

Television Community Service Grant (CSG) 2007 Review

CPB Management Recommendations

Executive Summary

In July 2006, the Corporation for Public Broadcasting (CPB) convened a panel of system leaders to review the policies governing the distribution of television Community Service Grant (CSG) funds. The panel completed its deliberations in April 2007, recommending a number of changes designed to increase CSG grantees' abilities to serve their communities. CPB management has reviewed those recommendations, and, after minor modifications, is presenting their recommendations to the CPB Board for their approval.

CPB management's full recommendations are described in more detail in the body of this document. In summary, they are:

1. Continue the current overall approach to distributing CSG funds:

After analyzing the policies implemented in response to the past three TV CSG reviews – 1996, 1998, and 2001 – to determine their effectiveness in promoting high-quality public television service across the public television system, CPB management agrees with the review panel that, on the whole, past policies were generally effective in achieving the desired objectives, particularly in supporting small stations, multi-transmitter stations and differentiation in Multi-Provider (“Overlap”) Markets.

Given the general effectiveness of the current policies and the fact that the federal appropriation is not likely to grow significantly over the short term (ensuring that any significant change in CSG policy that benefits one group will penalize another), CPB management believes that significant changes in the CSG formula should not be implemented at this time to allow CSG funding to remain a stable and predictable source of revenue for stations.

2. Promote program differentiation in Multi-Provider Markets:

In Multi-Provider Markets (formerly referred to as “overlap” markets), CSG policy should encourage rich and varied program services, not increased investments in infrastructure. CPB management believes that public television enhances its reach and impact when stations serving the same community offer complementary program services. To encourage multiple services in Multi-Provider Markets, the Program Differentiation Incentive is offered to secondary stations. CPB management recommends that this policy continue with some modifications to the definition and compliance guidelines.

- a. The current definition of program differentiation should be updated. For a secondary station to be eligible for the PDI, it must certify that no more than 10 percent of its schedule duplicates the schedule of any other station in the market.
- b. Compliance monitoring of program differentiation should be increased. Stations found falsely certifying compliance with this policy may lose their Program Differentiation Incentive for up to three years.
- c. The existing policy of sharing one base grant among all grantees in Multi-Provider Markets should be continued.

3. Support small stations:

CSG management recommends three modifications to existing policies that support small stations in order to ensure that all small stations benefit equally from current policies.

- a. Currently, stations with NFFS below \$800,000 must obtain an annual waiver to remain in the CSG program. CPB management recommends that any station with NFFS below \$800,000 should be allowed to automatically remain in the CSG program as long as they can provide a clean audit.
- b. The current method of calculating the Local Service Grant (LSG) portion of the CSG shifts a disproportionate share of LSG funds to stations with extremely low NFFS. CPB management recommends adjusting the method of calculation to improve the equity of the distribution of these funds.
- c. NFFS of \$2 million is currently the threshold for eligibility for the LSG. CPB management recommends that small stations remain eligible for the LSG and other small station programs if their three-year average NFFS is below \$2 million. This will reduce the fluctuation of stations inside and outside of these programs.

4. Where necessary, clarify existing CSG Policy:

CPB management recommends updating or clarifying the following existing policies:

- a. There is a transitional issue related to digital conversion in the calculation of the Distance Service Grant (DSG). CPB management recommends that grantees be allowed to substitute a digital transmitter and/or translator for an existing analog transmitter and/or translator without penalty under the DSG.
- b. CPB management supports the efforts of station leaders who wish to consider merging facilities. To remove any disincentive to mergers or joint operating agreements, CPB will develop practices that allow merging entities to maintain their eligibility for CSG funding as if they continued to operate as separate organizations. The period of time of this favorable treatment would vary depending on particular circumstances, with four years as the recommended minimum period.
- c. Some grantees have experienced unintended difficulties related to sudden swings in NFFS as a result of unusually large gifts or other revenue. CPB management recommends that grantees be given the option of amortizing over three years any gift that accounts for 10 percent of its total NFFS for any single year.
- d. CPB will develop practices to make grantee financial data reported on the Annual Financial Report (AFR) and audited financial reports available upon request by the public, and all requests will be shared with grantees as quickly as possible.

5. Refer issues that go beyond the CSG panel to other forums:

The panel reviewed a wide variety of issues that relate to station finances and the impact of CSG policy and other industry practices on station performance. It was agreed that a number of issues that affect station performance are not related to CSG policy and are best addressed through other means. These include issues related to PBS dues, PBS program pricing, and station efficiency. In addition, there was interest in examining new ways to increase system revenue so that CPB is not in a position of simply redistributing a fixed amount of funds. CPB management recommends that these issues be taken up by relevant organizations such as PBS and the Affinity Group Coalition.

