Public Service Content in a Connected Society

Ofcom's third review of public service broadcasting

Response from the Commercial Broadcasters Association to Ofcom

February 2015

A VOICE FOR COMMERCIAL BROADCASTERS IN THE UK

Executive Summary

1. We agree with Ofcom's overall conclusion that "the PSB system remains strong."[1] We base this on a number of positive factors:

    - Audience views: Viewer satisfaction increased significantly between 1998 and 2013, from 69% to 77%.[2]

    - Market position: The PSBs maintain near universal reach and, with their portfolio services, a combined audience share of 72.5%, representing nearly three quarters of the market.[3] Their on-demand services are market leaders.

    - Output: While PSB hours of first-run originations have fallen by 5% since 2008, the volume of new content in peak, when most audiences are watching, has increased.[4]

2. While PSBs' spending on first-run originations has dropped by 17.3% in real terms since 2008, the fact that first-run hours dropped by only 5% suggests this has not had a major impact on output. Moreover, declines levelled out in 2013, with most genres flat or rising slightly year-on-year. Where spending continued to fall – such as in news – hours were broadly flat.[5]

3. Additionally, the majority of the 17.3% decline is due to inflation, as Ofcom states. A major factor behind this is the flat licence fee settlement of the BBC, rather than any underlying market conditions. In addition, it is questionable whether all costs in the production sector have risen in line with inflation. And finally, PSBs' investment is being augmented by third-party investment from producers and the recently introduced tax reliefs for high-end television and animation. More than 80 television productions used the tax break last year, including such dramas as the BBC's Wolf Hall and Poldark, and ITV's Foyle's War and Downton Abbey.[6]

4. All of this is quite apart from the dramatic increase in investment in original content from non PSBs, who have increased their spending on first-run UK

[1] Public Service Content in a Connected Society, Ofcom's Third Review of Public Service Broadcasting, Section 2.46, page 3

[2] Ibid, Figure 20, page 44

[3] Ibid, page 81

[4] Ibid, Section 1.22.2, page 4

[5] Ibid, figures 28 and 29

[6] http://www.bfi.org.uk/news-opinion/news-bfi/announcements/new-bfi-stats-show-record-year-uk-film-2014

programming by 43% since 2008.[7] While we believe Ofcom's figures for non PSB commissions are conservative, they are broadly in line with COBA's 2014 Census and we welcome the regulator's overall analysis of the UK's increasingly "mixed ecology"[8] of PSB and non PSB investment as a positive – potentially ground-breaking – step in elucidating policy discussions.

5. Along with sustaining levels of investment in original content, and meeting many public service objectives, we believe this growing investment from non PSBs brings a number of unique – possibly irreplaceable – benefits to the overall ecology. These include:

    - Creating genuine plurality in commissioning beyond the four PSBs.
    - Providing audiences with increased choice, with a range of additional services, often serving niche audiences in a way that PSBs rarely do.
    - Strengthening the financing system for original production by widening the range of funding streams with pay TV revenues. During the last advertising downturn, between 2009 and 2011, multichannel commissions from independent producers remained stable, while commercial PSB investment dropped significantly.[9]
    - Further diversifying and strengthening funding streams for original production with access to overseas markets through substantial international divisions. COBA members report that 35% of their UK commissions involve leveraging investment from their international divisions.[10]
    - Sustaining the UK's global reputation for creativity by ensuring that a flow of new ideas reaches the screen. Non PSBs invest more than the BBC on new commissions from independent producers (as opposed to re-commissioning existing shows, or "returning series"), and nearly double the amount of the commercial PSBs combined. In 2013, the multichannel sector spent 58% (£221m) of its total investment in commissions from independent producers on new shows. In comparison, the BBC spent 34% (£162m) on new ideas; Channel 4 21% (£84m); Channel 5 15% (£6m); and ITV 8% (£29m).[11]

---

[7] Public Service Content in a Connected Society, Ofcom's Third Review of Public Service Broadcasting, December 2014

[8] Ibid, Section 1.6, page 1

[9] Independent Production Sector Financial Census and Survey 2014, Oliver & Ohlbaum Associates for Pact, page 14

[10] Building A Global TV Hub, Communications Chambers for COBA, page 7

[11] Independent Production Sector Financial Census and Survey, O&O for Pact, July 2014, page 16

6. Looking ahead, we believe the PSB system will remain strong for the foreseeable future. This is supported by Mediatique's analysis for Ofcom, which concluded that "fundamental challenges to the sustainability of PSB genres are unlikely to materialise over the medium term."[12]

7. We expect audience consumption patterns to evolve gradually, rather than change dramatically: despite technological developments, levels of live linear viewing remain at 84%.[13] PSBs have used the strength of their main PSB channels to grow their portfolio services, and this advantage is also benefiting their on-demand services. Out of all on-demand services, the BBC iPlayer is the most used at 38%, followed by ITV Player on 22% and 4OD on 20%.[14]

8. We therefore see no need for further intervention or changes to the existing framework. If Ofcom believes there is a gap in PSB provision, we suggest its first priority should be to ensure that the true value of the PSB licence is being realised on behalf of the public. Ofcom recently acknowledged that the value to the PSBs' linear portfolio channels from their relationship to a PSB service should be factored into the valuation of the commercial PSB licences.[15] We support this and ask Ofcom to also include the value to PSBs' on-demand services, if it is not already doing so.

