzy point in the unseen future.

Today, NBC will officially unveil its fall schedule for advertisers in New York, with other networks following this week. Then the networks' salespeople will enter several weeks of negotiations with advertisers' representatives over the bulk of commercial time, which is bought in advance for the new season — an annual rite known as "the upfront." Last year, advertisers salted nearly $9 billion among the five English-language broadcast networks during these preseason negotiations. Both sides seem to agree that the figure will likely be flat or even lower this year, as networks frantically try to hold the line against years of audience erosion.

Of course, advertisers and TV networks have had a love-hate relationship for more than half a century. But this year will bring some key differences.

For the first time, advertisers will come armed with Nielsen data showing how many people actually watch commercials, instead of, say, zapping through them with digital video recorders, which cable and satellite operators had helped push into an estimated 20% of U.S. homes by the end of 2006. (By December, nearly one-third of American homes will have the devices, according to Forrester Research.)

And that's not all. Nielsen has also greatly enlarged the proportion of DVR users in its statistical sample this season. That cuts both ways for the networks: On the one hand, it's bound to make the "live" viewing of broadcasts appear significantly smaller than before. But Nielsen also offers another set of numbers, which includes viewers who save programs on DVR and watch them up to one week later. That naturally boosts the final number, which networks like.

None of this data has been part of the ad-buying derby before, and that's why there could be a few chairs thrown during the conference-room horse trading this time.

Advertisers are demanding to pay only for those viewers who watch a program "live" during its initial broadcast, arguing (correctly, according to recent research) that the...
vast majority of DVR users skip most ads anyway. Network executives counter that viewers are viewers and that discounting "time-shifted" watching grossly underestimates the true reach of a show. (If the network position sounds crazy to you, just remember this: Despite years of audience erosion, the big broadcasters have until recently persuaded advertisers to pay more each year on a per-viewer basis. Pay more, get less? Yep — on the grounds that network TV is the only remaining mass medium.)

"This will be the crux of our impending upfront negotiations," said John Rash, senior vice president at Minneapolis ad firm Campbell Mithun, which represents large ad clients buying network TV time. He added that advertisers want to stick with comparing measurements of "live" viewing "because of how we believe people actually watch TV" (and because, he might have added, it'll inevitably prove cheaper to buy time that way).

But that's just it. How people watch TV is changing faster than even industry analysts can keep up with. Viewers set their own schedules with TiVos. They watch a lot of DVDs, not just of movies but of TV series too. They watch TV on YouTube.com or FunnyOrdie.com. They watch TV on their iPods. And although executives may be pained to hear it, viewers like to watch TV without ads. A few years ago, when he ran the WB Network, Jamie Kellner implied that network viewers who skipped ads were committing a kind of theft. (Maybe the threat of jail time would make you think twice about that bathroom break during your favorite show.)

Is everyone watching TV in all these wacky ways? No, not yet — Grandma probably isn't downloading "The Office" on iTunes. But enough people are changing their behavior that the statistics are starting to be affected, and not in ways that network executives like.

"2006 was a big year, as we nearly doubled the households with DVRs, making everyone in the industry sweat, as you're seeing in the prime-time audience drop," Forrester analyst James McQuivey wrote me in an e-mail last week.

Audience drop? Oh, right, about that.

It's not coincidental that this whole debate is unfolding at an atrocious time for the network TV business. Ratings this season have generally been lousy — among the key demographic of viewers ages 18 to 49, every network is down this season compared with last year (except for Fox, which is flat), according to Nielsen. And the drop-off has accelerated to downright alarming proportions this spring, as even onetime hits such as "Lost" and "24" have slumped to their lowest ratings ever. NBC earlier this year logged the least-watched week in its history. Not content with that dubious achievement, the network turned around and set another record low the following week.

TV executives have various explanations for the bad numbers. Daylight savings time started three weeks early this year, which made people stay outdoors longer. Fox's monster hit "Idol" continues to upset the harmonic rhythms of the TV gods. There are too many darned repeats. Too many programs stink (compared with when, exactly?). And so on.

But it's clear that DVRs are having more impact than any other single factor on the networks' shaky business model. And everyone knows it.

Advertisers simply aren't going to pay as much as they used to, in absolute terms, for conventional 30-second commercials. And networks are going to have to get a lot more creative about what might be called alternative revenue sources. McQuivey points out that networks are already charging a premium of 20%, on a per-viewer basis, for ads that run with TV shows on the Web, as opposed to those that air on broadcast. And new video-on-demand systems will make ad-skipping impossible.

And guess what? It's only going to get more complicated. Instead of counting their revenue in billions during every spring's upfront, network execs will be forced to squeeze dollars here and there from every iteration of new technology that engineers can devise.

Good news for average viewers: You'll have more choice. Bad news: You'll have more bills.

Sound familiar?

As McQuivey said, "Once the PC and TV get connected, then watch out."

But we don't have to wait till then for things to get interesting. Ad buyers and network suits may have their most crucial talks ever later this month. Some of them might even be more entertaining than what's on TV.
Whence the tar pit bubbles?

By Jia-Rui Chong

Someone's belching a lot of methane. PHOTOS

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