Public Television Community Service Grant (CSG) 2007 Review CPB Management Recommendations

According to the Public Broadcasting Act section (k)(6)(B), funds shall be distributed to public television stations based on eligibility criteria "...which the Corporation shall review periodically in consultation with public radio and television licensees or permittees or their designated representatives...." In accordance with this statute, CPB convened an advisory panel to review current CSG policy and to propose any changes to CPB management that the panel believed would enhance grantees' abilities to serve their communities. This panel was composed of members of the Affinity Group Coalition and representatives from PBS and APTS; the group met five times between July 2006 and April 2007. The members of the advisory panel may be found in Appendix A.

To inform its deliberation, the panel sought input from the broader public television system throughout the review process. The panel systematically shared its progress with various Affinity Groups on regular calls, and also consulted the broader public broadcasting system via email, during the Round Robin meetings, and at the PBS Planning Meeting. These recommendations were then presented to CPB management.

After review and minor modifications, CPB management is now presenting its recommendations to the CPB Board for consideration at its August 2007 meeting. Any areas where CPB management has modified the panel's recommendations are noted in the text below.

I. Background

As required by statute, CPB convenes a station advisory panel to review CSG policy every few years. The most recent reviews were conducted in 1996, 1998 and 2001. At each of these reviews, panels have recommended policy changes in the context of the federal funding situation and the state of the system's financial health.

The 1996 consultation, for example, took place in an environment of congressional concern about the overall efficiency of public television and particularly about the perceived overbuilt infrastructure in Multi-Provider Markets. The changes in CSG policy resulting from the 1996 consultation were significant and designed to respond to these congressional concerns. Changes included modifications to base grant calculations and the creation of a variety of special funds designed to improve the efficiency and fundraising effectiveness of public television. This panel also recommended the current "overlap" definition and suggested policies designed to encourage stations serving the same area to pool operations. The next two reviews – in 1998 and 2001 – refined and solidified the changes made in 1996. Each panel also recommended policies to provide additional support to classes of stations that were coming under economic stress. The 1998 panel, for example, suggested a range of programs to support small stations and the 2001 panel recommended policies to support the efforts of licensees operating multiple transmitter networks that cover significant geographic areas. Appendix B summarizes the results of those reviews.

This current review was held under the long shadow of the 2009 analog shutoff. This impending cutover to digital broadcasting has placed a serious economic burden on the system as stations work to convert their operations from analog to digital. It has also sparked uncertainty in the industry, as the impact of the move to digital on viewership, membership and competition all remains to be seen. Many of the current CSG policies that were developed for the legacy analog system will, in all likelihood, need to be re-examined when full digital broadcasting begins and the impact of the resulting multi-channel environment on the system

becomes clearer. Indeed, several of the recommendations made below are intended to provide short term solutions until the longer term impact of the conversion can be seen.

The difficult financial environment was also an important backdrop of this review. Of special concern was the flat level of federal funding experienced over the last two years and anticipated to extend for two more years. Under these conditions, a change in CSG policy would shift funds from one class of grantees to another, creating winners and losers. In the absence of a clear and compelling case for change, CPB management recommends maintaining current policy in order to avoid doing further financial harm to any grantee cohort.

II. Recommendations

1. Continue the current overall approach to distributing CSG funds

CPB staff and the review panel spent a great deal of time examining the state of the system and analyzing the impact of existing policies – specifically those instituted in the last three reviews – on all grantees. We were particularly interested to see if certain types of grantees had been uniquely disadvantaged by these policies and whether stations targeted for assistance benefited appropriately. To study this issue, we segmented public television grantees into a variety of station cohorts by both size and by licensee type. We then reviewed 10 years of data including changes in NFFS and in CSG, and considered the impact of these changes on station finances after application of the PBS dues formula. The purpose of this analysis was to determine whether recent CSG policy had caused any significant unintended benefit or penalty to any station cohort either in terms of the CSG itself or overall financial performance. We found that, by and large, no group experienced undue or unexpected benefit or harm because of changes in CSG policy and therefore concluded that the general approach currently in place to distribute CSG funds is appropriate.

In addition to reviewing this data, we were also aware that, in a period of flat funding, any change in CSG policy to benefit one cohort of stations would necessarily cause a financial loss to others. We are wary of recommending a change in CSG policy that would have such an effect for two reasons. First, the creation of classes of “winners” and “losers” within the public television community would be a detriment to the system overall. Second, based on feedback at the Round Robin meetings and within the Affinity Groups, we recognize the importance of the CSG as a constant, reliable source of funding at a moment in time when so much else is in flux. While we would have been willing to shift funds across the grantees if there were a class of stations that was being truly disadvantaged by current policy, the relative parity across the system in financial performance combined with system input suggested that major change was not advisable at this time.

Recommendation: CPB reaffirms the major provisions of current CSG policy since past and current policies have proved to be generally effective in achieving the statutory objectives of universal service and high quality public television service.

2. Promote program differentiation in Multi-Provider Markets

Public television most effectively serves the American public when it offers a wealth of content and service and when grantees in a single market do not offer duplicative programming in direct competition to one another.

In today's media landscape, signals from multiple public television stations are available to viewers in many communities, particularly viewers who subscribe to cable television or DBS services. Under current policy, CPB has designated 17 markets as being "overlap" markets, listed in Appendix C. (Going forward, CPB will adopt the term "Multi-Provider Market" as a more descriptive, neutral designation for these markets.)