9. Above all, we ask Ofcom to be mindful of the potential negative impact on the wider market of any proposals to strengthen the PSB regime. While Ofcom's analysis of investment by non PSBs is insightful, the regulator has not considered the impact on non PSBs from the suggested policy options.

10. Our view is that simply transferring revenues from non PSBs to PSBs risks a number of negative impacts. Reducing revenues for non PSBs would be likely to dampen the rate of growth in investment in original content – damaging the part of the industry that Ofcom has identified as the only source of growth in new commissions. At the same time, we are not clear how Ofcom would ensure PSBs would re-invest additional revenues in specific areas where there is perceived to be shortage, without introducing genre quotas.

11. Most importantly, though, damaging investment by non PSBs risks losing the often unique benefits they provide, including exceptionally high levels of

[12] PSB Review: Investment in TV genres, Mediatique for Ofcom, December 2014, page 75
[13] Public Service Content in a Connected Society, Ofcom's Third Review of Public Service Broadcasting, Section 2.46, page 21
[14] Ibid, page 145
[15] Methodology for determining the financial terms for the Channel 3 and Channel 5 licences, Statement, Ofcom, July 2013, Section 3.61

investment in new ideas, genuine plurality in commissioning, and access to a wider range of funding streams for original content.

12. It would also undermine their wider investment in the platforms and infrastructure that has helped build today's public service ecology. For example, the growth of the free-to-air DTT platform is not solely due to PSBs. Nearly half of the channels on Freeview are non PSB. These channels have invested in EPG positions, spectrum, marketing and infrastructure to help make the platform a success. The same can be said for those many channels on pay-TV platforms, which have helped drive innovation across the entire sector by pioneering different services such as 3D and mobile VoD, as well as providing increased choice for audiences.

13. Given the context of this consultation, we have outlined the value of non PSBs in terms of public service objectives, but it should also be borne in mind that non PSBs make a crucial economic contribution that may equally be undermined by any loss of revenues. The cable and satellite sector has, for example, doubled its direct employment in the UK over the last decade.[16] Multichannel broadcasters are also important investors in infrastructure and facilities. In 2012, QVC moved into a £33.6m, purpose-built facility in West London, from where it produces 17 hours of original television content per day and supports 2,000 UK jobs, in London and the North West.

14. This growth in employment, infrastructure and production skills has helped build the critical mass that the UK needs to sustain its position as a leading global television hub, acting as a self-reinforcing magnet for investment. Last year, the UK outpaced growth in global TV revenues and recorded the strongest increase in turnover out of any European market covered in Ofcom's international report.[17] The PSBs remain fundamental, but growth was driven by the multichannel sector.[18] Damaging this would be likely to have a profoundly negative impact on the UK's global competitveness.

[16] Skillset, Television Sector – Labour Market Intelligence Profile
[17] International Communications Market Report 2014, Ofcom, Figures 3.1 and 3.3
[18] Communications Market Report 2014, Ofcom, Figure 2.2

Introduction

1. The Commercial Broadcasters Association (COBA) is the industry body for multichannel broadcasters in the digital, cable and satellite television sector.

2. COBA members play a vital role in the success of the UK broadcasting sector, and the multichannel sector is arguably the fastest growing part of the UK television industry. They are increasing their investment in jobs, content and infrastructure:

   - Scale: In the last decade, the sector has increased its turnover by 30% to more than £5 billion a year. This is rapidly approaching half of the UK broadcasting sector's total annual turnover, and has helped establish the UK as a leading global television hub.[19] Last year, the UK outpaced growth in global TV revenues and recorded the strongest increase in turnover out of any European market.[20] Growth was driven by the multichannel sector.[21] The sector also contributes £4 billion per annum to the UK economy (GVA).[22]

   - Employment: As part of this growth, the multichannel sector has doubled direct employment over the last decade.[23]

   - UK production: In addition, the sector has increased investment in UK television production to a record £725m per annum, up nearly 50% on 2009 levels.[24] This was confirmed in Ofcom's 2014 review of public service broadcasting, which found that new commissions by the sector were up 43% since 1998 and were the only source of growth in investment in UK television production over this period.[25]

3. **For further information please contact Anna Missouri, COBA's Policy and Communications Executive, at anamaria@coba.org.uk or 0203 327 4054**

[19] Ofcom International Broadcasting Market Report 2013
[20] International Communications Market Report 2014, Ofcom, Figures 3.1 and 3.3
[21] Communications Market Report 2014, Ofcom, Figure 2.2
[22] Economic Impact Report, 2012, Oliver & Ohlbaum Associates for COBA
[23] Skillset, Television Sector – Labour Market Intelligence Profile
[24] COBA 2014 Census, Oliver & Ohlbaum Associates for COBA
[25] Public Service Content in a Connected Society, Ofcom's Third Review of Public Service Broadcasting, December 2014

Response to consultation questions

Question 1: Do you agree with our assessment of the context in which the PSB system operates, and how the trends identified might affect the PSB system? In particular, do you agree with our analysis of the independent production sector?

