
Review of the interaction between BBC Studios and the BBC public service

Findings

[Review of the interaction between BBC Studios and the BBC public service](#) – Welsh overview

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1. Overview

This document sets out the findings of our review of the interaction between the BBC public service and its main commercial subsidiary, BBC Studios.

The UK broadcasting industry has changed significantly since Ofcom took over regulation of the BBC in 2017. Advances in technology have allowed new business models to emerge, leading to an era of unprecedented innovation and consumer choice. Audiences are benefiting from significant growth in high-quality content available on TV and online, and competition has intensified for the services of production and distribution companies.

The BBC's commercial activities have also changed substantially in recent years. Its production and distribution arms have merged into a new BBC Studios, and additional production activities have shifted from the public service part of the BBC into this new entity. BBC Studios produces and distributes content for consumers to watch in the UK and around the world. It owns and operates channels (e.g. UKTV) and outside the UK, in partnership with ITV, owns the subscription video-on-demand service BritBox. BBC Studios also sells programme formats internationally (such as Strictly Come Dancing) and consumer products such as DVDs and merchandise.

Ofcom's role in regard to the BBC's commercial activities is set out in the Charter and Framework Agreement. Our regulation aims to make sure the BBC's commercial activities do not gain an unfair advantage over competitors by virtue of their relationship with the BBC. This means that the public service, and by extension the BBC licence fee, cannot be used to fund or subsidise commercial activities. To ensure that this is the case, we have put trading and separation requirements in place through a set of requirements and guidance. The BBC must put in place appropriate, robust controls and procedures to make sure it follows the regulation, particularly as the market changes and BBC Studios continues to evolve.

In this review we have sought to better understand how the BBC has implemented the rules we have put in place. We have also assessed whether our regulation remains effective (based on the current legal framework set out in the Charter and Framework Agreement). We initiated this review before the pandemic, and it has been substantially delayed as a consequence. In the interim the market and the BBC have continued to change at pace. We have therefore taken the opportunity to align this review with our broader review of the regulation of the BBC, which will in turn inform both the Government's Mid-Term Review and any changes to the regulatory framework for competition regulation and commercial activities that we may propose later in the year.

What we have found – in brief

Our key finding is that there are two significant areas where we are not currently satisfied that the BBC has appropriate controls and procedures in place to ensure that it is operating in line with our regulation. The rules are there to ensure that the relationship between the BBC public service and BBC Studios does not confer an unfair advantage or distort competition. In both cases the BBC now needs to take action so that we and stakeholders can be confident it has measures in place to ensure compliance with our regulation.

Secondary content sales – For certain categories of content that BBC Studios distributes, where the BBC public service owns the intellectual property, co-production arrangements are in place. Under these arrangements BBC Studios is entitled to the entirety of the profit related to the distribution of the associated secondary content rights. This is a long-established practice and it does not appear to us that the BBC has fully reviewed and updated it in the light of our rules.

We have not seen evidence that the public service has undertaken objective tests to ensure that its co-production arrangements with BBC Studios are at arm's length and on commercial terms, and therefore it is not clear to us how the BBC is satisfying itself that it is achieving compliance.

Supply and pricing of goods and services – The public service sells a range of goods and services to its commercial subsidiaries and to the market (including BBC Studios). To better understand the way the BBC does this, we looked at a small sample of transactions and found some issues with the administrative processes in place.

In the other areas considered in our Review, we are broadly satisfied with the BBC's approach to the exchange of information, its commercial governance structure and its reporting arrangements that ensure that there is appropriate separation between the public service and BBC Studios, and its approach to charging BBC Studios for the use of the BBC brand.

Next steps

Given the concerns we have identified, we expect the BBC Board to take action to update its approach and to look more broadly at the issues raised and satisfy itself that its processes and arrangements are in accordance with our rules.

Later this year we plan to consult on potential changes to the competition regulation as part of our review of how Ofcom regulates the BBC. In this consultation we will take account of our findings in this review and any subsequent changes made by the BBC in determining whether amendments to the existing rules are required to address our concerns.

The overview section in this document is a simplified high-level summary only. The findings and our reasoning are set out in the full document.

2. Background

2.1 In this section we set out: the legal framework, our rules, the background of BBC Studios, the wider market context and a summary of our review.

Background to the legal framework governing the BBC's commercial activities

The Charter and Agreement

2.2 The Charter and the Agreement determine what the BBC can do and how it is organised, as well as setting out Ofcom's regulatory role and duties. The BBC as a corporation must not directly undertake any commercial activities; these must be provided through one or more commercial subsidiaries.¹

2.3 Under the Agreement, the Operating Framework² must include the requirements Ofcom considers appropriate to ensure that the commercial activities do not, as a result of their relationship with the UK public services, trading activities³ and non-service activities (the public service⁴), distort the market or gain an unfair competitive advantage.⁵ The Agreement provides that this may include requirements to ensure appropriate separation between the public service and the commercial subsidiaries, by requiring that the relationships between the public service and the commercial subsidiaries are at arm's length and on commercial terms.⁶

2.4 In order to ensure appropriate transparency in the relationship between the public service and the commercial subsidiaries, our requirements⁷ may include - (i) the provision by the BBC to Ofcom of financial reports; and (ii) the publication by the BBC of information to demonstrate that the relationship of the commercial activities with the public service meets the trading and separation rules without jeopardising the ability of the commercial subsidiaries to operate effectively in the market.⁸

¹ The Charter, article 7(d), and The Agreement, clause 23(4). Defined terms in this document shall have the same meaning as they have in The Charter, The Agreement and the rules.

² As required under the Charter, Ofcom has developed an Operating Framework for the BBC, covering regulation of the BBC's performance, compliance and content standards and impact on competition.

³ Trading activities are activities which are commercial in nature but are not to be treated as commercial activities.

Trading activities involve the provision of goods and services by the BBC to its commercial subsidiaries, third parties and the general public. Trading activities are set out in Clause 31(1) and 31(2) of the agreement.

⁴ References to the 'public service' in the rest of this document should be read as references to BBC's UK public services, trading activities and non-service activities.

⁵ The Agreement, clause 28(1).

⁶ The Agreement, clause 28(1)(a)(ii).

⁷ Defined in clause 28(1) of the Agreement as "requirements Ofcom consider appropriate to ensure that the commercial activities do not, as a result of their relationship with the UK public services, trading activities or non-service activities, distort the market or gain an unfair competitive advantage".

⁸ The Agreement, clause 28(1)(b).

- 2.5 The BBC, in exercising its functions in relation to the public service, must comply with the general duties in articles 9 to 17 of the Charter,⁹ including the requirement to have particular regard to the effects of its activities on competition in the United Kingdom.¹⁰
- 2.6 In complying with the above, the BBC must (a) seek to avoid adverse impacts on competition which are not necessary for the effective fulfilment of the Mission and the promotion of the Public Purposes; and (b) have regard to promoting positive impacts on the wider market. The BBC must also observe high standards of openness and seek to maximise transparency and accountability.¹¹
- 2.7 The Charter and Agreement place a number of obligations on the BBC regarding commercial activities carried out by its commercial subsidiaries. It must ensure that these commercial activities fit with its Mission and Public Purposes, are commercially efficient, do not jeopardise the BBC brand, and do not distort the market or gain an unfair competitive advantage as a result of their relationship with the public service. Together, these obligations are known as the commercial criteria.
- 2.8 The BBC Board oversees the BBC's commercial activities.¹² As part of its duty to ensure that the BBC fulfils the Mission and promotes the Public Purposes, the BBC Board sets a strategy for the BBC's commercial activities. It must also consider proposals for material changes to these activities and assess them against the commercial criteria. These duties across the wider BBC Group require the BBC Board to have a degree of oversight over the governance of the commercial subsidiaries.
- 2.9 The BBC Board must ensure compliance by the BBC with its obligations under the Charter, the Agreement, the Operating Framework and general law.¹³ The BBC Board is also responsible for the overall oversight of the BBC's commercial activities. The Fair Trading Committee (a sub-committee of the BBC Board) is responsible for overseeing the BBC's compliance with its regulatory obligations for trading and separation between the public service and the commercial subsidiaries.

Legal basis for our review

- 2.10 We have conducted this review under Clause 28 of the Agreement and article 51(3) of the Charter.¹⁴ Ofcom has powers to investigate areas of concern, including carrying out and publishing additional reviews addressing any specific issues relating to the activities of the BBC that are subject to regulation.

⁹ The Charter, article 8.

¹⁰ The Charter, article 11.

¹¹ The Charter, article 12(1).

¹² The Charter, article 20.

¹³ The Charter, article 20(8).

¹⁴ The Charter, article 51 (3).

Our rules

2.11 In accordance with the Agreement,¹⁵ we put in place requirements and guidance in 2017 (the rules) which have been updated since.¹⁶ The rules cover four main areas, summarised in Figure 2.1 below.

Figure 2.1: Broad areas covered by the rules

Operational separation	Supply and pricing of goods and services	Commercial rate of return
Ensure that the governance of the commercial subsidiaries is distinct and separate from the public service, and restrict the commercial subsidiaries' access to information regarding the public service's strategy, priorities and activities, that is not available to third parties.	Regulate the terms and conditions on which the public service and commercial subsidiaries sell goods and services to each other. Goods and services sold by the public service to third parties are also covered.	The BBC is required to earn a commercial rate of return for each commercial subsidiary and line of business over an appropriate period of time.
Monitoring, reporting and transparency requirements		

BBC Studios

2.12 BBC Studios is the main commercial subsidiary and undertakes activities such as content production, distribution and branded services.¹⁷ Despite significant delays to productions as a result of global lockdowns, BBC Studios delivered turnover of £1.2bn in 2020/21 with profits¹⁸ of £151m. BBC Studios has two lines of business:

- a) **Production and distribution:** BBC Studios produces and distributes programmes and licenses these to broadcasters and platform owners globally. Titles produced for the BBC include shows such as *Top Gear*, *DIY SOS*, *Silent Witness* and *Seven Worlds, One Planet*. In 2020/21 BBC Studios secured 74 new commissions for the BBC and 16 new commissions for third parties in the UK.¹⁹ New partnerships were secured in 2020/21

¹⁵ The Agreement, clause 28(1).

¹⁶ [The BBC's commercial and trading activities: requirements and guidance, Ofcom, 15 July 2021](#). This is the unofficial consolidated version of the trading and separation requirements and guidance. The rules were updated in February 2019 and further minor changes were made in 2021 following our assessment of BBC Studios' changes to its lines of business. For the avoidance of doubt, in the case of any difference between texts, the text set out in the 11 February 2019 publication and any subsequent documents published on Ofcom's website shall take precedence.

¹⁷ In addition to BBC Studios the other two commercial subsidiaries are BBC Studioworks (studios and post-facilities provider) and BBC Global News Limited which operates the BBC's commercially funded international news services

¹⁸ Profits as measured by EBITDA or earnings before interest, taxes, depreciation and amortization.

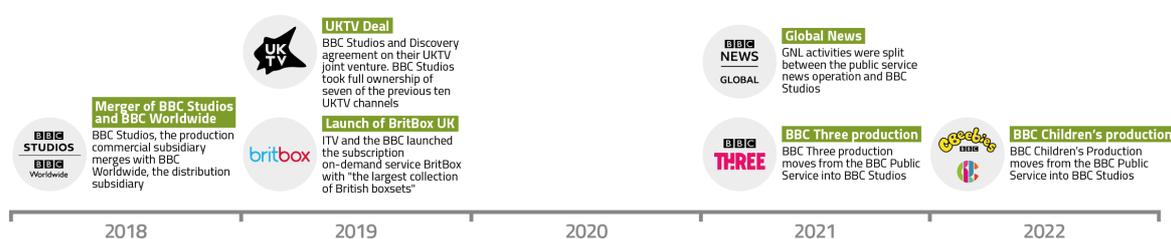
¹⁹ [BBC Annual Report](#), page 67.

including a deal with the Chinese entertainment platform Bilibili.²⁰ Production and distribution remained the largest line of business within BBC Studios, with a turnover of £929m and EBITDA of £66m in 2020/21.²¹

- b) **Branded services:** BBC Studios owns/has partnerships that include a number of channels and digital consumer services in the UK, such as UKTV, and outside the UK, such as joint venture and associate operations in BritBox US and Canada, BBC America and digital branded services including BBC Player in Asia. This line of business had a turnover of £383m and EBITDA of £85m in 2020/21.²²

2.13 Since BBC Studios was established in 2017, as set out in Figure 2.2, there have been a number of changes²³ to its business and its structure.