In Multi-Provider Markets, CPB has defined two classes of stations. The "primary" station is the grantee with the largest NFFS; "secondary" stations are all other grantees in the market. In order to promote differentiation of public television programming in these Multi-Provider Markets, current CSG policy provides a Program Differentiation Incentive (PDI) to secondary stations that differentiate their programming from primary stations in these markets. The PDI increases the amount of a secondary station's CSG, helping to compensate for the additional costs of airing a differentiated schedule, such as the cost of time-shifting content.

CPB management recommends making two modifications to the PDI program: refining the current definition of differentiation and increasing compliance monitoring of the program. Each of these is described in detail below.

A. Refine the definition of program differentiation in Multi-Provider Markets

The current definition of program differentiation was created in 2001. A station's programming is considered differentiated:

"...when its mission and service are reflected in broadcast content that is primarily targeted to unserved and underserved audiences and/or provides an alternative to the primary station. That is, a station that provides:

- Non-English language programming,
- ITV or other educational broadcast content,
- National content that is non-duplicative of the primary station in its content and/or time of day (time-shifted).

"The desired outcome of this policy refinement is to increase diverse local services within overlap markets."

Revised Definition:

CPB management recommends that this definition be refined so that it is more specific and measurable. The proposed revised definition is as follows:

- Programming that expands the choices available to viewers, such as non-duplicative content acquired from sources other than PBS, or
- Programming that is time shifted to provides audiences with increased access to programs and series distributed by the PBS National Program Service (NPS), and
- Programming that is non-duplicative of that of all other stations in a Multi-Provider Market at least 90 percent of the time the station is on the air.

To qualify for the Program Differentiation Incentive, CPB management recommends that we require secondary stations to certify that they have broadcast a minimum level of differentiated or non-duplicative programming *during the prior year*. That programming should be distinct for at least 90 percent of the hours

that the station broadcasts 24 hours a day, 7 days a week, 52 weeks a year (with no exception for pledge programming) in order for the station to be eligible for the PDI.

CPB management recommends that programming be considered as non-duplicative when no part of a specific program episode on one station overlaps the same program episode on another station. For example, starting a 60-minute episode of *Nova* on one station 30 minutes after the same episode has begun airing on another station will be considered duplicative. However, different episodes of the same series aired at the same time would be considered non-duplicative.

Finally, CPB recommends that, in order to be eligible for a PDI, a station's programming must be differentiated from *all* other stations in the Multi-Provider Market. The current policy requires only that secondary stations differentiate their programming from the primary station. The current policy is silent on the question of whether stations in Multi-Provider Markets with more than two stations must differentiate from each other.

The original creation of the Program Differentiation Incentive was considered primarily in an analog, over-the-air environment. CPB management recognizes that duplicated programming among stations will increase in a multi-channel, digital environment. For the present, CPB management recommends that only the programming on a station's primary channel be included in the calculation of a differentiated program service. At the next review panel, this is a topic that should be reconsidered to understand the relevancy and effectiveness of the PDI in a multicast environment.

Recommendation: CPB will update the definition of program differentiation in its Program Differentiation Incentive policy to one that is specific and measurable.

B. Verify compliance with PDI requirements

CPB management recognizes that it is important for grantees receiving a PDI to comply with the differentiation definition stated above. To ensure that stations receiving the PDI are eligible, we recommend developing a two-step compliance policy.

Step 1: Self-certification

Every eligible secondary station wishing to receive a PDI would be required to certify that its previous year's programming was differentiated from every other station in the Multi-Provider Market. Secondary stations would be required to maintain and supply to CPB upon request adequate records and supporting documentation to verify the certification. Primary stations would be encouraged (but not required by CPB) to maintain records of their previous year's schedules and would be expected to be able to provide appropriate and relevant data if filing a complaint against another public television station operating within the market.

Step 2: Annual Review

CPB would verify station certification by reviewing a small number of markets each year as part of its normal desk audit process. In doing so, CPB would examine several weeks of programming. If duplication is found in any week in excess of 10 percent, CPB may find that the station (or stations) has falsely certified its eligibility for a PDI. While primary stations would not be required to maintain records of their previous

year's schedule, CPB's ability to review differentiation in any market in which the primary station failed to maintain adequate records would be limited.

CPB would accept complaints about undifferentiated programming from other stations in the same market. These complaints would serve as one factor in selecting markets to verify. CPB would encourage stations to work together to resolve conflicts over program differentiation, however, before they lodge a complaint.

Penalties:

Stations that falsely certify differentiated programming on a repeated or intentional basis should be penalized. CPB management recommends that this penalty be loss of eligibility for the Program Differentiation Incentive for up to three years.

Recommendation: CPB will develop a mechanism to verify that stations receiving a PDI maintain a differentiated program schedule. Stations with a pattern of non-compliance may lose their PDI for up to three years. Stations filing complaints should support their concerns with relevant data.