1.1 We agree with Ofcom's assessment that the PSB system remains "strong",[26] and expect this to continue to be the case for the foreseeable future. PSBs retain near universal reach and, with their portfolio services, account for 72.4% of television viewing.[27] Ofcom's research indicates that audiences remain extremely satisfied with PSB provision.[28]

1.2 This view is supported by Mediatique's analysis for Ofcom as part of the review, which states:

"Our view is that the conditions required to result in fundamental challenges to the sustainability of PSB genres are unlikely to materialise over the medium term."[29]

1.3 Looking ahead, on-demand consumption may be increasing, but linear viewing remains robust, at around 84% of all television consumption for audiences with a DVR.[30] Furthermore, PSBs are able to leverage their market position in the on-demand world. Online catch-up services outstrip viewing of all other on-demand services, accounting for 5% of viewing compared to 3%.[31] PSBs perform particularly well in this regard, using their strong position in the linear market to carve out market-leading positions in on-demand. Out of all on-demand services, the BBC iPlayer is the most used at 38%, followed by ITV Player on 22% and 4OD on 20%.[32]

1.4 We therefore believe PSB broadcasters remain in a strong, market-leading position across a range of platforms and means of delivery. We look at this in more detail in response to Question 3.

---

[26] Public Service Content in a Connected Society, Ofcom's Third Review of Public Service Broadcasting, Section 2.46, page 3
[27] PSB Annual Report 2014, Ofcom, Figure 3.13, page 31
[28] Ibid, Section 1.22.5, page 4
[29] PSB Review: Investment in TV genres, Mediatique for Ofcom, December 2014, page 75
[30] PSB Annual Report 2014, Ofcom, Section 2.46, page 21
[31] Communications Market Report 2014, Ofcom, page 10
[32] Ibid, page 145

1.5 In terms of investment in production, the 17.3% decline that Ofcom identifies has only translated into a 5% fall in overall first-run hours since 2008 (while first-run hours in peak have actually risen slightly).[33] Over the same period, audience satisfaction has increased, from 69% to 77%.[34] This suggests that the fall in investment has not led to a discernible impact in provision. We agree with Ofcom that there are a number of possible reasons for this, including third-party funding and increased efficiencies. We look at this in response to Question 6.

1.6 It should also be noted that investment by non PSBs has grown strongly since Ofcom's last PSB Review, and we welcome Ofcom's finding that "the only growth in primary commissions during this period was from non PSB channels".[35] COBA has consistently highlighted the growth in original commissioning from its members and how this makes an increasingly important contribution to the UK broadcasting ecology. Although we raise some points about the detail of Ofcom's figures, we broadly welcome Ofcom's findings, which overall are in line with COBA's 2014 Census. We examine this in more detail in response to Question 8.

1.7 On the question of the ownership of producers by multinational companies, we welcome the recent comments by the Secretary of State for Culture, Media & Sport on this point in his speech to the RTS, in which he said:

"In his MacTaggart lecture, David Abraham raised concerns about American companies investing in British production houses. But is that a bad thing?...For me, that's a massive vote of confidence in the work you do – work that has had an incredible impact on the UK economy."[36]

1.8 Multinational investment, both through ownership of UK producers and through commissions by multinational broadcasters from third-party UK producers, opens up opportunities for UK producers, providing them with access to overseas funding. This helps generate the producer deficit funding and/or distributor advances that Ofcom highlights on page 74 of the consultation paper. Downton Abbey, for example, is part financed by NBCUniversal, in exchange for international rights, through its ownership of the series' producer.

1.9 Many COBA members are uniquely placed to do this through their strong international presence, giving the UK producers that they commission or

33 Public Service Content in a Connected Society, Ofcom's Third Review of Public Service Broadcasting, Section 1.22.2, page 4
34 Ibid, Figure 20, page 44
35 Ibid, page 15
36 https://www.gov.uk/government/speeches/sajid-javids-speech-at-the-royal-television-society-conference

invest in a competitive advantage in raising production funding from international markets. A recent survey of COBA members commissioned from Communications Chambers found that 35% of UK commissions by COBA members involved an element of funding from their own international divisions.[37]

1.10 Crucially, as Ofcom notes, multinational ownership often creates a relationship to a UK broadcaster that means the producer does not qualify as an independent producer on a statutory basis. This means they are not entitled to the Terms of Trade and may not make programmes under the PSB quota for independent productions. Therefore concerns expressed around the applicability of the Terms of Trade to large, consolidated companies are premised on a false argument.