Figure 2.2: Timeline of changes to BBC Studios: 2018-22²⁴



Market context

- 2.14 In October 2020, alongside our Call for Evidence, we published a [report by Mediatique](#) and invited views on whether the report represented a reasonable basis for us to consider the market context for this review.
- 2.15 BBC Studios operates in global markets that are increasingly characterised by digital technology. Broadcaster video-on-demand (VoD) and subscription video-on-demand (SVoD) services, such as Netflix and Amazon Prime, are at the forefront of technological changes in the sector. There is increased choice for consumers and while people still view content from broadcasters more than they do SVoDs, the former is declining while the latter is increasing.²⁵
- 2.16 The BBC has [announced plans](#) to expand the BritBox International JV in up to 25 markets across the world. In February 2021, the BBC also launched a new SVoD channel called BBC Select in America and Canada, and has plans for exploring new digital revenue streams in the future.

²⁰ [BBC Annual Report](#), page 67.

²¹ [BBC Annual Report](#), page 68.

²² [BBC Annual Report](#), page 68.

²³ Changes we have assessed within the materiality framework (we considered and have determined that the developments were not material under this framework).

²⁴ In 2022 ITV also acquired the BBC's stake in BritBox UK.

²⁵ Ofcom estimates modelled from BARB, Comscore and TouchPoints data. Viewing of content from broadcasters averages over three hours a day per person, while viewing to SVoDs averages just over an hour a day per person.

- 2.17 In relation to the production sector, as noted in the Mediatique report, public service broadcasters (PSBs) remain the largest commissioners of content in the UK but their spend is declining.²⁶ In PACT's most recent census, commissioning spend from PSBs was reported to be at its lowest level in a decade, at £1.1bn, due to the impact of the pandemic.²⁷ The declining spend by PSBs has in recent years largely been offset by increased commissions from SVoDs and global players seeking more original content for their platforms. The increased competition for content that appeals to these platforms' global audiences has led to production price inflation in key genres such as drama in recent years.²⁸
- 2.18 Distribution has also seen changes. Mediatique noted that the increasingly global nature of demand for TV content from international SVoD players has led to changes in rights windows. 'Rights windows' refers to the length of time that a particular company has the rights to a piece of intellectual property. SVoDs are increasingly seeking exclusive global rights, thereby placing pressures on windowing conventions in many domestic markets, including the UK. There are trends towards content becoming exclusive upfront, and longer availability windows.²⁹
- 2.19 The pandemic has had immediate and potentially enduring effects on the markets in which BBC Studios operates. As Mediatique noted³³, the short-term effects have been particularly acute in the UK and in international production, in content sales and in branded services. The effects were anticipated to accelerate existing trends.

Details of our review

- 2.20 The purpose of the Review was to get a better understanding of how the BBC has implemented our rules and how the BBC Board is satisfying itself that it is compliant with these rules. This is different from an enforcement investigation, whose purpose is to investigate specific concerns we might have about compliance. As part of this Review, we have gathered and considered information relating to the general implementation of our rules across the areas we are looking at. We have also reviewed information provided by the BBC, stakeholder responses to our Call for Evidence and publicly available information. We have not reached any decisions as to whether the BBC has or has not complied with our rules.

Call for Evidence

- 2.21 In our October 2020 Call for Evidence³⁰ we acknowledged the main stakeholder concerns that we were aware of, and set out the details of the proposed scope of our Review, inviting further views from stakeholders on the key areas of our rules.³¹ We also invited

²⁶ [Mediatique report](#), page 2.

²⁷ [PACT Financial Census 2021](#), page 15.

²⁸ [Mediatique report](#), page 3.

²⁹ [Mediatique report](#), page 5.

³⁰ Ofcom, [Call for evidence: Review of the interaction between BBC Studios and the BBC public service](#), 9 October 2020.

³¹ Our scope of work covered the monitoring, reporting and transparency requirements under the three main areas of our rules.

views on any other areas of stakeholders' concerns which might indicate that BBC Studios was gaining a potential unfair advantage or that there was a market distortion as a result of its relationship with the public service. Our proposed scope included the following areas:

- a) **Operational separation:** We set out our intention to assess how the BBC has implemented our rules and to consider whether there are appropriate safeguards in place. This included assessing the BBC's reporting and the processes in place on how information is being shared between the public service and BBC Studios.
- b) **Supply and pricing of goods and services:** A number of goods and services are supplied between BBC Studios and the public service (and vice versa). To establish how goods and services are provided, we set out our plan to assess a sample of pricing methodologies to check for consistency with our rules and the associated charges.
- c) **Rate of return:** As part of our Review, we said that we would provide more clarity in relation to rate of return. In particular we said that we would provide guidance on what we consider represents a range for a commercial rate of return and the appropriate period over which BBC Studios (and its lines of business) should earn this rate.

Responses to our Call for Evidence

2.22 We received a broad range of responses to our Call for Evidence; from the BBC, Directors UK, PACT, RNIB,³² Sky, TAC³³ and three individuals.³⁴ These responses covered a range of issues in relation to our rules which we discuss in detail in sections 3 and 4.³⁵ Respondents also raised some issues which were outside of our proposed scope of work; we discuss these below and explain why we have not taken them forward as part of this Review.

Commissioning

2.23 Some stakeholders raised concerns about commissioning of programmes by the public service.³⁶ PACT said that although information published by the BBC on commissioning (in its TV Commissioning Supply Report) was a step in the right direction, it would like more information. TAC also raised concerns about the lack of clarity many production companies had on how the BBC ensures they are treated fairly in the commissioning process, and suggested that this had led to a lack of trust in the BBC among producers.

2.24 Stakeholders also raised concerns about the public service prioritising BBC Studios: TAC members were concerned that the public service's knowledge and familiarity with BBC Studios meant that it might be more inclined to go 'in house' when commissioning programmes and choose BBC Studios over independent production companies. On the other hand, the BBC raised concerns about Ofcom potentially opening up this area, given

³² Royal National Institute of Blind People.

³³ Teledwyr Annibynnol Cymru / Welsh Independent Producers.

³⁴ We published the non-confidential responses on [our website](#).

³⁵ Some respondents, PACT, Directors UK raised some minor points regarding the report by Mediatique discussed above

³⁶ Commissioning by the public service was not in the proposed scope of our review given our focus is on the interaction between the public service and BBC Studios. Separate rules are in place to ensure commissioning is fair, reasonable, non-discriminatory and transparent and these rules were reviewed in February 2019. See Ofcom, [Statement: Commissioning for the BBC public services](#), February 2019.

our recent review of the commissioning rules and the fact there had not been any issues raised in Ofcom's previous Annual Report on the BBC.

- 2.25 Some of the issues which stakeholders raised with us were considered as part of our review of the commissioning rules in 2019. We also monitor the BBC's performance on commissioning and engage with producers regularly to help identify any issues. We published the output from our ongoing monitoring work and engagement with producers on commissioning in our last Annual Report on the BBC (and are carrying out similar engagement this year).³⁷ As such, we decided not to address commissioning further in this Review.

Other responses outside our proposed scope

- 2.26 Stakeholders raised some other issues which did not fall in the scope of our review. Directors UK raised some points about the public service's supply of content to iPlayer. RNIB highlighted concerns about the accessibility of BBC content on BritBox and third-party video-on-demand services, which we will consider in our broader work on on-demand accessibility – see our [further recommendations](#) to Government on making the accessibility of on-demand services a legal requirement.
- 2.27 Sky raised concerns that the BBC had a strategy which favoured BritBox, and some concerns regarding the cross-promotion of BritBox. In our 2019 decision on BritBox we said we expected the BBC to inform us of its plans before it proceeded with any promotion of BritBox, and that we would separately consider whether safeguards were needed. Since then, the BBC has carried out two promotions of programmes on BritBox, and in both cases provided us with information about their impact. We therefore decided it was not appropriate to consider this issue in our Review. [X]

BBC Studios' changes to lines of business

- 2.28 As part of our review, we assessed, and concluded in April 2021³⁸, that BBC Studios' changes to its lines of business (from five to two, notably combining the production and distribution activities into a single line of business), were appropriate. We also set out a new process for the notification of future changes to lines of business by the BBC.
- 2.29 As part of our statement, we recognised that the relationship between the combined production and distribution lines of business and the public service was complex. We highlighted our intention to undertake further work to understand how this relationship works, and how it might impact BBC Studios' rate of return, as part of our review. We discuss this further in Section 4.

³⁷ Ofcom, [Annual Report on the BBC 2020/21](#), 25 November 2021.

³⁸ Ofcom, [BBC Studios' lines of business: Assessment of BBC Studios' changes to its lines of business](#), 30 April 2021.

How Ofcom regulates the BBC

2.30 Separately from this Review, today we have also published our report on [how Ofcom regulates the BBC](#). As part of that, we plan to issue a consultation in the autumn that may include proposals for changes to our rules.

Structure of this document

2.31 The rest of this document is structured as follows:

- a) Section 3 sets out analysis and findings on operational separation; and
- b) Section 4 sets out our analysis and findings on the supply and pricing of goods and services.

3. Operational separation

Summary of findings

- We have assessed how the BBC has implemented our rules relating to the exchange of information between the public service and BBC Studios. Overall, on the basis of the information we have obtained, we have found that the BBC has appropriate processes and measures in place.
- There has been a marked improvement in the transparency of the arrangements in place since we introduced a requirement for the BBC to publish annual statements on operational separation in 2019. We have identified some minor areas where further information is appropriate, in line with the BBC's duties, to give greater comfort to us and other stakeholders on an ongoing basis. We therefore expect the BBC to include additional details in Annual Statement on operational separation (Annual Statement) as soon as practicable, and no later than in the annual statement 2022/23.

3.1 This section has two sub-sections: exchange of information and governance. For each topic, we provide a brief overview of our rules before discussing a summary of stakeholder views, our approach, the BBC's arrangements, and our findings.

Exchange of information

Our rules

3.2 Our rules address the risk that public service information, which is not available to third parties, is shared with commercial subsidiaries at governance and/or operational levels where it has the potential to give rise to an unfair competitive advantage or distort the market. The BBC must have in place appropriate measures, controls and processes to ensure that its commercial subsidiaries and joint ventures do not have access to information about the public service's strategy, priorities and activities that is not available to third parties, other than:

- a) information that is necessary to ensure that the commercial activities fit with the BBC's Mission and Public Purposes;
- b) information that is necessary for the fulfilment of any contract; or
- c) information that if shared, does not carry any risk that commercial subsidiaries or joint ventures could, as a result of having access to that information, distort the market or gain an unfair competitive advantage.³⁹

3.3 When information is shared under these specific circumstances, the BBC must have in place appropriate measures, controls and processes to ensure that it is only used for the

³⁹ Requirement A.2.

specific purpose for which it was obtained.⁴⁰ Commissioning information presents the greatest information-sharing risk. If BBC Studios were to obtain information regarding the public service's commissioning strategies that was not available to third parties, it might be able, for example, to tailor its pitches to align with the public service's strategy and gain an unfair competitive advantage over third parties. The BBC must have processes in place to manage information-sharing risks⁴¹ and is required to report on these alongside its Annual Statement.⁴²

Summary of stakeholder views

- 3.4 In response to our Call for Evidence, two stakeholders made general comments on the exchange of information. Sky was concerned about the lack of meaningful separation between the public service and BBC Studios. It considered that the operational overlap between the public service and BBC Studios made it impossible for the BBC to comply with Ofcom's rules to limit information sharing.⁴³ Sky also highlighted the overlap in governance responsibilities and personnel between the public service and the commercial subsidiaries, including BBC Studios.
- 3.5 Directors UK noted the importance of ensuring that BBC Studios does not have access to public service information on commissioning and distribution activities, to ensure that BBC Studios competes independently in the market.⁴⁴
- 3.6 Relevant issues were also raised in our engagement with stakeholders. One stakeholder⁴⁵ considered that it was important for the BBC to have policies in place to ensure that staff moving from the public service to BBC Studios do not bring up-to-date knowledge with them that could give BBC Studios an unfair competitive advantage (e.g. a requirement for gardening leave). Producers have told us that as more commissioning is conducted online they have better access to commissioners, regardless of where they are based.⁴⁶

Our approach

- 3.7 We looked at how the BBC has implemented our rules. We have considered the Annual Statements⁴⁷ and further information gathered from the BBC as well as stakeholder views. In this section we discuss:
- a) risk identification and the processes in place to manage risk;
 - b) the training of employees;
 - c) IT systems;

⁴⁰ Requirement A.3.