C. Maintain the current policy of evenly distributing one base grant in each Multi-Provider Market

In addition to refining CPB's policies around the PDI program, CPB staff and the review panel spent a considerable amount of time reviewing the current policy of distributing one base across all the stations in Multi-Provider Markets. This topic was addressed at multiple panel meetings and was the hardest issue on which to reach consensus.

The current base grant policy was recommended by the 1996 panel partly in response to congressional interest in what were perceived to be overbuilt public television facilities. At that time, CPB developed the concept of Multi-Provider Markets (then called "overlap" markets) and defined the base grant as an infrastructure grant that would provide a basic complement of public television facilities in each market. In Multi-Provider Markets, one base grant was divided among all grantees in the market. Each grantee continued to receive a full NFFS incentive grant. The total amount saved by reducing the number of base grants was put into a fund to support station collaboration or consolidation in these markets. Much of this available funding to support collaboration went unclaimed, and in 2001 the undistributed money in this fund was returned to the CSG pool.

CPB staff and the panel spent considerable time over the course of several meetings discussing both the philosophical underpinnings and the financial impact of this policy on the system. While there was both support for and sentiment against the concept of the base grant as an infrastructure grant, CPB management recommends that the current policy be maintained.

During this review, we examined three models for increasing CSG funds for grantees in Multi-Provider Markets:

- Providing full base grants to all grantees in these markets,
- Providing every grantee in these markets with a half-base grant, regardless of the number of grantees in the market,

- Allowing all grantees in a Multi-Provider Market to have access to PDI funds.

The financial impact of each of these approaches is outlined below.

➤ **Full Base Grant**

We examined the impact of providing each grantee in a Multi-Provider Market with a full base grant. Approximately \$9.6 million would be drawn from the incentive pool to fund this scenario. As a result, grantees not in these markets would see an average CSG decrease of \$21,500, with a range of \$1,800 to \$355,000. Under this scenario, 139 grantees, over 80 percent of the system, would receive reduced grants.

➤ **Half Base Grant**

Of the 17 Multi-Provider Markets, six have more than two grantees. In these markets, the base grant is split equally among all the grantees. For example, each grantee in a market with three grantees receives one-third of the normal base grant. In order to provide additional funds to markets with more than two grantees, we examined the impact of providing all grantees in Multi-Provider Markets with half a base grant.

Approximately \$1.3 million would be drawn from the incentive pool to fund this scenario. As a result, grantees outside of the six markets would see an average CSG decrease of \$7,000, with a range of \$223 to \$115,000. Under this scenario, 157 grantees, over 90 percent of the system, would receive reduced grants.

➤ **Program Differentiation Incentive to all Multi-Provider Market stations**

We examined the possibility of expanding eligibility of the PDI from secondary stations in Multi-Provider Markets to both primary and secondary stations in these markets. Approximately \$1.5 million would be drawn from the incentive pool to fund this scenario and directed to the primary stations. As a result, grantees outside of Multi-Provider Markets would see an average CSG decrease of \$9,600, with a range of \$384 to \$131,500. Secondary stations in Multi-Provider Markets would also lose CSG funds and would see an average CSG decrease of \$12,400 with a range of \$4,560 to \$26,700. Under this scenario, 162 grantees, over 93 percent of the system, would receive reduced grants.

In addition to the loss of funds to secondary stations and all other stations, CPB management believes that expanding the PDI to primary stations runs counter to the philosophy of the program. Secondary stations often face additional costs to differentiate their programming and they are not able to fully capitalize on PBS's marketing and advertising for NPS programming. The PDI is designed to help offset such costs, not to provide additional support to the primary stations in the market.

After a thorough review of these options, CPB management recommends that we maintain the current policy. In management's opinion, the current policy encourages stations in Multi-Provider Markets to deliver service efficiently while still providing local programming. This was the rationale outlined by the 1996 panel and it remains as relevant today as it was then.

Recommendation: CPB should maintain the current base-grant policy in Multi-Provider Markets. While the panel felt that this issue should be raised again at the next review, particularly if federal funding increased significantly, CPB management supports the existing policy and endorses the basic rationale outlined by the 1996 panel, regardless of the level of federal support.

3. Support small stations

The Public Broadcasting Act points CPB towards the goal of universal service, defined as the provision of public broadcasting service to every household in the U.S. Today, public broadcasting has largely achieved the goal of universal service, with over 99 percent of the U.S. population able to access public broadcasting.

CPB and the public television system have long recognized the special challenges that small public television stations face in providing service to their communities, and in helping achieve CPB's goal of universal service. Many of these small stations operate in rural communities with limited financial resources.

For many years, CPB has had a variety of provisions in its CSG formula that provide special assistance to small stations. "Small stations" are currently defined as grantees with less than \$2 million of NFFS. CPB staff and the panel spent significant time reviewing these provisions that support small stations. In this area, CPB management recommends the following three amendments to our current policies and programs: ease the basic eligibility requirements for small stations already in the CSG program, modify the Local Service Grant calculations to ensure greater equity across small stations, and allow small stations to use a three-year average NFFS to determine their eligibility for small station programs. Each of these recommendations is described in more detail below.