1.11 At the same time, as Ofcom points out in Section 2.37, the production supply sector remains competitive, with growth in commissioning from mid-tier companies in particular. Policymakers should question arguments that producers owned by multinationals somehow exercise power in the UK programme supply market due to the global scale of their parent companies. This is based on a misunderstanding of the supply market. Crucially, the commissioning broadcaster determines whether the commission goes ahead, and the domestic commission will typically determine whether a production will go ahead at all. The scale of a producer's owner on an international level is irrelevant to a producer's ability to win a UK commission.

1.12 Furthermore, the ownership of the producer does not determine the cultural specificity of the programme. The commissioning broadcaster will be closely involved in determining the nature of the programme – often down to signing off on production personnel.

1.13 Above all, there remains a high level of public intervention in the UK market, with the remit of the five main PSB channels overseen by the Government, Parliament and Ofcom in various ways. Ultimately, this means there is public oversight of channels with a market share of 72%, providing a range of checks and balances to ensure that content meets public service objectives.

1.14 It is therefore hard to see any negative impact from multinational ownership, while there are clearly positives.

Question 2: Have we identified the key differences in Northern Ireland, Scotland and Wales?

[37] Building A Global TV Hub, Communications Chambers for COBA, page 7

2.1 As far as we are aware, yes.

Question 3: Do you agree with our assessment that the PSB system remains strong overall?

3.1 Yes. PSB broadcasters remain in a very strong market position. The five main PSB channels accounted for 51.1% of all TV viewing last year.[38] While this has declined since 2008, this drop is more than offset by increases at their portfolio channels, yielding a total share of viewing of 72.4% - or nearly three quarters of all viewing.[39]

3.2 Similarly, the reach of the five main PSB channels remains strong, at 86.7% in 2013. While this was down fractionally, this decline was more than offset by increased reach for PSB portfolio services.[40]

3.3 Crucially, the success of the portfolio channels is driven by their relationship to a PSB service. COBA recently commissioned analysis of the value of the ITV PSB licence from Communications Chambers. The report, which we have provided separately to Ofcom, highlighted a range of ways in which the portfolio channels benefit from their relationship to a PSB, including:

- The ability of portfolio channels to cross promote.
- Flowing audiences from the main channel to the portfolio channels with, for example, The Xtra Factor on ITV2 immediately after The X Factor on ITV1.
- Awareness of the channels' programming when showing repeats from the main PSB service.

3.4 Communications Chambers' analysis indicates that the relationship with PSB channels has allowed the portfolio services to build share in a highly competitive market. While viewing share of PSB portfolio services in multichannel homes grew from 5% in 2001 to 21% in 2013, non PSB multichannel share dropped from 38% to 29%.[41]

3.5 Communications Chambers concludes:

"Each of the PSB groups has been able to launch portfolios that captured substantial share and continued to do so over a long period of time. This

[38] PSB Annual Report 2014, Ofcom, Section 3.40, page 30
[39] Ibid, Figure 3.13, page 31
[40] Ibid, Section 3.36, page 29
[41] The Costs and Benefits of the C3 Licences, Communications Chambers for COBA, December 2014, figure 7, page 16

supports the view that a 'champion' parent channel is highly important to the performance of the portfolio channels."[42]

3.6 This competitive advantage is also apparent in the on-demand market. On-demand catch-up services outstrip viewing of all other on-demand services, accounting for 5% of viewing compared to 3%.[43] Out of all on-demand services, the BBC iPlayer is the most used at 38%, followed by ITV Player on 22% and 4OD on 20%.[44]

3.7 In terms of investment in original commissions, the majority of the decline in PSB spending that Ofcom identifies is due to inflation.[45] Over the same period, hours of first-run content have dropped by a relatively small amount, while audience satisfaction remains high, suggesting that this real terms decline has made little impact on delivery. We will examine this in more detail in response to Question 6.

Question 4: Given the resources available, to what extent is the system meeting the needs of as wide a range of audiences as practicable?

4.1 We believe the PSB system is meeting the needs of a wide range of audiences. According to Ofcom's audience research, most of the satisfaction ratings for PSB purposes and characteristics increased between 2008 and 2013.[46] Overall viewer satisfaction increased significantly during this period, from 69% to 77%.[47]

4.2 There may well be a need to improve certain areas, notably the representation of cultural and ethnically diverse groups, people with disabilities and women. In many ways these are challenges for the television industry as a whole. However, we would highlight significant steps taken by some PSBs and non PSB broadcasters to improve many of these areas over the last 12 months, with Sky, Channel 4 and the BBC unveiling new strategies for improving B&ME diversity. We also note that access services are widely available on PSB and non PSB channels.

---

42 The Costs and Benefits of the C3 Licences, Communications Chambers for COBA, December 2014, page 17
43 Communications Market Report 2014, Ofcom, page 10
44 Ibid, page 145
45 Public Service Content in a Connected Society, Ofcom's Third Review of Public Service Broadcasting, Section 2.46, page 73
46 Ibid, Section 3.51, page 44
47 Ibid, Figure 20, page 44

Question 5: Given the resources available, does the PSB system deliver the right balance of spend and output on programming specifically for audiences in Wales, Scotland and Northern Ireland and programmes reflecting those nations to a UK-wide audience?