⁴¹ Requirements A.1 – A.5.

⁴² Requirement D.2.

⁴³ Sky response to Call for Evidence, page 4.

⁴⁴ Directors UK response to Call for Evidence, page 3.

⁴⁵ [redacted]

⁴⁶ [Ofcom Annual Report on the BBC 2020-21](#), page 59.

⁴⁷ This includes [Annual Statement](#) 2018/2019, [Annual Statement](#) 2019/2020 and [Annual Statement](#) 2020/2021.

- d) staff movement; and
- e) arrangements for co-located employees.

Risk identification and the processes in place to manage risks

Summary of BBC arrangements

- 3.8 The BBC published an information-sharing protocol⁴⁸ in 2019 which sets out the output from the BBC's risk assessment process. The protocol sets out principles to guide information sharing and includes details of the types of information which can and cannot be shared between the public service and the commercial subsidiaries. For example, information that can be shared is anything in the public domain, communications with regulatory bodies, and HR reports relevant to BBC Studios personnel. Information that cannot be shared includes things like commercial agreements with competitors and Commissioners' appraisals of specific bids. The protocol also provides guidance on how colleagues should determine what information can and cannot be shared.
- 3.9 The BBC Policy and Competition and Regulatory legal teams are asked for ad-hoc advice on what information can be shared, and this is used to identify new issues and risks.⁴⁹ Ad-hoc advice given has included topics such as information sharing in relation to the recent move of children's production activity from the public service into BBC Studios, and information sharing with BBC Studios for a meeting with another broadcaster.⁵⁰ The BBC said the risk environment is well understood within the organisation and that this, along with the ongoing provision of ad-hoc advice, negates the need for any formal ongoing review of the risks that underpin the information-sharing protocol.⁵¹

Our findings

- 3.10 It is important that the BBC identifies and manages information-sharing risks on an ongoing basis. Risks need to be identified and assessed, and to have clear ownership and effective mitigation measures as well as robust monitoring and reporting. The [Orange Book](#) published by HM Government sets out principles and concepts for the management of risk.
- 3.11 While we acknowledge that the BBC considers that new risks are effectively captured through the provision of ad-hoc advice by the BBC Competition and Regulatory Legal and Policy Teams, we do not agree that this means there is no need for formal assessments of the risks on an ongoing basis.
- 3.12 We expect the BBC to demonstrate to us and other stakeholders that it is actively managing risks on an ongoing basis and that the information-sharing protocol and its

⁴⁸ [Information Sharing Protocol](#)

⁴⁹ BBC response to question 2 of the Information request dated 9 March 2021 reference: 01128003. In its fair trading training programs, the BBC advises colleagues to seek advice from these teams when considering sharing any information that is not business as usual and include them at the beginning of projects so that they can feed into decisions throughout. The BBC provided us with access to its training courses which Ofcom accessed on 7 June 2021.

⁵⁰ BBC response to question 1 of the Information request dated 9 March 2021 reference: 01128003.

⁵¹ BBC response to question 2 of the Information request dated 9 March 2021 reference: 01128003.

underpinning risk assessment are reviewed at least annually. The outcome of this review should be included in the Annual Statement.

Training of employees

Summary of BBC arrangements

- 3.13 The BBC provides training to its employees in order to ensure they understand their obligations and the rules in place. There are different levels of training available, including Fair Trading Awareness training, which includes a broad overview of operational separation issues (Awareness Training). This training is mandatory for anyone making day-to-day decisions regarding commercial or trading activities, deals with third parties, or assessing the BBC's market impact. There is also a more detailed Fair Trading Advanced Training with a module dedicated to operational separation (Advanced Training), which is targeted at senior roles that typically handle more sensitive information, such as executive producers, commissioning editors and finance business partners.⁵² Tailored training is also run by the BBC Policy and Competition and Regulatory Teams when requested.⁵³ Deloitte reviews the content of the Awareness and Advanced Training courses as part of its annual Fair Trading Audits, and in its 2019/2020 report considered the training courses to be effective.⁵⁴
- 3.14 In the BBC's 2020/21 Annual Report, it set out completion rates for the Awareness Training and Advanced Training, which were 92.3% and 98.2% respectively.⁵⁵ This was a significant increase on 2019/2020, when the completion rates were 64% and 58% respectively.⁵⁶ The BBC attributed the lower completion rates in 2019/20 to the introduction of a new system for identifying training needs which almost doubled the training populations for both courses. In 2018/2019, the completion rates were 92% for the Awareness Training and 86% for the Advanced Training.⁵⁷

Our findings

- 3.15 Employees need to be appropriately trained and understand their responsibilities in managing the exchange of information. As part of our assessment, we accessed the Awareness and Advanced Training courses. The materials provide information on why there are rules in place for the exchange of information, and what staff must do to ensure compliance with the BBC's obligations. The Advanced Training provides more detail on these areas. The training material provided comprehensively covered the relevant risks.
- 3.16 The completion rates of the Awareness Training and Advanced Training courses in 2018/19 to 2020/21 have generally been high. We note the lower completion rate in 2019/20

⁵² BBC response to question 2 of the information request dated 19 November 2021 reference: 01378552.

⁵³ [Information Sharing Protocol](#).

⁵⁴ BBC response to question 2 of the information request dated 19 November 2021 reference: 01378552.

⁵⁵ [BBC Annual Report 2020/2021](#), page 122.

⁵⁶ BBC response to question 9 of the information request dated 9 March 2021 reference: 01128003.

⁵⁷ BBC response to question 9 of the information request dated 9 March 2021 reference: 01128003.

appears to be a one-off, associated with the introduction of a new process part-way through the year.

IT systems

Summary of BBC arrangements

- 3.17 The BBC manages the IT systems that control the information flow between the public service and BBC Studios in a number of ways:
- a) technical separation, where BBC Studios only has access to its own information (e.g. SAP, Audience Portal);
 - b) access policies, where technical separation is not possible e.g. Archives; and
 - c) non-disclosure agreements (NDAs), are used in rare cases where technical separation is not possible and a very limited number of BBC Studios' staff require access to potentially sensitive information in order to do their jobs.
- 3.18 All systems also require each user to agree to Terms of Use (or similar) which include a requirement to use the system only in order to do their job, and prohibits any sharing of information accessed.
- 3.19 We asked the BBC to provide a list of the IT systems used by both the public service and BBC Studios as well as the method(s) of information management used. The BBC explained that there were six programs in which the above techniques were employed to prevent BBC Studios employees accessing inappropriate information.⁵⁸ These cover a range of systems including commissioning and scheduling of TV and some radio programmes, business reporting, submission of programme ideas and logging production quotas. Two of these systems relate to production reporting, specifically⁵⁹:
- a) PTK Compliance allows for logging of programme compliance details before broadcast/publication. BBC Studios Distribution and Production staff have access to manage paperwork, and access for the production team mirrors the in-house production access. Access is limited to the submission and approval of paperwork only. The BBC explained that given the volume of production BBC Studios makes for the public service, and the fact that BBC Studios is fully aware of the BBC's editorial requirements (given the editorial guidelines apply also to BBC Studios), BBC Studios self-comply to avoid duplication⁶⁰.
 - b) Silvermouse is a production reporting tool used to submit post-production paperwork. Access is limited to BBC Studios to submission and approval of paperwork – BBC Studios Production self-manage accounts and BBC Studios Distribution access is supported by an NDA. The BBC explained again that given the volume of BBC Studios'

⁵⁸ BBC response to question 4 of the Information request dated 9 March 2021 reference: 01128003.

⁵⁹ BBC response to question 4 of the Information request dated 9 March 2021 reference: 01128003.

⁶⁰ BBC response to question 2 of the Information request dated 19 November 2021 reference: 01378552.

productions for the BBC, allowing BBC Studios direct access eliminates additional and unnecessary effort for BBC staff to input data.⁶¹

Our findings

- 3.20 IT systems are responsible for the transfer of huge amounts of information, and it is essential that information-sharing risks are managed effectively. During the pandemic a significant amount of work was done remotely, making it more important than ever that appropriate IT system controls are in place.
- 3.21 Broadly, we have found that the BBC has appropriate IT management systems in place. After analysing IT systems to which both the public service and BBC Studios have access, we found that for the majority of programs, access is limited and is managed effectively to prevent inappropriate information flows.
- 3.22 From the information provided by the BBC regarding systems where BBC Studios has greater access than independent producers, on the face of it, it does not appear that there are any competition issues associated with this access. However, we recognise that stakeholders might not be aware of the differing access for BBC Studios to these systems.
- 3.23 We therefore consider it is important in the interest of transparency for the BBC to set out details of IT programmes where there is differential access for BBC Studios compared to third-party producers, and the justification for this, as part of its Annual Statements.

Staff movement

- 3.24 As discussed above, some stakeholders raised some concerns about staff moving between the public service and commercial subsidiaries, which led us to consider this issue.

Summary of BBC arrangements

- 3.25 Staff movements between the public service and BBC Studios are relatively infrequent; for example, 44 moves took place in 2020⁶² (BBC Studios had a headcount of 2753).⁶³ The BBC has a policy in place to manage temporary transfers of staff from the public service to BBC Studios to ensure that no inappropriate information is shared.⁶⁴ Temporary staff moves are assessed on a case-by-case basis. Any move that would give staff access to information that could give BBC Studios a competitive advantage is not permitted.⁶⁵ In the most sensitive areas of commissioning and production, temporary staff moves are not permitted.⁶⁶
- 3.26 We understand that the BBC does not have a policy in place to manage permanent staff moves between the public service and BBC Studios. The BBC has told us it does not

⁶¹ BBC response to question 4 of the information request dated 9 March 2021 reference: 01128003.

⁶² BBC response to question 7 of the information request dated 9 March 2021 reference: 01128003.

⁶³ [BBC Annual Report 2020/2021](#), page 53.

⁶⁴ BBC response to question 4 of the information request dated 19 November 2021 reference: 01378552.

⁶⁵ BBC response to question 4 of the information request dated 19 November 2021 reference: 01378552.

⁶⁶ BBC response to question 7 of the information request dated 9 March 2021 reference: 01128003.

consider these to be necessary, as such measures are usually designed to prevent commercial harm through disclosure of information to a competitor, which the BBC believes does not reflect the relationship between the public service and BBC Studios.⁶⁷ The BBC argued that since these moves are permanent, staff could not bring back information that is sensitive.⁶⁸ When permanent staff moves do take place, details of the relevant staff members are updated in the Joiners Movers Leavers Record.⁶⁹ From there, IT accounts are created for the new role, and the previous IT access rights are revoked at the start of the new role. This prevents staff from continually accessing programmes and accounts from a previous role in the public service in their new role in BBC Studios.

Our findings

- 3.27 As BBC Studios continues to evolve and grow, there may be an increased risk that staff from the public service moving to roles in BBC Studios may be bringing knowledge with them that could distort the market and give BBC Studios an unfair competitive advantage. We expect any such risk to be effectively managed.
- 3.28 It is unclear why the BBC has implemented a management policy for temporary staff moves but not for when staff move permanently to the commercial activities. While there are processes in place to ensure that IT access rights are revoked when staff move, they could bring information to their new role that could give BBC Studios an unfair competitive advantage.
- 3.29 We therefore consider it is important that the BBC has adequate processes in place to manage permanent staff moves as well as temporary ones. We expect the BBC to articulate developments taken in this area and to include this information in its Annual Statements.

Arrangements for co-located employees

Summary of BBC arrangements

- 3.30 The BBC has measures in place where BBC Studios staff are co-located with public service commissioning staff to prevent the exchange of information.⁷⁰ This includes measures such as:
- a) ensuring that Commissioners and BBC Studios staff work in different parts of the building;
 - b) ensuring that a regular assessment of access to Commissioners is carried out to ensure parity between BBC Studios and independent production companies; and

⁶⁷ BBC response to question 4 of the information request dated 19 November 2021 reference: 01378552.

⁶⁸ BBC response to question 4 of the information request dated 19 November 2021 reference: 01378552.

⁶⁹ BBC response to question 7 of the information request dated 9 March 2021 reference: 01128003.