A. Ease eligibility requirements for the smallest stations already in the CSG program

As a general rule, a grantee must have a minimum NFFS of \$800,000 to be eligible to receive a CSG. CPB has a long-standing practice, however, of allowing grantees with NFFS under \$800,000 to continue receiving a CSG under certain circumstances. First, a grantee may have suffered a traumatic event that resulted in a temporary loss of NFFS – for example, a sudden, unanticipated drop in support from state funding. If CPB management believes that the grantee will recover from the event, it will waive the minimum NFFS rule to allow the grantee to continue in the CSG program. Second, a grantee may operate with less than \$800,000 on a continuing basis, finding a way to achieve financial stability and provide meaningful community service with minimal resources. Under today's practice, any station with NFFS below \$800,000 must write to CPB annually and request that we waive the NFFS minimum requirement for that year. Going forward, CPB management recommends that grantees with NFFS below \$800,000 be automatically allowed to continue in the CSG program provided that they continue to receive clean audits, with no audit findings that question the grantee's continuing operating viability.

Recommendation: CPB will allow stations with NFFS below \$800,000 that are in the CSG program today to automatically be eligible for a CSG assuming they continue to receive clean audits, with no audit finding that question their continuing operating viability.

B. Ensure equity in Local Service Grant calculations

Under the current CSG policy, all small stations (i.e., grantees with NFFS of less than \$2 million) receive a Local Service Grant (LSG). Each year, CPB withdraws \$3 million from the CSG pool and distributes the

funds to eligible small stations in inverse proportion to their NFFS. The smaller the grantee's NFFS, the larger the LSG the grantee will receive.

We spent a considerable amount of time reviewing the mechanisms of the current LSG program and found that the current method of distributing LSG funds in inverse proportion to NFFS resulted in a sub-optimal allocation of these funds. Because there are some stations in the CSG program today with NFFS well below \$800,000, the current formula provides these stations with unusually small NFFS a disproportionate share of the \$3 million at the expense of all other small stations. In some cases, the LSG for these very small stations is larger than their NFFS. CPB management believes that this is inconsistent with the purpose of the LSG, which is to supplement the CSG rather than to provide the majority of the station's federal support.

To ensure that the LSG funds are more equitably distributed across all small stations, CPB management recommends that LSG formula be modified. We recommend freezing the NFFS component of the LSG calculation at \$800,000 for grantees with NFFS of less than \$800,000. In other words, for the purposes of this grant calculation, CPB would calculate grants for the smallest stations as if their NFFS was \$800,000 in order to ensure that they do not receive a disproportionately large share of the funds.

This change will significantly affect three grantees. To minimize the impact of this change, CPB management recommends that this policy be phased in over three years so that these grantees are not unduly disadvantaged in a single year. CPB management also recommends that one very small grantee be exempt from this policy because it provides the sole broadcasting service – either public or commercial – to its community.

Recommendation: CPB will implement an \$800,000 NFFS floor in the LSG grant calculation. This floor should not apply to television stations that provide the sole broadcast service, public or commercial, to their communities.

C. Refine small station eligibility

Today, grantees are eligible for the LSG and several other CPB-funded, non-CSG programs if they have NFFS below \$2 million. A small number of grantees have seen their NFFS fluctuate around the \$2 million cut-off. To prevent a small increase in NFFS from having a drastic impact on CSG funding, CPB management recommends that we use a three-year average to determine small station status for those stations with NFFS hovering around \$2 million. The three-year averaging would only be used for grantees that had NFFS below \$2 million at least once over a three-year period.

Recommendation: For grantees with NFFS near \$2 million, CPB will use three-year averaging in computing NFFS for the purpose of determining eligibility for small station status in CSG calculations.

4. Clarify existing CSG policy

A. Update Distance Service Grant eligibility

Distance Service Grants (DSG) provide supplemental CSG funding to grantees that operate multiple repeater transmitters or translators to distant communities. Current CSG policy states that grantees that serve distant populations with repeating transmitters are eligible to receive Distance Service Grants (DSG).

Repeater transmitters help the system achieve the goal of universal service, and grantees that operate them often bear additional costs to maintain transmission facilities in distant communities. The DSG helps to offset this cost.

Under current CSG policy a grantee is eligible to receive a DSG if it operates three or more distant transmitters, or an equivalent combination of transmitters and translators. The DSG increases with the number of transmitters the grantee operates. For the purposes of the DSG, ten translators equal one transmitter. Today, 38 grantees receive a Distance Service Grant.

Digital transmitters were not included in this calculation when the policy was created in 2001. As the digital conversion of 2009 approaches, CPB management expects that more grantees will be converting from analog to digital transmitters and will want digital transmitters to be counted in their DSG calculations. We recommend that grantees be allowed to substitute digital transmitters and/or translators for existing analog transmitters and/or translators without penalty. New digital transmitters and translators that provide service to new geographic areas should also be included in the DSG calculation just as an analog facility would be in the current policy. If a grantee chooses to continue operating an analog facility while adding a digital transmitter or translator to serve the same area, however, only one transmission facility should be counted in the calculation.