5.1 Yes. The BBC and Channel 4 are in the process of increasing the amount of programming they commission from the devolved Nations and English regions, and Ofcom's audience research for this consultation found "a marked increase" in satisfaction with the portrayal of the nations and regions.[48]

Question 6: Is declining investment affecting the quality of PSB and is it a cause for concern?

6.1 No, our belief is that declining investment has not led to a corresponding fall in quality or volume. According to Ofcom, while spending by PSBs has fallen by 17.3%, first-run hours dropped by only 5%, and rose in peak.[49] This indicates a number of factors may be offsetting declining investment by PSBs. Firstly, investment from third parties has helped bridge any gap. This is in part a by-product of the introduction of the Terms of Trade in the 2003 Communications Act– as PSB broadcasters no longer retain all IP rights when commissioning content, they have been less willing to meet the entire cost of the production, leaving the producer to bridge the gap by selling those IP rights, typically overseas.

6.2 It is worth noting that such third-party funding is particularly prevalent in drama, one of the most exportable of genres and one where producers regularly sell IP rights overseas. Furthermore, drama has benefited from the recently introduced tax relief for high-end television production. Figures released by the BFI this month show that more than 80 television productions, with a total spend of more than £600m, used the tax break last year. This included many PSB drama commissions, such as the BBC's Wolf Hall and Poldark, and ITV's Cilla, Grantchester, Foyle's War and Downton Abbey.

6.3 In addition, the majority of the 17% decline in PSB spending is due to inflation.[50] It is not clear whether costs in the production sector have risen with inflation. Certainly, there have been some efficiencies, notably the drop in producer margins highlighted by Ofcom in this paper.

---

[48] Public Service Content in a Connected Society, Ofcom's Third Review of Public Service Broadcasting, page 46
[49] Ibid, Section 2.46, page 73
[50] Ibid, page 73

6.4 Further allaying concerns, a substantial part of this real terms drop in investment by PSBs is due to the BBC's flat-rate licence fee settlement, rather than any underlying market issues.

6.5 We also note that declines in most genres appear to have stabilised or reversed recently. PSB spending in each of the children's, factual, drama, entertainment, arts and religion genres was flat or up slightly year-on-year in 2013.[51] Spend on first-run films rose strongly over the period.

6.6 Only news, education and sports showed year-on-year declines in 2013 in terms of PSB spend. However, PSBs' total hours of UK news rose slightly, while hours of education were flat.[52] The drop in sport in 2013 may well have been down to the previous year's World Cup.

6.7 Even if PSBs have moved to potentially cheaper entertainment and comedy genres, evidence suggests that viewers had no objection to this, with audience satisfaction rising significantly over the period, as we have outlined in response to Question 4.

6.8 Finally, it is important to bear in mind that non PSBs have substantially increased their investment in original content over this period. Much of this content is of high quality and meets public service objectives, as we detail in response to Question 8.

Question 7: Do you agree with Ofcom's provisional findings in the Review of C4C's delivery of its media content duties?

7.1 We are concerned that Ofcom has identified a "relative lack of ambition"[53] on the part of Channel 4 in meeting its statutory duty to provide content for older children. This obligation has been in place since the Digital Economy Act. Channel 4 should be held to account on this duty, and we support Ofcom's suggestion that Channel 4 disaggregate figures for older children in order to provide transparency, as well as publish a strategy for future investment.

Question 8: To what extent do you agree with our assessment of the degree to which the non-PSB services play a role in helping to deliver the public service objectives? In doing so please set out your views on the

---

51 Public Service Content in a Connected Society, Ofcom's Third Review of Public Service Broadcasting, Figure 25, page 49

52 Ibid, Figures 28 and 29

53 Public Service Content in a Connected Society, Ofcom's Third Review of Public Service Broadcasting, section 3.187, page 70

delivery by the PSB portfolio channels, other non-PSB channels, on-demand and internet services and also radio services separately.

8.1 Overall, we welcome Ofcom's assessment of the contribution to public service objectives made by non PSBs as a significant - indeed, potentially ground-breaking - step forward in understanding the different factors driving growth in the UK broadcasting sector.

8.2 We agree with Ofcom's conclusion that the UK benefits from "a strong mixed ecology"[54], fuelled by growth in investment from non PSBs and a PSB system that remains strong. This echoes recent comments by the Secretary of State for Culture, Media & Sport in his speech to the RTS, in which he said:

"[I]n recent years we have moved from a market driven solely by public service broadcasting to a more mixed, more global ecology."[55]

<u>Level of investment from non PSBs</u>

8.3 We broadly welcome Ofcom's analysis of UK commissioning by non PSBs. COBA has consistently argued that multichannel investment is growing substantially. Ofcom's figures indicating that non PSB investment in first-run originations has increased by 43% since 2008 are broadly in line with data collected in our last Census of the sector.[56] We also agree that total spending by the multichannel sector – excluding sports – now represents around 15% of all investment in first-run originations. However, we believe this is the case even excluding PSBs' portfolio channels, as Ofcom's sample understandably does not capture all non PSB investors, as we will explain. Including sports production, we estimate the non PSB sector accounts for around 20% of all spend on first-run originations, again excluding PSBs' portfolio channels.