⁷⁰ [Annual Statement 2020/2021](#), pages 7-9.

- c) re-locating a BBC Studios team bidding on a production during the tender process if the bidding team is co-located with the relevant Commissioner.

3.31 By way of example, in the BBC's main London office, Broadcasting House, Commissioners work on a separate floor to BBC Studios staff and all communication about independent production confined to controlled areas. Similarly, in a location in Salford, Commissioners are located on a separate floor to production staff, with regular assessments to ensure parity of access between BBC Studios and independent producers.⁷¹ The BBC has highlighted to us that this issue is now less of a concern as remote working is commonplace since the pandemic.⁷²

Our findings

3.32 We have considered the arrangements the BBC has in place and note that online working has made commissioning briefings more accessible.⁷³ As work practices develop, in response to the pandemic, or for other reasons, the BBC should continue to provide updates in its Annual Statements.

Governance

Our rules and approach

- 3.33 Effective and independent governance arrangements for the commercial subsidiaries are an important component of ensuring that the commercial activities are not undertaken directly by the public service, as required by the Charter and Agreement, and that the relationship between the public service and the commercial subsidiaries does not distort the market. We have examined the governance arrangements in place using the Annual Statements, information from the BBC, and stakeholder views.
- 3.34 Our rules require that the commercial subsidiaries' governance bodies must have distinct and separate membership from the BBC Board and its executive committees. These boards and executive committees must consist of an appropriate number of directors who are not members of the BBC Board and/or its executive committee.⁷⁴ Our rules also require transparency of the BBC's governance, including the publication of information relating to governance arrangements. We require the BBC to have robust measures, controls and processes in place to prevent any conflict of interest that might arise as a result of a dual role, and to report annually to us on such conflicts.⁷⁵

⁷¹ [Annual Statement 2020/2021](#), pages 7-9.

⁷² [Annual Statement 2020/2021](#), page 9.

⁷³ [Ofcom Annual Report on the BBC](#), pages 59-60.

⁷⁴ Requirement A.4. When assessing these rules, we take into account factors including the balance of non-executive to executive directors, whether the chair is sufficiently independent from the public service, the extent of overlap in membership between the boards or executive committees of the relevant commercial subsidiary and the BBC Board and public service executive committees and the degree of influence that the public service has on governance and decision making within the relevant commercial subsidiary. See Guidance A.16.

⁷⁵ Requirement A.5, D.3.

Summary of BBC arrangements

- 3.35 The BBC Board is responsible for ensuring that the BBC delivers on its Mission and Public Purposes and ensuring that the commercial activities fit with the Mission and Public Purposes, are commercially efficient, do not damage the BBC brand or gain an unfair competitive advantage as a result of the relationship with the public service. The BBC Board is responsible (among other things) for setting strategy and governance arrangements consistent with those aims and assessing their effectiveness.⁷⁶ In setting the governance arrangements for the commercial activities, it is for the BBC Board to decide how to structure the boards and executive committees in line with its obligations (including our rules). There is also:
- a) the Fair Trading Committee (FTC) which is a BBC Board sub-committee and is responsible for overseeing the BBC's compliance with our rules;⁷⁷
 - b) the BBC Commercial Board⁷⁸ which is the main decision-making body for the BBC's commercial activities and is responsible for the governance, assurance and oversight of the BBC commercial subsidiaries. It is responsible for implementing the commercial strategy agreed by the BBC Board. It also makes decisions relating to the commercial subsidiaries, as appropriate within the delegated framework of approvals. The Commercial Board consists of ten members and comprises a majority of six non-executive members alongside four executive members⁷⁹;
 - c) the BBC Studios Board has a narrow role which is limited to statutory functions;⁸⁰ and
 - d) the BBC Studios Executive Committee is the executive approval body of BBC Studios Group.⁸¹
- 3.36 The process of identifying whether a decision should be escalated is undertaken in line with the financial delegation framework.⁸² The BBC has explained that investment and revenue deals in excess of £20m have to be escalated from the BBC Studios Executive Committee to the BBC Commercial Board or above. Specific rules apply for deals with an equity element, or those that could be considered contentious or novel. In relation to budget setting, the process for BBC Studios aligns with the wider BBC process.⁸³

⁷⁶ The Charter, article 20 (3) (j).

⁷⁷ [Fair trading committee - About the BBC](#) [accessed 21 April 2022].

⁷⁸ The BBC Commercial Board was announced on 30 March 2022 and was formerly the BBC Commercial Holdings Board.

⁷⁹ [Commercial Board - About the BBC](#) [accessed 21 April 2022].

⁸⁰ [Companies House, BBC Studios](#) [accessed 17 November 2021].

⁸¹ BBC Studios, [Executive Committee](#) [accessed 21 April 2022].

⁸² For a public example, please see the BBC Studios Executive Committee Terms of Reference which contains financial delegation limits See BBC: [BBC Studios Executive Committee Terms of Reference](#). [accessed 21 April 2022].

⁸³ BBC e-mail on 8 June 2022.

Summary of stakeholder views

- 3.37 Several stakeholders commented on the governance arrangements⁸⁴ the BBC has in place. Directors UK noted the overlap in governance responsibilities and personnel on both the BBC Board and the then Commercial Holdings Board.⁸⁵ It recognised the importance of there being appropriate and effective safeguards in place to prevent knowledge of the operational strategy of the public service being transferred to the commercial subsidiaries as a result of board members involvement in the operational running or governance of both entities.⁸⁶ Directors UK also recognised that if the BBC's governance processes are effective, the BBC can operate in the market fairly without being overly questioned due to concerns over a lack of separation and transparency.⁸⁷
- 3.38 Sky raised concerns about the overlap in governance responsibilities and personnel between the public service and the commercial subsidiaries, including BBC Studios. It argued that there was a *“lack of separation between BBC Studios and the public service, combined with the lack of transparency around how these two entities interact. The BBC has been able to game the system and enter into intra-group arrangements which risk distorting the market in breach of the BBC’s regulatory obligations.”*⁸⁸

Our findings

- 3.39 As discussed above, the Charter provides for the BBC Board having a role in setting the strategy for the BBC's commercial activities. The BBC Board also has ultimate responsibility for ensuring the commercial activities fit with the Mission and Public Purposes, are commercially efficient, do not damage the BBC brand or gain an unfair competitive advantage as a result of the relationship with the public service.
- 3.40 We therefore consider it appropriate that there is some representation from the BBC Board on the Commercial Board and our rules do not preclude overlaps in the membership between the public service and commercial subsidiaries boards/executive committees.⁸⁹ We welcome the recent changes the BBC has made to the Commercial Board, notably that a majority of the members, six out of ten are non-executives members (which is a change since stakeholders submitted responses to our Call for Evidence).⁹⁰

⁸⁴ PACT also raised some non-governance specific points. It stated it is unclear within the current BBC complaints guidance what aspects of fair trading processes link up with the complaints process (at page 14 of its response to our Call for Evidence). We expect the BBC to give appropriate prominence to information regarding how to make a complaint on its website. PACT also called for Ofcom to explain how it would intervene if the BBC breached the rules. As with any potential breaches of our regulations, we would assess any complaints from stakeholders or concerns we identify, before taking further action if appropriate.

⁸⁵ Directors UK response to the Call for Evidence, page 1.

⁸⁶ Directors UK response to the Call for Evidence, pages 1-2.

⁸⁷ Directors UK response to the Call for Evidence, page 2.

⁸⁸ Sky response to the Call for Evidence, page 8.

⁸⁹ Requirements A.15, A.16.

⁹⁰ As set out in Requirement A.4, when assessing these rules, we take into account factors including the balance of non-executive to executive directors, whether the chair is sufficiently independent from the public service, the extent of overlap in membership between the boards or executive committees of the relevant commercial subsidiary and the BBC Board and public service executive committees and the degree of influence that the public service has on governance and decision making within the relevant commercial subsidiary. See Guidance A.16.

Conflicts of interest

3.41 The BBC must have in place appropriate measures, controls and processes to ensure that where a director serves on the board and/or executive committee of both the public service and a commercial subsidiary any potential conflicts of interest are identified recorded and addressed. Greater overlap between members of the public service and commercial subsidiary committees increases the risk of information being inappropriately shared. The BBC is also required to report to Ofcom the conflicts of interest⁹¹ identified and describe all measures, controls and processes that it has implemented to address the resulting risks.

Summary of BBC arrangements

3.42 The BBC has explained that the BBC Board has a clearly defined and published code of practice⁹² which sets out guidance and requirements for all directors on conflicts of interest.⁹³ This code deals with all conflicts of interest (not just the ones specifically regarding our rules). The BBC said that the code is supported by its policy on information sharing (discussed above). The BBC has confirmed that meetings are assessed for conflicts of interest and any conflicts are noted in the minutes of the meeting as appropriate.

3.43 In addition, the BBC noted that decisions on all potential conflicts (i.e. not just the ones in relation to our rules) are also informed by the professional judgement of the secretariat team in discussion with affected individuals, regulatory policy and legal advisers, and take account of relevant professional guidance. Decisions on conflicts of interest ultimately rest with the Chairs of the relevant committees, based on the advice of the Secretariat.⁹⁴

3.44 The BBC stressed that it takes a cautious approach to conflicts of interest. For example, it said that any representative from BBC Studios would not be involved in a discussion on the BBC performance review papers if they included data on past audience reporting.⁹⁵ It considered that this was an overly cautious approach, but as there was a possibility the discussion could stray into future content and strategy discussions, it would not be appropriate for a representative from BBC Studios to be involved.⁹⁶

Conflict of interest reporting 2018/19 to 2020/21

3.45 The BBC has confirmed that it only shares with Ofcom⁹⁷ what it considers to be 'regulatory' conflicts of interest that relate to matters covered by Requirements A.1-A.5. In three years of annual reporting of conflicts of interest to Ofcom, the BBC has reported eight conflicts of interest. For example, three conflicts were reported relating to the CEO of BBC Studios being excused from the BBC Board discussion of programme investment cases.

⁹¹ Requirements A.5, D.2, D.3.

⁹² [Code of practice](#) [accessed 21 April 2022].

⁹³ BBC response to question 12 of the information request dated 9 March 2021 reference: 01128003.

⁹⁴ BBC response to question 12 of the information request dated 9 March 2021 reference: 01128003.

⁹⁵ BBC response to question 3 of the information request dated 19 November 2021 reference: 01378552.

⁹⁶ BBC response to question 12 of the information request dated 19 November 2021 reference: 01378552.

⁹⁷ BBC response to question 3 of the information request dated 19 November 2021 reference: 01378552.

Summary of stakeholder views

- 3.46 In response to our Call for Evidence, PACT requested that the BBC's annual conflicts of interest report to Ofcom be made public. It also stated that Ofcom's role in managing conflicts of interest is unclear.
- 3.47 The reporting information provides us with insight into how the BBC is complying with our rules but contains confidential information, so we continue to consider it appropriate that the BBC does not publish this. In relation to our role in this area, we monitor the BBC's compliance with our rules as well as respond to any complaints or concerns.

Our findings

- 3.48 Through our assessment, we have assurance that the BBC has effective policies and procedures in place to manage conflicts of interest. We consider that these policies and procedures would benefit from additional transparency on the arrangements in place on an ongoing basis. Therefore, we expect the BBC to include in its Annual Statement definitions of what the BBC considers relevant conflicts of interest to be, and a description of how conflict-of-interest decisions are taken. We also expect the BBC to include details of any changes made to its conflict-of-interest arrangements in its Annual Statement.

4. Supply and pricing of goods and services

Summary of findings

We have looked at how the BBC has implemented our rules on the supply and pricing of goods and services between the public service and the commercial activities. Our review has been informed by substantial information we have gathered from the BBC as well as other stakeholders and independent auditors.

Supply and pricing of goods and services – The public service sells a range of goods and services to its commercial subsidiaries and the market (including BBC Studios). To better understand the way the BBC does this, we looked at 14 transactions, representing about 8% of the value traded between the public service and BBC Studios in 2019/20, and found some issues with the administrative processes in place.

Secondary content sales – For certain categories of content where the public service owns the intellectual property and BBC Studios distributes it, co-production arrangements are in place. Under these arrangements BBC Studios is entitled to the entirety of the profit related to the distribution of the associated secondary content rights. This is a long-established practice and it does not appear to us that the BBC has fully reviewed and updated it in light of our rules.