Recommendation: CPB will allow grantees to substitute a digital transmitter and/or translator for an existing analog transmitter and/or translator without penalty.

B. Clarify funding policies for merging grantees

In recent years, the changing media environment has caused many public television stations to revisit their business models and rethink the way that they operate. Included in such considerations are the questions of closer cooperation and mergers among licensees. CPB staff and the panel reviewed these issues noting that some stations have decided to merge, combining resources and scale of operations to save money or better serve local community needs. Mergers and collaborations often reduce the cost of operation, at times allowing a station to improve service and, in some cases, preserving public television service to a local community that would otherwise be lost.

Grantees that merge often face the immediate loss of a base grant, a Local Service Grant, and the Program Differentiation Incentive. This reduction in CSG can often pose a significant financial barrier to the merger and offset the financial benefits that might have otherwise resulted from combining operations. The loss can be significant enough to stop the merger.

CPB management recognizes that local television managers and their boards are best able to judge whether a merger is in the interest of their communities and believes merging grantees should be “held harmless” from CSG reductions that would result from the merger. CPB management recommends that we modify CSG policy to allow a newly merged entity to receive all the funds that would have been granted to each of the separate grantees before the merger for an extended transition period. This transition period should vary based on the specific circumstances of the merging grantees.

Specifically, CPB management recommends that the policy differentiate between merging grantees that serve the same community and merging grantees that are more distant. CPB management also recommends that

the policy differentiate between merging grantees with relatively large NFFS and grantees with small NFFS or mergers where one grantee is large and the other distant.

CPB management recommends that the minimum “hold harmless” period for merging grantees be four years for the largest grantees serving the same market. CPB management would like the flexibility to use its discretion in defining “hold harmless” periods for grantees merging in more challenging circumstances. In the most extreme cases when, for instance, a large grantee agrees to merge with a small grantee that is located some distance away and is about to fail, the “hold harmless” period may need to be very long. The need to be flexible must be balanced with CPB’s management concern about the difficulty of managing indefinite commitments. CPB management therefore recommends that the “hold harmless” period in these cases be structured so as to allow periodic review.

Recommendation: CPB will allow merging grantees to receive CSG support based on pre-merger eligibility for a transition period. This period should vary by the circumstances of the grantees merging but should be a minimum of four years.

C. Amend reporting guidelines for one-time major gifts in NFFS

Several grantees have raised the concern that while a one-time major gift creates a significant increase in NFFS for a single reporting year, it also causes PBS dues to increase over several years. With the progress of the Major Giving Initiative, it is likely that more grantees may find themselves receiving significant major gifts and may face this situation.

Large one-time gifts can also become an issue for grantees with NFFS below \$2 million. In some cases, a large major gift can raise their NFFS above \$2 million and make them ineligible for small station funds such as the LSG for that one year. This scenario can be particularly challenging if the major gift is restricted since restricted major gifts are included in NFFS but may not be available to support station operations.

To help ameliorate this issue, CPB management recommends that grantees have the option of amortizing large gifts over several years. Only gifts that represent 10 percent or more of a grantee’s total NFFS should be eligible for three-year amortization.

Recommendation: CPB will allow grantees the option of amortizing over three years gifts that are 10 percent or more of a single year’s NFFS.

D. Release AFR grantee data

By statute, grantees must make their Annual Financial Report and audited financial statements available to the public upon request. The “public” includes members of the press and individuals representing other stations. Currently, CPB refers requests for station data to the appropriate local station, but going forward CPB management recommends that we make this public information available directly to a requestor. CPB would then notify grantees in as timely a manner as possible once we have received such a request.

This policy does not apply to SABS data which is not subject to the public disclosure requirement.

Recommendation: CPB will make a grantee's Annual Financial Report and audited financial reports available upon request by a member of the public. CPB will communicate the request to the grantee as quickly as possible.

5. Refer issues that go beyond the CSG panel to other forums

CPB staff and the panel reviewed a number of issues that were beyond the scope of the Community Service Grant, including PBS dues and system efficiencies and mergers. CPB management believes these are important issues for the system to debate, but contends that they would more appropriately be addressed by other organizations in the system

A. Explore relationship between CSG and PBS dues

The amount of a station's CSG is an important variable in the calculation of PBS dues. In previous years, many stations were able to fund their PBS dues entirely with their CSG payment. More recently, as the federal appropriation that funds CSGs has been flat and the costs of producing and distributing programming have increased for PBS, several stations are finding that they are unable to pay their PBS dues entirely with their CSG. Because of this, some members of the station community that the CSG formula should be modified so that stations could again fully fund their PBS dues with their CSG payment.