8.4 Ofcom's analysis confirms an overwhelming body of work indicating that the non PSB multichannel sector is substantially increasing its investment in content. Analysis by Oliver & Ohlbaum Associates (O&O) for Ofcom for this consultation finds that there has been a modest growth in overall investment in originations since 2009, driven by a substantial increase in multichannel spending on first-run originations of 11.4% CAGR (by far the highest level of growth from any investor). O&O concludes that:

[54] Public Service Content in a Connected Society, Ofcom's Third Review of Public Service Broadcasting, Section 1.6, page 1
[55] https://www.gov.uk/government/speeches/sajid-javids-speech-at-the-royal-television-society-conference
[56] COBA 2014 Census: Multichannel Investment in TV Production, O&O for COBA, June 2014

"[G]rowth has been on the back of increased multichannel spend on UK content rather than PSB spend, although PSBs remain the main spenders."[57]

8.5 This is further supported by O&O's work for COBA's 2014 and 2012 Censuses, which reached similar conclusions[58], and also by O&O's work for producers' body Pact, which found that multichannel (non PSB) commissions from external suppliers were worth £381m in 2013, more than double the equivalent 2008 figure of £158m.[59] This represents more than 22% of all commissions of independent producers and has been vital to the growth of the independent production sector, with increased investment from non PSBs more than compensating for declining spend from PSBs since the last PSB review: without multichannel investment, primary commissions from the independent production sector would have fallen slightly since 2009, instead of growing by £200m.

8.6 As part of this, multichannel broadcasters are spending a significant proportion of their investment on commissions from medium and smaller independent producers, helping ensure plurality in the supply sector. Non PSBs spent 53% of their commissions on medium-sized suppliers (£25m-£70m annual turnover) in 2013, which was a higher proportion than any PSB, and 22% on smaller producers (under £25m annual turnover), comparable to or higher than the PSBs.[60]

8.7 We would, however, like to raise a number of points related to the methodology and presentation of Ofcom's data that we believe are important in elucidating the policy discussions that will flow from this review.

<u>Sports production investment</u>

8.8 In the wider context of the broadcasting sector as a whole, investment in sports, including rights payments, makes a major contribution to supporting infrastructure and jobs. In terms of PSB, we believe investment in sports production is an important factor in understanding developments in the sector. Investment in sports production benefits in-house and external producers, nurtures talent and skills, supports production infrastructure such as studio facilities and post production houses, and helps build critical mass. In addition, sports channels make a valuable public service contribution by offering access to many niche sports. Sky, for example, shows a wide range of women's sports, including women's cricket, rugby, athletics and squash, as

[57] The Evolution of the TV Content Production Sector, page 13, O&O for Ofcom, Sept 2014
[58] COBA 2014 Census: Multichannel Investment in TV Production, O&O for COBA, June 2014
[59] Independent Production Sector Financial Census and Survey, O&O for Pact, July 2014, page 14
[60] Ibid

well as such disability sports as wheelchair rugby, wheelchair basketball, and hand-cycling, amongst others.

8.9 We understand that sports production has been excluded by Ofcom due to a lack of disaggregated data, rather than any policy rationale. We accept this but ask Ofcom to make it absolutely clear that there is a public service (and economic) value in sports investment, and that investment in this genre is over and above the figure of £345m for non PSB production spend. This is important for future policy discussions, which will be informed by this review, as it goes to an understanding of the actual levels of investment in UK production. It is particularly relevant in terms of any consideration of transferring revenues from non PSBs to PSBs, as sports represents a larger proportion of overall spending for non PSBs than for PSBs. We also ask Ofcom to make this latter point clear in order to help remove uncertainty and the use of inaccurate figures in future policy discussions.

8.10 On a related point, in Figure 3 of the consultation paper, Ofcom says that it has excluded sports rights investment for non PSBs but not for PSBs. We are not sure that this is actually the case, but are concerned if it is. Spending should be measured on a like-for-like basis and we ask Ofcom to clarify why it has taken a different approach to PSBs and non PSBs, if this is the case.

<u>Sample size</u>

8.11 For understandable reasons, i.e. not wishing to place disproportionate reporting burdens on channels with smaller audience shares, Ofcom data for non PSB investment excludes several significant investors in UK content. We estimate that this investment is comparable to the amount spent by commercial PSBs' portfolio channels on originations, and certainly several tens of millions. We ask Ofcom to acknowledge there is additional investment from non PSBs outside its sample.