We have not seen evidence of objective tests to ensure that co-production arrangements are warranted in every case and it is not clear to us how the BBC is satisfying itself that its arrangements are compliant with our rules.

Brand fee – We are broadly satisfied with the BBC's approach to charging BBC Studios for the use of the BBC brand.

Introduction

- 4.1 We have put in place rules for how goods and services should be supplied between the public service and BBC Studios (transfer charges). These are to ensure that BBC Studios does not receive an unfair advantage as a result of its relationship with the public service by, for example, the public service supplying studio space to BBC Studios at lower than market rate. The aim of our review is to better understand how the BBC has implemented our transfer pricing rules, to inform our view on whether the BBC has adequate information and processes in place to ensure compliance.
- 4.2 Our review has been informed by publicly available information as well as additional information we have gathered from the BBC and other stakeholders. As part of our work, we aim to increase transparency for stakeholders by setting out more details of the arrangements the BBC has in place.
- 4.3 In this section we provide an overview of our rules and discuss in detail three main areas that our analysis has focused on:

- a) **Review of total charges and sample of charges** – we have assessed a sample of transfer charges and their associated pricing methodologies to better understand how the BBC has implemented our rules. We have also reviewed the public service’s total charges for the different categories of goods and services it supplies to BBC Studios, to assess whether they look broadly appropriate.
- b) **Secondary content sales** – BBC Studios distributes programmes which are licensed to broadcasters and platform owners within the UK and globally (following the primary licence period with the commissioning broadcaster). The revenue from secondary content sales where the public service owns the IP is a significant revenue source for BBC Studios. Following some initial work we undertook in this area as part of our work on BBC Studios’ lines of business, we have sought to understand the BBC’s arrangements in more detail and how the BBC satisfies itself that it complies with our transfer pricing rules.
- c) **Brand fee** – the BBC brand is an asset which the BBC’s commercial subsidiaries, including BBC Studios, may derive value from. For example, BBC Studios may be able to charge higher prices or secure additional sales, compared to a situation in which it was unable to use the BBC brand. The BBC brand’s development and maintenance is funded by the licence fee, so in this review we have sought to understand how the BBC has implemented our rules to ensure that BBC Studios is paying an appropriate amount to the public service for the use of this asset.

Our rules

- 4.4 Where the public service provides goods and/or services to the commercial subsidiaries or joint ventures, it must ensure that this takes place at arm’s length and on commercial terms.⁹⁸ Our rules require the BBC to set prices and terms for goods and/or services supplied by the public service to the commercial subsidiaries, using an open market process (e.g. competitive tendering), or appropriate market benchmarks. In the absence of that market information, or where it is disproportionate to undertake specific benchmarking exercises, the BBC must set prices for goods and/or services using cost as a proxy for market prices. The BBC must ensure that any price based on cost includes all relevant long-run incremental costs of providing the good and/or service in question, an appropriate contribution to the relevant common and capital costs, and an appropriate margin.⁹⁹ In addition, our rules state that where the public service supplies goods and/or services to third parties, the BBC must not discriminate unduly as to terms and prices.¹⁰⁰
- 4.5 The BBC must set prices for business support goods and/or services which the public service only shares with the commercial subsidiaries that at least cover the long-run incremental costs of providing these services.¹⁰¹

⁹⁸ Requirement B.1.

⁹⁹ Requirement B.3.

¹⁰⁰ Requirement B.2.

¹⁰¹ Requirement B.4.

4.6 Our guidance sets out that where the public service supplies goods/and or services to its commercial subsidiaries and/or third parties the relevant economic concept for pricing is the opportunity cost to the public service. This reflects what the public service is giving up by choosing to supply a good or service to a particular party.¹⁰² Where the public service supplies a commercial subsidiary, rather than a third party, it is giving up the market price it could get from supplying that third party instead.

Total charges and accounting records

4.7 The BBC must also provide Ofcom a breakdown of total charges set by the public service to each commercial subsidiary, and by each commercial subsidiary to the public service.

4.8 The BBC must maintain accounting records:¹⁰³

- a) to show and explain the BBC's transactions;
- b) to disclose with reasonable accuracy, at any time, the financial position of the BBC; and
- c) to enable the members of the Board to ensure that any accounts required to be prepared comply with the Charter.

4.9 Our rules also require the BBC to maintain accounting records, including but not limited to relevant correspondence, contracts and invoices, for a period of six years from the date on which each record was created. The BBC must ensure that these records are sufficient to provide an adequate explanation of how the BBC has complied with each of the Requirements.¹⁰⁴

Secondary content sales

4.10 In 2019 we updated our rules to make it clear that transactions involving the licensing of content by the public service were included under the rules.¹⁰⁵ The guidance states that the supply of content/IP for secondary exploitation should be priced using market prices or benchmarks and in accordance with the 'opportunity cost' principle (set out above). In this case, assuming the public service would receive the same upfront investment from third parties, the opportunity cost of not distributing programmes through a third party is the residual revenue that the public service would otherwise be entitled to receive as an IP holder. Any differences between how the public service treats BBC Studios compared to third-party distributors need to be objectively justified.

¹⁰² Guidance B.11.

¹⁰³ Requirement D.24.

¹⁰⁴ This requirement includes providing an adequate explanation of the information published and provided to Ofcom (as applicable) pursuant to Requirements D.1 to D.17.

¹⁰⁵ Guidance B.15(a).

Brand fee

- 4.11 Our rules require that the BBC should set the brand fee by reference to market pricing or market benchmarking.¹⁰⁶ This ensures that the prices reflect the opportunity cost to the public service – the revenue forgone by not selling the product to a third party – which we consider best reflects the price which would be paid in an undistorted, competitive market. Where BBC Studios uses the BBC brand, this should be assessed in terms of what a third party might be willing to pay for the use of the BBC brand.¹⁰⁷ While this might be difficult to ascertain in practice, a reasonable proxy for this rate may be the proportion of revenues directly linked to its use.¹⁰⁸ Further, the BBC should ensure that its benchmarks are reviewed regularly in line with market practice, and it should be able to demonstrate that the data used is up to date and takes into account the nature and duration of the underlying contractual arrangements.¹⁰⁹

Review of total charges and sample of charges

- 4.12 The main services traded between the public service and BBC Studios are support services such as HR, finance and technology, as well as services such as production facilities, external communications and commercial rights.¹¹⁰

Summary of stakeholder responses and our views

- 4.13 Three stakeholders responded on our proposed scope of work in this area – Directors UK, PACT, and Sky. Broadly, the stakeholders agreed with our proposed work and in some areas suggested we should go further.
- 4.14 Directors UK agreed that goods and services should be provided at arm's length on commercial terms and that the BBC should be transparent in its reporting.¹¹¹ Sky also questioned how transparency would be improved.¹¹² One of the objectives of our work is for us and stakeholders to better understand the arrangements the BBC has put in place to comply with our rules.
- 4.15 In relation to our proposed sample of transactions, PACT welcomed the work we proposed to do, although it considered we should commission an independent audit of the whole of the BBC's transfer pricing system (not just the methodologies or principles).¹¹³ It noted that the BBC's 2018 review of its commercial activities found there were limits to the assurance

¹⁰⁶ Guidance B.15, 18 and 21.

¹⁰⁷ Guidance B.15 and B.21. This would take into a range of factors, including any restrictions that the public service might reasonably impose on the licensee of the BBC brand to protect the reputation and value of the BBC brand.

¹⁰⁸ Guidance B.15 and B.21.

¹⁰⁹ Guidance B.6 and B.19.

¹¹⁰ The full list of services traded between the public service and BBC Studios is set out in the [BBC Fair Trading: Consolidated Group Trading Manual](#).

¹¹¹ Directors UK's response Call for Evidence pages 2-3.

¹¹² Sky's response to Call for Evidence, pages 7-8.

¹¹³ PACT response to Call for Evidence, page 6.

provided by Deloitte’s fair trading report.¹¹⁴ Pact also highlighted EY’s recommendation in this review that the BBC should consider undertaking “*spot checks on prices to ensure they are appropriate and proportionate – to date we are not aware of this happening apart from general statements that ‘reviews’ are carried out each year on the prices – these do not confirm whether or not spot checks are made or whether the ‘review’ is carried out, what is found and then changed.*”¹¹⁵

- 4.16 We agree with Pact that a sample of transactions should be considered and not just the methodologies. However, we did not consider that an independent audit would be proportionate given that our main aim was to understand how the process worked in practice. We considered that our review of a small sample gives us a good understanding of the processes the BBC has in place and if we were content, would also provide us with a level of assurance over the rest of the transactions.
- 4.17 On support services, Pact was concerned that the use of the public service professional functions could be an indirect subsidy to BBC Studios. It also argued that market benchmarking and business support functions should include a margin to the public service.¹¹⁶ Sky agreed that charges for shared business support staff should be on commercial terms.¹¹⁷ As part of our 2019 review of the rules, we considered that the sharing of services such as HR, ICT and finance is a replicable advantage that competitors would enjoy as part of a large company with economies of scale.¹¹⁸ We have not revisited this issue as part of this review.

Existing assurance

- 4.18 As set out in our February 2019 Statement,¹¹⁹ we gain some assurance from the annual reviews already in place, such as the fair trading audit undertaken by Deloitte (commissioned by the BBC), the regularity and financial audit undertaken by the NAO, and an internal audit undertaken by the BBC.¹²⁰ Below, we describe these audits in further detail to help inform the additional work necessary within our review.

¹¹⁴ PACT response to Call for Evidence, pages 4-5.

¹¹⁵ PACT response to Call for Evidence, pages 4-5.

¹¹⁶ PACT response to Call for Evidence, page 6.

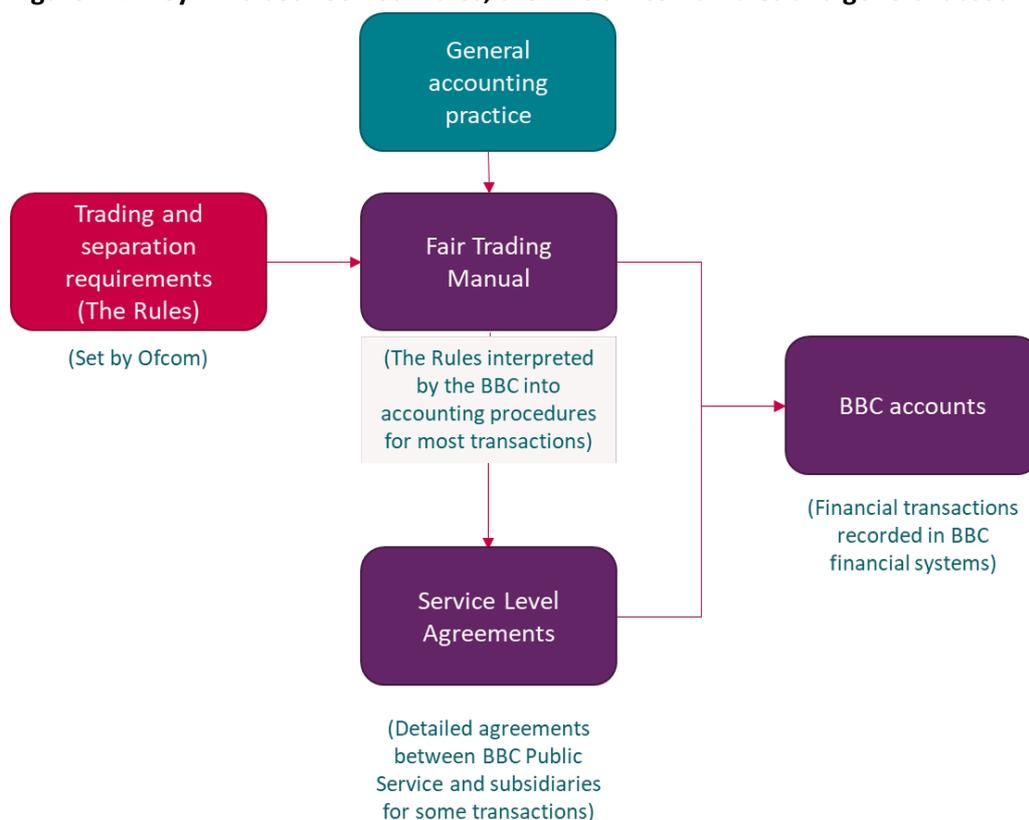
¹¹⁷ Sky response to Call for Evidence, pages 7-8.