To respond to these concerns, CPB staff and the panel examined the difference between CSG revenue and PBS expense for a variety of station cohorts. We found that most grantees still receive larger CSGs from CPB than they owe in PBS dues. However, there appeared to be a discrepancy in the portion of the CSG consumed by PBS dues in Multi-Provider Markets. Small, secondary stations in Multi-Provider Markets that participate in PBS's Program Differentiation Plan (PDP) tend to have more of their CSGs remaining after paying PBS dues. Large, primary stations in Multi-Provider Markets were the most likely to pay more in PBS dues than they received in their CSGs. After thoroughly reviewing the data, CPB management concludes that this issue is related to the PBS dues formula and is best addressed with PBS.

B. Study station and system efficiencies

At the panel's request, CPB provided recent research on potential station and system efficiencies to the panel for their review. This research, conducted by multiple firms between 2001 and 2005, highlighted opportunities in many areas, particularly broadcast operations. The research also described a variety of cultural barriers and issues that public broadcasters face when considering industry efficiencies including: (1) low emphasis on cost-cutting relative to service; (2) high value placed on group decision-making and consensus; and (3) an emphasis on station "uniqueness" rather than commonalities shared by stations. Data was also provided on the performance of stations in Multi-Provider Markets in comparison with those in sole service markets to see if lessons could be learned from those markets that would be particularly relevant in a digital, multi-casting environment.

Finally, information was presented on the short depreciation schedule for digital infrastructure. Today, only 10 percent of the current depreciation expense among all public television stations is funded, and, in a digital environment, this depreciation expense is unlikely to represent a paper loss. Instead, short depreciation schedules may accurately reflect rapid obsolescence and the need to place equipment on a much faster replacement schedule than stations are accustomed to in an analog world. Combined with other financial pressures, the demands of equipment replacement may drive stations to look for more efficient ways to operate and pressure formerly reluctant stations to develop value-creating collaborations.

CPB management agrees with the panel's assessment that the development of station and system efficiencies and meaningful collaboration among stations will become more important over the next few years. In an environment of flat federal funding, however, CPB management does not believe it is feasible to build incentives into the CSG program to encourage stations to adopt new business models because the overall shift in funding allocations would be too disruptive. Instead, CPB management agrees with the panel that, outside of the CSG program, CPB and other national organizations should continue to work with stations to develop and encourage adoption of new ways of doing business.

Recommendation: Relevant organizations, such as PBS and the Affinity Group Coalition, should continue to pursue issues around the PBS dues structure. CPB and other national organizations should continue to work with stations to develop and encourage the adoption of new efficient and collaborative ways of doing business.

III. Conclusions

Public television is facing one of the largest transformations in its history. As new video distribution platforms emerge, public television has a unique opportunity to re-think its business models from programming to fundraising, from new revenue streams to increased efficiencies and cost reductions. Federal funding in public broadcasting has helped fund this initial digital transition, and now stations must decide how to best use this investment to develop new services and encourage more meaningful collaboration.

At the same time that new opportunities exist, public television is also facing a financial crisis. Revenues from a variety of sources are falling. Federal support remains one of the most stable sources of income and stations have become increasingly reliant on these funds in recent years. In fact, federal dollars are a growing percentage of total system revenue. The increasing reliance on these funds, however, comes at the very same time that our appropriation is stagnant, representing a loss in real dollars. New business models need to be developed if we are to truly "grow the pie" and significantly increase our level of service.

Recognizing these challenges, CPB management recommends that we hold the bulk of CSG policy steady for the immediate future. CPB management understands that it is important to have a source of stable, dependable revenue in a time of great flux. At the same time, we are well aware that we cannot stand still for long. The broadcasting landscape is changing and CSG policy will need to adapt to those changes. Many of the policies outlined above reflect the transitional moment in which we worked and will need to be reviewed and no doubt revised once the 2009 digital conversion is complete.

Appendix A – Panel Members

The following individuals from the served on the 2006-2007 CSG Panel:

- Elizabeth Christopherson, NJN
- Thomas Crockett, PBS
- Trina Cutter, WNEO
- Jason Daisey, PBS
- Mark Erstling, APTS
- DeAnne Hamilton, WKAR
- John Hesse, HoustonPBS
- Skip Hinton, NETA
- John King, VPT
- Bill Kobin, MMG
- Ted Krichels, WPSU
- Lance Ozier, WGBH
- Mel Rogers, KOCE
- Wick Rowland, KBDI
- Dan Schmidt, WTTW
- Rob Shuman, MPT
- Larry Smith, KUED
- Allen Weatherly, AETN

CPB is grateful for the time, energy, and insights that these panelists contributed to the review process.

CPB staff also contributed to the panel process: Vinnie Curren, Fred DeMarco, Jessica Johnson, David Liroff, Loren Mayor, Marc McDonald, Andy Russell, Brian Sickora, Sean Simplicio and Duffy Winters.

Appendix B – Recent CSG History and Milestones

Reviews of the CSG program occur every few years. Most recently, reviews were conducted in 1996, 1998 and 2001. At each review, policy changes were made in the context of the federal funding situation and the state of the system's financial health in order to meet the financial needs of public television stations, cope with technological and other environmental changes, and maintain or improve incentives for stations to stimulate nonfederal financial support. Below is a summary of major CSG policy changes.