<u>The global context</u>

8.12 Historically, Ofcom's research has understandably focused on collecting data from the UK-licensed channel business. However, in an increasingly global market, this approach may exclude legitimate investment in UK commissions that comes from different parts of a multinational business (but which may still be licensed by Ofcom on a non-domestic basis and subject to conditions imposed by Ofcom regulations). We believe there are three additional forms of legitimate investment in UK content that Ofcom might consider going forward:

- Firstly, many multinational businesses will part fund UK commissions using revenues from overseas channels. In many cases these channels may be licensed by Ofcom on a non-domestic basis, and therefore impacted by any changes to UK regulations. A recent survey by Communications Chambers found that 35% of UK commissions by COBA members involved an element of funding from their international channels.[61]

- Secondly, some multinational broadcasters operate separate silos of investment for European commissions. This may not be counted as part of the UK-licensed business, but any investment made in a local commission will be done on the expectation of making a return in that market (and overseas).
- Thirdly, multinational broadcasters may occasionally premier UK commissions on their overseas channels (this is often a sign of that show's expected success). We understand that this is excluded.

8.13 We ask Ofcom to consider making these points clear in its eventual statement for this review, again to help inform subsequent policy discussions.

Delivering public service objectives

8.14 We welcome Ofcom's conclusion that non PSBs meet certain public service objectives. The simplest indication of this are shows such as Sky's The South Bank Show and Disney's Art Attack, previously commissioned by PSBs but now have a new home as original first-run commissions on non PSBs.

8.15 COBA members are strong providers of original content in certain genres that have experienced declines in PSB investment. For example, COBA members including Sky, CNN and CNBC invest nearly £90m a year in UK-made news, and have increased this investment by 2.8% per annum since 2011.[62] Similarly, multichannel broadcasters are investing in children's content, factual, comedy, drama and the arts. This is not just a matter of providing investment, it is also creating high quality content: for example, Sky News and CNN International have between them won the RTS News Channel of the Year for the last three years running, beating off competition from the BBC. Sky News' longstanding and significant commitment to high quality news in the UK is well known, and it has won the RTS News Channel of the Year award for a record nine times. Perhaps less understood is that CNN employs 200 people in the UK working directly on its news output, and that its London operation is responsible for 20 hours of live programming every week.

8.16 That non PSBs are making an important contribution to public service goals is, in our view, supported by the findings of Ofcom's audience research. This

[61] Building A Global TV Hub, Communications Chambers for COBA, page 7

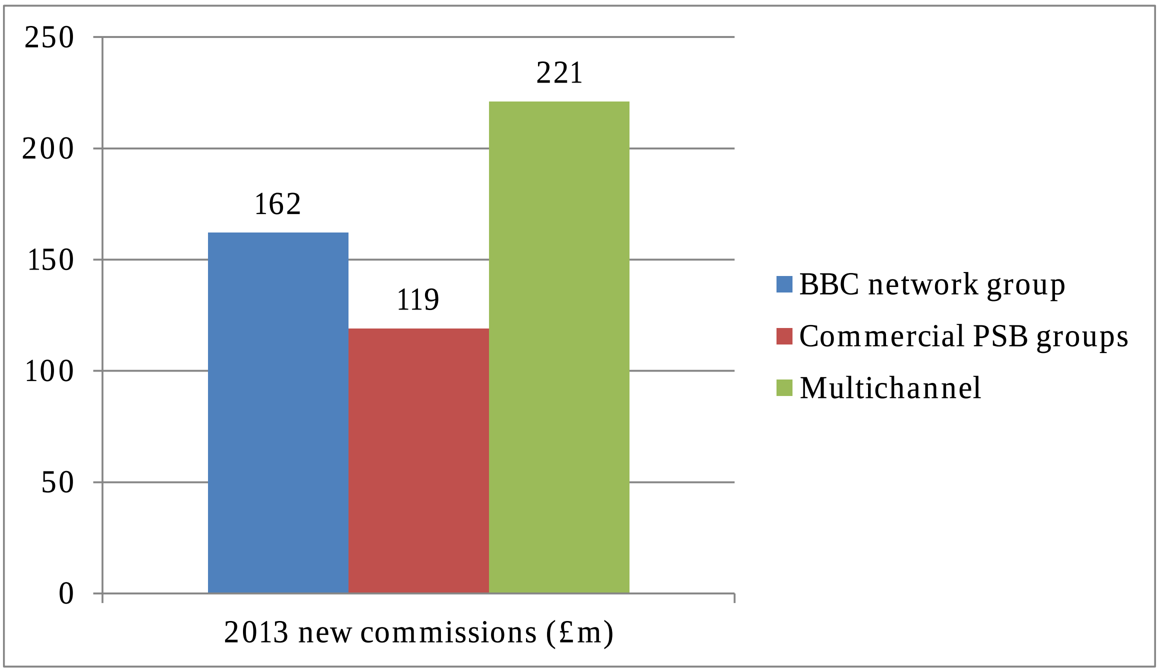
[62] COBA 2014 Census: Multichannel Investment in TV Production, Oliver & Ohlbaum Associates for COBA, page 19

concluded that audiences believe that, beyond PSBs, "a wide range of organisations are producing content delivering PSB purposes and characteristics."[63]