¹¹⁸ [The BBC's commercial and trading activities: requirements and guidance, Statement on modifications to Ofcom's requirements and guidance](#), 11 February 2019. In footnote 116 (page 41) we note that we consider it is appropriate for the commercial subsidiaries to benefit from certain legitimate advantages where these services are replicable by third parties.

¹¹⁹ [The BBC's commercial and trading activities: requirements and guidance](#), Ofcom 11 February 2019.

¹²⁰ February 2019 Statement, paragraphs 6.101 to 6.108.

Figure 4.1: Key links between our rules, the BBC’s internal rules and general accounting rules



- 4.19 The BBC interprets our rules and general accounting practice into a set of accounting procedures in its Fair Trading Manual, which covers most of the transactions that are covered by our rules. Some of those transactions are also supported by Service Level Agreements (SLAs).¹²¹ The Fair Trading Manual and SLAs in turn inform how transactions are recorded in the BBCs accounts.
- 4.20 Deloitte’s fair trading assurance assesses whether the BBC has a system of internal controls in place that provides reasonable assurance that it has complied with our rules (including transfer charges).¹²² However, Deloitte does not look at actual transfer prices to check whether they are in line with our rules. It only assesses the extent of the controls that the BBC has in place in relation to the service level agreements, and if any changes to the transfer pricing methodologies applied by the BBC are appropriate in the context of our Rules.
- 4.21 The NAO as the BBC Group’s external auditors provide a regularity opinion on whether the BBC has materially complied with relevant laws and regulations that comprise the Group’s framework of authorities, having due regard to evidence of compliance with Ofcom requirements. They also audit the financial statements and balances and disclosures therein for the BBC group and its commercial subsidiaries and provide an opinion as to

¹²¹ Service Level Agreements are a contract between a service provider and customer (in this case between the public service and the commercial activities) that sets out the price and terms and conditions associated with the provision of goods and services.
¹²² The pricing principles are set out in Requirement B.3.

whether these statements and disclosures provide a true and fair view of the financial position and results of the audited entities.

- 4.22 In addition, the NAO's audit is subject to the materiality levels it sets for each entity in each year. The NAO sets the overall materiality level for the entities that make up the BBC group at £25m in the 2019-20 and 2020-21 financial years.¹²³ The materiality thresholds would be lower for the individual audits of the financial statements for the BBC's subsidiaries (including BBC Studios). These materiality levels are comparatively high for the consideration of transfer pricing because they relate to the financial results of the whole of BBC group and its subsidiaries. This means that certain issues which the NAO reasonably considers immaterial for audit purposes could be material for our consideration of transfer pricing.
- 4.23 We have also asked the BBC whether there were any one-off reviews of the BBC's transfer prices as part of its 2019/20 internal audit work and third-party reviews. The BBC set out a number of reviews it had undertaken as well as those of third parties which covered the rules. In particular, EY undertook a review of the Fair Trading Activities to assess the compliance of the BBC's trading activities with the BBC's Fair Trading requirements.¹²⁴ This review focused on the supply and pricing of goods by the BBC to the commercial subsidiaries and to the wider market, and the monitoring and transparency of those transactions. EY provided the BBC with actions for improvement, in relation to governance, transparency, records management, compliance monitoring and training. The BBC reported to the Fair Trading Committee how it had carried out these actions in January 2020. The review undertaken by EY, along with the BBC's response on the resulting actions does provide us with additional assurance, in particular around the consistency of the transfer charging with the information provided in the Fair Trading Manual. However, EY did not consider whether the sample demonstrated compliance with the rules.
- 4.24 The other relevant one-off reviews that took place as part of the 2019/20 internal audit work include:
- a) The internal audit team undertook a sample check of transactions to confirm whether there was an SLA in place and whether the charges made complied with pricing defined in the SLA/contracts; and
 - b) EY undertook a review of third-party income to the public service to ensure compliance with the Fair Trading Requirements.
- 4.25 All these audits provide some assurance on whether the BBC's transfer charges are set in compliance with our rules and whether the BBC reports those transfer charges accurately and completely. However, none of these audits look at the entirety of the BBC's approach, and whether this complies with the rules. Consequently, we have carried out our own review of the transfer charges to better understand in detail the processes and procedures by which the BBC sets these charges, invoices them and receives payment, in line with the

¹²³ [BBC Group Annual Report and Accounts 2020/21](#), page 196.

¹²⁴ BBC response to information request 01051318, question 10.

rules. Given the findings of our own review which we explain below, we will continue to monitor these audits and the BBC's compliance.

Our approach

- 4.26 We have reviewed how the BBC has implemented our rules in relation to transfer pricing in further detail. We have also attempted to gain a more detailed understanding of how the transfer charges are set. We have done this in the following ways:
- a) The main competition concern is that the level of transfer pricing for the goods and services that the public service provides to BBC Studios is set too low. We therefore considered the total transfer charges for key categories that take place between the public service and BBC Studios, and carried out a high-level review as to whether the transfer charges were reasonable, given the nature and size of the operations carried out by BBC Studios and its relationship with the public service.
 - b) We selected a small sample of goods and/or services from the Fair Trading Manual and reviewed one of the 2019/20 transactions for each of those services to gain a better and more detailed understanding of how the BBC ensures it sets transfer charges in accordance with our rules, and whether the BBC uses sufficient information and evidence to ensure compliance. This exercise was to gain a better understanding of how the BBC's processes work in practice; it was not an audit and it was not designed to enable us to form an opinion on the BBC's overall compliance with our rules.
- 4.27 Our analysis in both areas was focused on the financial year 2019/20 as this was the most recent time period available to us at the time. However, in our sample of charges work we also looked at the methodologies set out in the BBC's Fair Trading Manual¹²⁵ and considered whether the setting of the charges changed between 2019/20 and 2020/21. In undertaking our analysis, we reviewed publicly available information including the annual reports for the BBC and BBC Studios and the Fair Trading Manuals as well as information reported to us by the BBC and stakeholder responses to our Call for Evidence. We also gathered additional information using our formal powers.

Review of total charges

- 4.28 We completed an analytical review of the total transfer charges BBC Studios paid to the public service during the 2019/20 financial year for each key category. Using the reporting provided by the BBC under our rules¹²⁶ and the Fair Trading Manual, we looked at each category of transfer charge and compared the total with other related operational and financial data such as headcount, operating cost and revenue, depending on how costs were driven. Our aim was to assess the reasonableness of the amounts of the transfer charges BBC Studios paid the public service in each key category. For example, we compared property cost with headcount, based on the logic that headcount would largely

¹²⁵ [BBC Fair Trading: Consolidated Group Trading Manual, 6 July 2021.](#)

¹²⁶ Requirement D.8 requires the BBC to provide to Ofcom a breakdown of total Transfer Charges charged by the public service to each Commercial Subsidiary; and each Commercial Subsidiary to the public service.

drive the amount of office space required. Therefore, we would expect some correlation between headcount and property costs.

Our findings

- 4.29 We found that the overall level of the transfer charges looked reasonable for each of the key categories (we set out our concerns regarding secondary content sales separately below).
- 4.30 However, the work we did in this area highlighted some issues with the 2019/20 regulatory reporting provided to us under our rules. There were small errors in the reporting of the split of transfer charges into the key categories. There were also issues in mapping the Fair Trading Manual to the regulatory reporting. This reduced our understanding of how the transfer pricing process works as we were unable to rely fully on the Fair Trading Manual to understand the methodologies that underpinned the charges.
- 4.31 We wrote a letter to the BBC setting out our concerns about the accuracy of its regulatory reporting. In response, the BBC advised us in a letter dated 9 March 2022 of the changes it has now made to its process to address these concerns. The changes included additional training in relation to Ofcom's regulatory reporting requirements (implemented in September 2021) which will be refreshed at least annually with the guidance documentation updated twice a year. The BBC has also introduced a number of new checks to update its regulatory accounting processes and ensure transactions are accurately reported.
- 4.32 We note that the 2020/21 regulatory reporting has improved in these areas. We will continue to review and monitor the regulatory reports we receive to ensure they provide sufficient transparency.

Review of sample of charges

- 4.33 As explained above, we carried out this review to gain a better and more detailed understanding of how the BBC ensures that it sets transfer charges in accordance with our rules and whether it uses sufficient information and evidence to ensure compliance. This exercise was not an audit to enable us to form an opinion on the BBC's compliance with our rules.
- 4.34 The BBC's Fair Trading Manual sets out the different categories of transfer charges that are traded between the public service and BBC Studios. These categories cover charges such as HR, property, finance and legal as well as more production specific charges such as production facilities, archives, and commercial rights and business affairs.
- 4.35 We selected one service from each of the 19 transfer pricing categories and asked the BBC to provide the largest five transactions for each of these services. We then selected transactions from these services, ensuring we covered the different bases for the prices i.e. benchmark, direct cost and market price, as well as across a range of different monetary values. In total, we selected 14 transactions for our sample review (accounting for £5.2m out of the £67m total transfer charges BBC Studios paid the public service in 2019/20).

- 4.36 For each transaction we asked the BBC to provide all the information it used to ensure the transaction was consistent with the Fair Trading Manual and complied with our rules. We expected the BBC to provide the following types of information:
- a) Calculations or explanations for how the transfer charges were set by the public service. Where the charges were based on cost, we expected there to be some underlying calculations which set out how much should be passed on to BBC Studios.
 - b) Where the charges were set using a benchmark, we expected the BBC to have evidence of how the benchmark was set, along with evidence that the charges are in line with the benchmark.
 - c) Where the charges were based on the market price, we expected there to be evidence of the process taken to determine market price and documentary evidence of the market price benchmarks obtained.
 - d) Relevant documentation setting out the terms that have been agreed between the public service and BBC Studios such as the price, how long that price is set for, terms of payment as well as evidence of those terms being met.

Our findings

- 4.37 Our review proved more challenging to complete and took more time and effort than expected. To be able to receive the information necessary to complete our work, we had to go through various rounds of requests to the BBC for clarification, to obtain missing information or explanations.
- 4.38 The process of our review (including the challenges) and the totality of the information provided did not give us comfort that the BBC uses sufficient information and evidence and has all the necessary checks and balances in place to ensure compliance with our rules. We set out below some examples of the findings that have led us to this view:
- a) The BBC did not appear to have evidence of agreed settlement terms for some of the sample transactions.
 - b) In relation to one sample transaction, the BBC did not provide sufficient evidence that the settlement terms were set on a commercial basis. It has now made adjustments to ensure the terms are commercial.
 - c) The BBC did not retain complete records of its calculations relating to one of the sample transactions.
 - d) With regard to one of the transactions we sampled, the BBC had set the transfer prices below the market prices. This issue was later identified by a BBC review and was addressed.
 - e) The BBC did not provide sufficient supporting calculations/information for some of the assumptions or inputs to the sample transactions.
- 4.39 In the course of our review, the BBC asked us to consider targeting our regulatory reporting on the areas which carry a demonstrable risk of market harm. The BBC also asked

us to establish a materiality threshold for our rules to avoid disproportionate compliance costs. We plan to consider these requests within the upcoming competition consultation as part of our review of how Ofcom regulates the BBC.

Secondary content sales

- 4.40 BBC Studios produces and distributes programmes which are licensed to broadcasters and platform owners globally. Before the creation of BBC Studios in April 2017, the public service produced much of its content in-house. BBC Worldwide (now BBC Studios) typically distributed this content once the primary window had finished (i.e. it licensed the content on behalf of the public service to be shown on third-party UK and international broadcaster channels and platforms). In 2017 the majority of production was moved out of the public service and BBC Studios was created. The public service retained the intellectual property (IP) for any programmes created before this date, including those where the public service was still commissioning returning series. This was to ensure it did not provide BBC Studios a significant competitive advantage of a large library of exploitable content at the point it was created. Secondary content sales from distributing the related content is a significant revenue source for BBC Studios.¹²⁷
- 4.41 In this section we set out stakeholder responses, the arrangements the BBC has in place and our findings. Finally, we discuss the interaction of this issue with our rules relating to commercial rate of return.