Summary of Recent CSG Milestones

Date	Context & Goal	Outcomes
1996	Prepare public television for potentially significant decreases in Federal support.	<ul style="list-style-type: none"> - Reduced based grant calculation from .12% to .11% of appropriation, which increased funds available for incentive grant. - Each Multi-Provider Market received one base grant, which was divided among the recipients in inverse relation to their NFFS. - Moved to one base grant per licensee, eliminating additional base grants for licensees that operated multiple transmitters. - Established funds to encourage industry productivity and efficiency (Overlap Fund, Transition Fund, Future Fund). - Base grant eliminated for grantees with NFFS larger than \$55.
1998	Review and evaluate impact of 1996 policy changes	<ul style="list-style-type: none"> - Extended funds designed to encourage productivity and efficiency. - Created Special Assistance Grants to provide additional CSG support to stations with comparatively low levels of NFFS. - Reaffirmed the modifications to base grant calculations recommended in the 1996 review and adopted by CPB. - Removed capital funds from NFFS calculations to prevent large one-time gifts from distorting CSG payments.
2001	Meet the special funding needs of certain station cohorts, continue to promote efficiency and productivity.	<ul style="list-style-type: none"> - Created Distance Service Grants to support licensees operating multiple transmitters serving distant communities. - Replaced Special Assistance Grants with the Local Service Grant program to support local activities. - Developed the Program Differentiation Incentive to encourage stations in Multi-Provider Markets to offer distinct program services. - Created Collaboration Fund to support the development and operation of shared infrastructure.
2003		<ul style="list-style-type: none"> - Ended the \$2.5 million Transition Fund and created a \$1 million Small Station Fund, drawn from the CSG pool, to assist small stations facing extreme hardship and to provide support for collaboration and professional assistance and development. - Base grant in a Multi-Provider Market divided equally among all grantees in market.
2004	Revise operations to comply with findings of GAO report	<ul style="list-style-type: none"> - Cease withdrawing funds from the CSG pool to support the Collaboration Fund, Small Station Fund and Future Fund.

Appendix C – Multi-Provider Markets and Differentiation Recipients

<u>Atlanta</u> Georgia Public Broadcasting WPBA*	<u>Chicago</u> WTTW WYCC* WYIN*	<u>Denver</u> KBDI* KRMA	<u>Lincoln</u> KUON NETV
<u>Los Angeles</u> KCET KLCS* KOCE* KVCR*	<u>Madison</u> WHA WPTV	<u>Miami</u> WLRN* WPBT	<u>New Orleans</u> WLAE* WYES
<u>New York City</u> WNET WNYE*	<u>Orlando</u> WBCC* WCEU* WMFE	<u>Philadelphia</u> WHYY WYBE*	<u>Salt Lake City</u> KBYU* KUED* KUEN
<u>San Francisco</u> KCSM* KQED KRCB*	<u>San Juan</u> WIPR WMTJ*	<u>Seattle/Tacoma</u> KBTC* KCTS	<u>Tampa</u> WEDU WUSF*
<u>Washington, DC</u> WETA WHUT*			

Bold stations are primary station in market

*Receive Program Differentiation Incentive

Appendix D – Glossary & Abbreviations

Base Grants – Flat grant given to all qualifying television grantees.

Distance Service Grant – A grant that is calculated as a percent of base grant for grantees with 3 or more transmitters and equivalent translators (10 translators equal one transmitter).

Incentive Funds Pool – Pool of funds that are used for grantee incentive grants.

Incentive Grants – Variable matching grants based on NFFS and given to all grantees.

Incentive Rate of Return – Formula for determining grantee’s incentive funds. Calculated by dividing Incentive Funds Pool by total system NFFS.

Local Service Grant – A \$3 million grant distributed in inverse-proportion of a grantee’s NFFS. Only grantees with NFFS less than \$2 million are eligible.

Multi-Provider Market – A multiple station market in the same state where: (1) the broadcast signal of one station reaches more than 50% of the population served by another station and (2) less than 20% of the population served by the station is unduplicated. Formerly called Overlap Markets.

Multi-Transmitter Stations – Grantees with 3 or more transmitters or equivalent translators.

Net CSG Grant – CSG minus PBS dues.

NFFS – Nonfederal financial support

Primary Station – A primary station is the grantee with the largest NFFS in a Multi-Provider Market.

Program Differentiation Incentive – An incentive to secondary stations in designated Multi-Provider Markets that substantially differentiate their programming from the market’s other stations.

Secondary Station – A secondary station is a grantee that does not have the largest NFFS in a Multi-Provider Market.

Small Stations – Grantees with under \$2 million in NFFS.

Sole Service Station – The station operates the only primary broadcast service (radio or television) within a 50-mile radius from the station’s transmitter. Licensees operating multiple services (Radio/Radio, Radio/TV) serving the same community may qualify as a single sole service grantee.

Translators do not qualify as sole service stations because of their secondary status. Secondary services also do not preclude a prospective station from qualifying for a sole service grant.