Summary of stakeholder responses

- 4.42 In response to our Call for Evidence, Directors UK stated that *“where there is a transaction between the public service and BBC Studios relating to the production or distribution of content directed by freelance directors, they, along with other rights holders, should be compensated at commercial rates.”*¹²⁸ We set out our consideration of this response in our analysis section below. No other stakeholders commented specifically on content in relation to our Call for Evidence.
- 4.43 In March 2021, we wrote to nine production companies which ranged in size, asking questions in relation to their agreements with distributors (which in some cases was a related group subsidiary). Four companies responded and the arrangements they have in place mirror those BBC Studios has in place for its own IP or when it distributes third-party content. They also stated that the commission the distributor kept was between 25% to 30% of sales or at market rates.

¹²⁷ The value of this may also be larger than the revenue from all other transfer charges combined. Based on gross profit from secondary content where the public service own the IP in 2017/18 and 2018/19 we estimate [£] could be returned to the public service as the IP holder whereas total transfer charges from the public service to BBC Studios were c.£67m (2019/20).

¹²⁸ Directors UK's response to the Call for Evidence, pages 2-3.

Summary of BBC arrangements and its explanation

- 4.44 BBC Studios distributes content where the IP is owned either by BBC Studios, the public service or third parties. We understand that the arrangements in place to distribute some content where the public service owns the IP reflect long-standing agreements which appear not to have been reviewed since we introduced our rules in 2017 (and updated them in 2019). The vast majority of investment into currently PS owned IP occurred prior to 2017. The public service owns the IP for the following programmes:
- a) Productions made before 2017 (i.e. before the majority of production activities were moved out of the public service to BBC Studios);
 - b) Returning series, where the first series was created or was in production before April 2017 (e.g. *Dr Who*, *Top Gear*, *Silent Witness*),¹²⁹ and
 - c) New productions made by staff who remained in the public service (e.g. children's).¹³⁰
- 4.45 BBC Studios has often provided (and in the case of returning series, may continue to provide) upfront investment in content for which it does not own the IP. We understand that BBC Studios has the following distribution arrangements:
- a) Where a third-party producer owns the IP, BBC Studios would usually be entitled to retain: the costs it incurs relating to selling the content, its commission and any royalties it is responsible for (e.g. to talent), and to recoup any upfront investment in the programme. Any remaining revenue is subject to any terms of the relevant investment agreement, which returns that revenue, or a proportion of that revenue, to the IP holder; and
 - b) Where the BBC public service owns the IP, there is a different process depending on whether BBC Studios (or previously BBC Worldwide) had invested/continues to invest in the programme:
 - i) Where there was no upfront investment, BBC Studios returns the residual revenue directly to the public service (as the IP holder for this content).¹³¹ This is similar to the arrangements it has with third-party producers where BBC Studios has made no upfront investment to secure distribution rights.
 - ii) Where BBC Studios (or previously as BBC Worldwide) invested, and (in the case of returning series) continues to invest in a programme, it does not return residual

¹²⁹ Our regulation requires the BBC to tender out the production of all relevant programmes by 2027, there is no requirement on it to have a competitive process in place in relation to tendering the distribution rights. Therefore, regardless of who wins the production for hire contract for returning series, BBC Studios will continue to distribute all new series (where it was distributing the original series), and retain the right to distribute the previous series, as long as it continues to provide upfront investment. The term duration for all previous series will automatically be extended. If the incumbent distributor is not willing to provide upfront investment, the public service may seek a new distributor which is willing to provide this. To aid this, it may negotiate with the old distributor to release earlier series in order to sell a bundled package of distribution rights for the entire series. If it is unsuccessful in securing a new distributor, then the incumbent distributor may retain the rights to distribute the new series.

¹³⁰ Note, BBC children's production moved into BBC Studios in April 2022. As a result, there are now very few productions that are produced by the public service and distributed by BBC Studios.

¹³¹ The amount of revenue returned for this content is reported to Ofcom as part of confidential transfer pricing reporting.

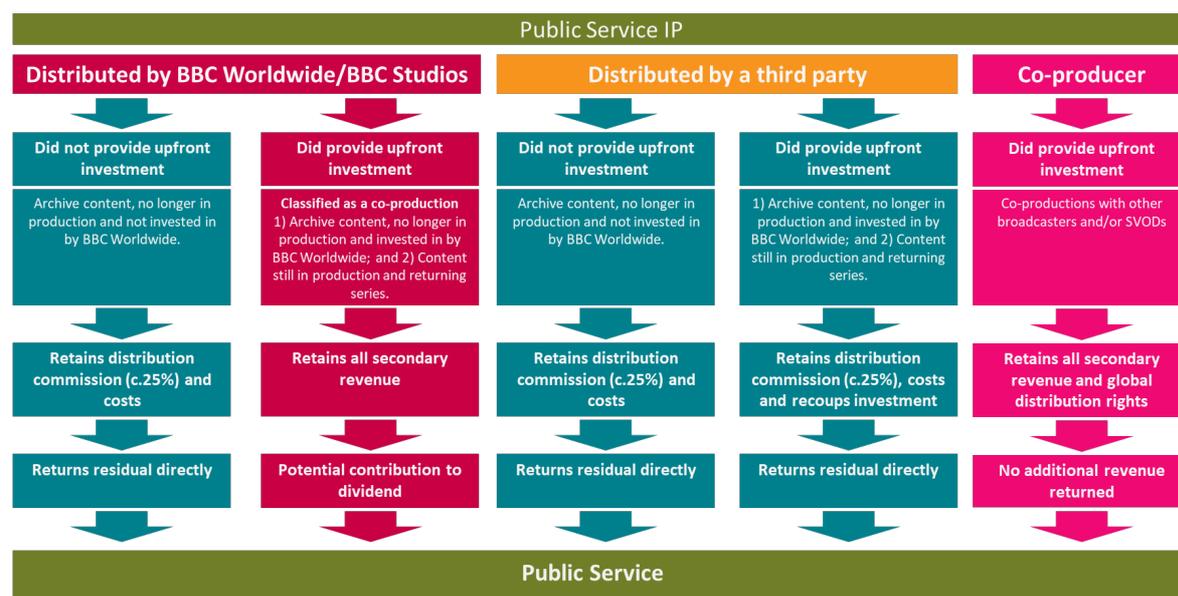
revenue directly to the public service but retains it within BBC Studios. The BBC classifies these productions as co-productions irrespective of the amount of up-front investment.¹³² In May 2022, the BBC wrote to us setting out how it considered its approach was fully consistent with our rules, and the Charter and Agreement i.e. by virtue of co-production agreements being in place.

- 4.46 The BBC classifies the programmes where the public service owns the IP and BBC Studios has invested as co-productions for the following reasons:
- a) BBC Studios (distribution) is acting as a co-producer when it is investing in programmes where the public service owns the IP (similar to when the PS enters a co-production deal with an international broadcaster, VOD platform or distributor);
 - b) As a co-producer BBC Studios will provide / be entitled to creative input, e.g. on casting, story arcs, etc;
 - c) In co-production deals, key exploitation routes are often 'traded away' in exchange for up-front investment i.e. the producer receives more cash upfront than would be the case in a sales-agent relationship; and
 - d) In addition to programme investment, Studios delivers benefits to the public service that are not reflected in individual deals, like brand protection, promotion of the BBC brand and management of compliance.
- 4.47 Where third parties distribute content for which the public service owns the IP, the third-party distributor deducts an agreed distribution commission and expenses from sales revenue, and after any other contractual payments (e.g. payments to talent) and recouping any upfront investment, returns all residual revenue back to the public service. This is irrespective of the level of upfront investment i.e. these agreements are not classified as co-productions in the same way.¹³³ This is consistent with the arrangements in place when BBC Studios distributes third-party content.
- 4.48 Figure 4.2 represents our summary of these arrangements. As highlighted in red, for programmes where the public service owns the IP, there are different arrangements in place for content, depending on whether BBC Studios provided upfront investment or did not do so, or where third parties distribute the content.

¹³² In its May 2022 letter to Ofcom, the BBC shared a definition of a co-production as: "an investment agreement under which money (or value in exchange for monetary value) is invested into an in house programme or content by an appropriate party, in return for rights in and to the programme or content, publishing or other rights, and the co-producer will have varying degrees of editorial input into their version. Co-productions can be done with a range of partners so long as they are deemed 'appropriate' in accordance with the BBC Editorial Guidelines (such to be determined in conjunction with Editorial Policy). Traditionally this was with broadcasters, but this is no longer necessarily the case. Appropriate co-production partners may include broadcasters, programme/film distributors, independent producers, record companies, audio visual producers, software and web service producers and institutions involved in arts and education (such as theatres and music companies)." CRBA Guidance on working with commercial partners in co-productions, co-venture etc

¹³³ This is set out on page 44 of the 2020 BBC Fair Trading Manual.

Figure 4.2: Summary of the public service’s arrangements for the distribution of content



Source: Ofcom, based on explanations from the BBC. This is a simplified diagram for illustrative purposes. In each scenario there may be payments made to others e.g. talent – but these are likely to be similar under each scenario.

4.49 The BBC estimated that the gross profit¹³⁴ for BBC Studios relating to the distribution of titles where the public service owns the underlying IP ranged from [£<]. The BBC was unable to provide similar information for 2019/20 and 2020/21 as its new accounting system was designed around the information BBC Studios management use to monitor financial performance, i.e. by title, genre and portfolio. The BBC stated it was not designed to monitor performance by IP owner. However, it should be noted that, while the gross profit from distribution of this content will likely vary year by year depending on the distribution revenue mix, it is likely to decline in absolute terms as series are discontinued, and in relative terms as BBC Studios develops its own IP.

Our findings

4.50 As part of our statement on BBC Studios’ changes to its lines of business,¹³⁵ we recognised that the relationship between the combined production and distribution lines of business and the public service was complex. To gain a better understanding of the BBC’s arrangements in relation to secondary content sales we engaged with the BBC to understand how it was approaching compliance with the requirements for arrangements to be at arm’s length and on commercial terms and non-discriminatory.

¹³⁴ Where gross profit equals distribution revenue less amortisation of distribution rights, commission, contributor costs and other direct costs.

¹³⁵ Ofcom, [BBC Studios' lines of business: Assessment of BBC Studios' changes to its lines of business](#), 30 April 2021.

- 4.51 Based on the differences noted above, we have two concerns in relation to content distributed by BBC Studios where the public service owns the IP and BBC Studios/Worldwide has invested upfront (which the BBC classifies as a co-production):
- a) BBC Studios keeps the entirety of secondary content sales when distributing this content. As such, the arrangements may not fully reflect the requirement for transfer charges to be at arm's length on commercial terms, as set out in our rules;¹³⁶ and
 - b) The BBC has not objectively justified why other third-party distributors were not able to access the same terms as BBC Studios. Therefore, these arrangements could have the potential to be unduly discriminatory.
- 4.52 Based on the information provided to us over the course of our review, it appears that the BBC has the same co-production arrangement in relation to all productions where BBC Studios/Worldwide invested upfront and the public service owns the IP. The BBC explained that public service staff who are experts in content arrangements review the levels of upfront investment, and the additional value BBC Studios adds as a co-producer, to ensure that the deals are set on a commercial basis.
- 4.53 We do not consider that the views of internal experts can provide the same assurance as an objective set of criteria which can be applied without discrimination to BBC Studios and third parties. We have not been provided with evidence of any analytical methods or checks the BBC undertakes to verify that the deals its staff are making are on commercial terms. The risks here are particularly acute, given the risk identified when BBC Studios was created that it should not be gifted IP. The substantial value being traded has an impact on BBC Studios' cashflow and its rate of return.
- 4.54 In principle, the public service entering into a co-production deal with BBC Studios for a specific programme could be compliant with our rules. However, based on the information we have seen, we are still concerned that there may not be adequate processes in place to determine whether the value the public service receives from BBC Studios as its distributor/co-producer is in line with the value of the rights being traded. We are therefore not clear how the BBC Board is satisfying itself that these arrangements are at arm's length and on commercial terms.
- 4.55 We recognise that the commercial arrangements with BBC Studios (formerly BBC Worldwide) are long-standing arrangements which were in place before our rules took effect. However, they are now within the scope of our regulation, and it is for the BBC Board, in the first instance, to consider how to address the issues identified above.
- 4.56 We will be consulting in the autumn on changes to our competition regulation as part of the review of how Ofcom regulates the BBC. As part of this consultation, we will take account of how the BBC has responded to these findings in determining what (if any) changes or further action we consider to be appropriate.

¹³⁶ See paragraphs 4.4 to 4.6 and 4.10.

- 4.57 We would also be interested in representations from stakeholders if they have any concerns about the BBC's arrangements, to assist with our ongoing regulation of the BBC.

Secondary content sales and interaction with rate of return

- 4.58 BBC Studios is required to earn a commercial rate of return over an appropriate period of time (including for each line of business within it).¹³⁷ As discussed in Section 2, in this review we set out to provide more clarity in this area, including publishing the results of our benchmarking analysis.
- 4.59 Given our concerns regarding the content issue, we have decided not to publish the results of our benchmarking work as we are unable, at this time, to select appropriate benchmarks for BBC Studios' lines of business.¹³⁸ We will set out a timeline for the publication of benchmarking in our autumn consultation.¹³⁹

Brand fee

Summary of stakeholder response and our views

- 4.60 In response to our Call for Evidence, PACT said it would like to see more detail about how the BBC calculates the transfer charges for use of its brand, and reiterated its concern regarding the uncertainty of the exact value of the BBC brand. It stated *"it is unclear what ranges are used in the calculations and that simply stating a percentage is unclear."*¹⁴⁰ PACT asked what information Ofcom received, and whether we are able to confirm that we *"interrogate any instance where the brand fee is excluded."*¹⁴¹ No other stakeholders commented on the brand fee.
- 4.61 One of the aims of our review was to provide more transparency to the arrangements the BBC has in place, so by doing so, we have in part, addressed PACT's comments raised.

Summary of the BBC's arrangements

- 4.62 Distribution and production revenues have brand fees applied and have separate Brand Licences¹⁴² which include different calculations. This is covered on pages 42 to 44 of the BBC's Fair Trading Manual. We set out a summary of these below.

¹³⁷ Requirement C.1. If the BBC determines that it will not earn a commercial rate of return, it must notify us and take appropriate steps to return to earning a commercial rate of return over an appropriate period (Requirements C.4 and C.5)

¹³⁸ If changes were to be made to the arrangements, it is likely that BBC Studios' (and the production and distribution line of business') rate of return would need to be adjusted.

¹³⁹ Our benchmarking will probably to take account that BBC Studios does not own the IP for most of the programmes it distributes.

¹⁴⁰ PACT response to Call for Evidence, December 2020, page 5.

¹⁴¹ PACT response to Call for Evidence, December 2020, page 5.

¹⁴² Brand Licence – The agreement between the BBC Group and BBC Studios, allowing BBC Studios to use the BBC brand on its products. These licences set out the Brand Royalty Rate, criteria for included revenues, payment terms and how the brand can be used.

BBC Studios Production

- 4.63 The BBC has two principles for determining which production revenue streams it considers the brand fee should be applied to:
- a) BBC Studios Production should only pay a brand fee where it has benefited from the BBC brand to win commissions and the revenues associated with each commission; and
 - b) BBC Studios Production should not have to pay a brand fee on revenues which derive from BBC Studios Distribution, as a brand fee will already have been paid under the arrangements relating to distribution.¹⁴³
- 4.64 The BBC has set out which production revenue streams it considers should attract a brand fee:
- a) Third-party primary commissioning revenues: When BBC Studios produces for a third-party commissioner, a brand fee will be charged at [X] of the resulting revenues; and
 - b) Third-party secondary commissioning revenues: When BBC Studios distributes through a third-party distributor, and the commissioner is also a third party, a brand fee will be charged at [X] of the resulting revenues.

BBC Studios Distribution

- 4.65 Within BBC Studios Distribution there are two revenue streams on which a brand fee is charged: branded revenues and non-branded revenues. These brand fees are set out below:
- a) [X] of revenue raised by BBC Studios Distribution from commercial activity generated from services using the BBC Masterbrand (e.g. BBC America, BBC Books or BBC Earth); and
 - b) [X] of all revenue raised by BBC Studios Distribution from all its other operations, with some exclusions.
- 4.66 As set out in the Fair Trading Manual, the BBC has decided that some revenue streams should not have a brand fee applied, as it considers that they do not derive a benefit from the BBC brand, or to avoid double counting. The BBC listed these revenue streams, along with an explanation which we discuss further below and in table 4.3.

Table 4.3: Revenue streams excluded from brand fee¹⁴⁴

Detail of revenue stream	Summary of the BBC's explanation why the brand fee is not applied
Primary and secondary production revenue deriving from BBC commissions	Brand does not contribute to BBC Studios winning BBC commissions, as programme will already have BBC branding

¹⁴³ The Brand Fee Methodology of the [BBC Fair Trading Manual](#), 6 July 2021, pages 42-44.

¹⁴⁴ This table shows the revenue streams relevant to BBC Studios.

Detail of revenue stream	Summary of the BBC’s explanation why the brand fee is not applied
Secondary production revenue deriving from third party commission, distributed by BBC Studios	BBC Studios distribution pays a brand fee already, so excluding this revenue stream avoids double counting
Indies and consolidated income from UKTV	Commercial performance is not linked to BBC brand, as they do not feature the BBC brand or have a public profile as BBC entities. Programme sales to UKTV are included in branded revenues
Hedging	Hedging income does not have a relationship to the BBC brand

Source: BBC response to information request reference 01128003, dated 31 March 2021, Question 21.

- 4.67 In relation to the percentage of revenue used to calculate the brand fee, the BBC has confirmed that it continues to use a report commissioned from PwC in October 2011 as guidance for its pricing principles. This was a report requested by the BBC to review the appropriate pricing principles for the licensing of the BBC brand to its commercial subsidiaries, and BBC Worldwide in particular. In this report PwC benchmarked the BBC’s use of the BBC brand against comparable brand licensing arrangements. It found that a royalty payment in the range of [x] to [x] on revenue is consistent with market practice. PwC ‘s findings highlighted that the BBC royalty rate should fall towards the lower end of the range provided, due to the limitations in how the BBC can exploit its brand.¹⁴⁵ The BBC has confirmed that it uses this as guidance for its royalty rate range and explained that it continues to use the lower end of the range where the BBC brand is not directly involved, and a higher fee for activities clearly using the BBC Masterbrand.¹⁴⁶
- 4.68 In response to our request for information, the BBC explained that the percentages used for brand fees were reviewed by EY in its 2016 report. This found that the BBC’s approach and use of the benchmarking report was appropriate.¹⁴⁷ EY did find issues around documentation, record-keeping and transparency with regard to external stakeholders.¹⁴⁸ EY noted that the public service and commercial subsidiaries engage in open-ended contracts with limited (if any) scope for review of pricing and other contractual arrangements, and considered that there should be regular reviews of the relevant pricing benchmarks to ensure that the terms continued to be in line with market practice.¹⁴⁹

¹⁴⁵ Summary of PwC report *What is an appropriate royalty for the use of the BBC brand by BBC Worldwide?*, October 2011, pages 3-4.

¹⁴⁶ BBC response to information request reference 01128003, 31 March 2021, question 23.

¹⁴⁷ BBC response to information request reference 01128003, 31 March 2021, question 23.

¹⁴⁸ Executive Summary of *A review of the BBC’s transfer pricing regime*, EY report for the BBC Trust, June 2016, pages 3-6.

¹⁴⁹ EY report for the BBC Trust, *A review of the BBC’s transfer pricing regime*, June 2016, page 65.

Other revenue sharing arrangements

- 4.69 There are some revenue-sharing arrangements which relate to the licensing of BBC brands to third parties. These include royalties paid by BBC Studios to the BBC in relation to children's-related magazines and merchandising, and CBeebies Land at Alton Towers.¹⁵⁰
- 4.70 For example, in relation to BBC-branded children's magazines and merchandising, BBC Studios retains a small share of gross revenue from magazine publishers in relation to titles where BBC Studios maintains an editorial governance process, and therefore incurs cost. As with other forms of BBC content, where BBC Studios has not invested, it returns the residual revenue back to the BBC, whereas where BBC Studios provided upfront investment to license the rights, it did not pass any revenue back to the public service. However, we note that the amount of revenue BBC Studios receives in relation to this is relatively small.¹⁵¹
- 4.71 We also note the arrangements the BBC has for licensing its brands to Alton Towers, for example within CBeebies Land and Hotel. We understand that Alton Towers pays both a fixed-fee element, and a share of secondary income. A share of the revenue received by BBC Studios is passed to the public service as a fee.¹⁵²

Our analysis and findings

- 4.72 We have assessed the BBC brand fee methodology and consider that this is consistent with our rules. The brand fee charged relates to the value the activity derives from the BBC brand. We agree with the principles the BBC uses to determine which revenue streams have a brand fee applied to them. We consider that the brand fee should relate to the ability of BBC Studios to derive benefit from use of the brand, and we agree that a brand fee does not need to be paid twice for the same content. We also agree with the BBC's conclusion¹⁵³ that the revenue streams set out in table 4.3 should not attract a brand fee for the explanations given. We note there is a higher rate on distribution activities which directly use the BBC Masterbrand,¹⁵⁴ and a lower rate for other activities which benefit from the brand to win commissions,¹⁵⁵ reflecting differences in the value derived from the brand.
- 4.73 As set out in our rules,¹⁵⁶ the BBC is required to review its benchmarks regularly to ensure that they reflect current market practices and norms. As noted above, the brand fee was last reviewed in 2016; specifically, the benchmarking for percentage applied to calculate the brand fee was examined by EY. We are not aware that the BBC has plans to update the

¹⁵⁰ This revenue totalled [redacted]. Source: BBC response to information request reference 01128003, dated 31 March 2021, question 18.

¹⁵¹ We understand that BBC Worldwide sold this business for £121m.

¹⁵² BBC response to information request reference 01378552 dated 19 November 2021, Question 8. C

¹⁵³ As provided in the BBC's response to information request reference 01128003, dated 31 March 2021, question 21.

¹⁵⁴ The BBC Masterbrand within BBC Studios' registered Corporate Names (e.g. "BBC Earth") and Business Names (e.g. "BBC Books"), Brands and Usage of the [BBC Fair Trading Manual](#), 15 September 2020, page 47.

¹⁵⁵ The Brand Fee Methodology of the BBC Fair Trading Manual, 15 September 2020, pages 48-50.

¹⁵⁶ Requirement B.6 and Guidance B.19.

percentages charged for brand fees. It is important that the BBC reviews the brand fee on a regular basis, we expect a review of this to be undertaken shortly in order to satisfy the guidance in this area, to ensure this reflects the changing market context and norms. When the BBC reviews the brand fee, it would be helpful if it provided information on this as part of its Fair Trading Manual and increase transparency in this area (including information on updates to the percentage applied to each revenue stream (subject to commercial confidentiality)).

- 4.74 In relation to revenue-sharing arrangements (such as children’s merchandising and CBeebies Land), the opportunity cost principle set out in our rules¹⁵⁷ applies where the public service is supplying goods/and or services to the commercial subsidiaries. The opportunity cost of not licensing the BBC brand to third parties is the residual revenue that the public service would otherwise be entitled to. We consider that BBC Studios ought to have the same arrangements in place that it has with third parties, and that any differences should be objectively justified. We expect the BBC to review its revenue-sharing arrangements (detailed above at paragraphs a4.69-4.71) in the light of our rules, including the opportunity cost pricing principle, and to ensure that it aligns with them.

Next steps

- 4.75 Based on the above findings, we conclude that the BBC must strengthen its approach to compliance with our rules. We expect the BBC Board to take action to update both its approach to secondary content sales and the supply and pricing of goods and services.
- 4.76 It is for the BBC Board to assure itself that it has the right processes and procedures in place and all the relevant information to ensure compliance with the rules.
- a) Secondary Content Sales – given the risks of an unfair advantage or market distortion, the BBC’s reliance on its expert staff is insufficient. We expect the BBC to review its arrangements against a set of objective tests.
 - b) Transfer Pricing – our findings show that the BBC should conduct its own assessment and detailed review of its transfer charging process and make any necessary changes to these as a result of its assessment. These changes could include strengthening both the internal controls and the internal audits with respect to transfer charges.
- 4.77 We also expect the BBC Board to look more broadly at the issues raised and satisfy itself that its processes and arrangements are in accordance with our rules.
- 4.78 Later this year we plan to consult on potential changes to the competition regulation, as part of our review of how Ofcom regulates the BBC. In that consultation we will take account of the findings of this review and any subsequent changes made by the BBC to determine whether new rules, or amendments to the existing rules, are required to address our concerns.

¹⁵⁷ Guidance B.11.