8.17 This investment from non PSBs creates a number of benefits for the public service ecology, which we outline below:

8.18 New ideas: The UK is renowned worldwide for its creativity, for producing fresh and distinctive content, but this depends on a healthy flow of new ideas reaching the screen. Non PSBs play a perhaps surprisingly important role in this. According to Pact, they now invest more than the BBC on new commissions from independent producers (as opposed to re-commissions of existing shows, or "returning series"), and more than the commercial PSBs combined. According to Pact's latest census, in 2013 the multichannel sector spent 58% (£221m) of its total investment in independent originations on new commissions. In comparison, the BBC spent 34% (£162m), while Channel 4 spent 21% (£84m). Channel 5 spent 15% (£6m) and ITV 8% (£29m), as the chart below highlights.[64]

Investment in new UK commissions from independent producers (£m), 2013



Source: O&O/Pact Financial Census (adjusted data)

[63] Public Service Content in a Connected Society, Ofcom's Third Review of Public Service Broadcasting, Section 2.52, page 24

[64] Independent Production Sector Financial Census and Survey, O&O for Pact, July 2014, page 16

8.19 As non PSBs increase their original commissioning, the proportion of their spend going on new ideas might be expected to go down. However, they have in fact reduced their relative spending on returning series, from 47% in 2009 to 43% in 2013. During the same period, all PSBs have increased the proportion they spend on returning series, in most cases to a significant extent. COBA's assumption is that non PSBs have had a long established core of returning series, but have expanded into new areas as their budgets for original commissioning have grown.

8.20 Creative Competition: Along with sustaining levels of investment in original production, the non PSB sector provides strong creative competition for PSBs. For example, the BBC launched a 24 hour news channel following the introduction of Sky News, and more recently has raised its game in its coverage of football in response to Sky. It has also announced a major boost for its arts coverage following the launch of Sky Arts.

8.21 Innovation: Pay TV services offering premium content are arguably the most incentivised of all broadcasters to drive innovation in order to attract audiences. Non PSBs have been at the forefront of innovation, launching mobile on-demand services, HD channels and 3D services. For example, in 2013, NBCUniversal's Syfy was the first UK broadcaster to launch a channel-wide second screen app, while Sky has recorded more than half a million subscribers for its 3D service. This has helped encourage innovation across the sector, for the benefit of audiences.

8.22 Infrastructure: Non PSBs have invested substantial sums in developing their businesses, paying for EPG positions, spectrum, infrastructure and marketing, in turn increasing the UK's competitive intensity and helping drive the growth of free-to-air and pay-TV platforms. In so doing, they have ensured that UK audiences benefit from a genuine choice of services available across a range of platforms. In the context of this consultation, it is worth highlighting that this includes significant investment in making the free-to-air DTT platform a success. Freeview audiences now have access to around 85 channels, with nearly half of these being non PSB even when the portfolio channels of the PSBs are excluded. Some of these non PSB services are founder broadcasters on the platform, while many have contributed to the platform's subsequent growth.

The USP of non PSBs

8.23 We have already covered some of the ways in which non PSBs meet public service objectives. In addition, non PSBs meet these objective in ways that PSBs do not, or that PSBs deliver only to a limited degree. In this way, non

PSBs make a potentially irreplaceable contribution to the overall public service system which would be likely to be lost in a transfer of revenues from non PSB to PSBs. These include:

8.24 Diversity of revenue streams: Non PSBs diversify and strengthen revenue streams for original production in ways that free-to-air PSBs cannot. Along with advertising, many non PSBs generate revenues through pay-TV. This makes the UK broadcasting sector less reliant on any one revenue stream and more resilient during cyclical advertising downturns or a flat licence fee settlement. During the last advertising downturn, between 2009 and 2011, multichannel commissions from independent producers remained stable, while commercial PSB investment dropped significantly.[65]

8.25 Access to global revenues: Many non PSBs are uniquely placed through their strong multinational presence to provide UK producers with a competitive advantage in accessing investment from global markets. As we have previously noted, around 35% of UK commissions from COBA members involve an element of funding from their international channels.[66] In addition, in comparison to PSBs, multichannel broadcasters often commission programmes in longer runs, which are more suitable for exporting. This global context is likely to be increasingly important going forward: with exports of content one of the fastest growing sources of income for the UK television sector, the UK's ability to exploit international markets will be key to unlocking future growth.

8.26 Increased choice: The 500+ UK-licensed multichannel services greatly increase range and choice for audiences. While PSBs tend to seek mass audiences, many multichannel broadcasters offer specialist or niche content that serves audiences with particular interests, providing a level of choice that PSBs cannot. For example, multichannel audiences often skew towards specific demographic groups, such as gender or age, or, as Ofcom highlights in the consultation paper, cultural or religious background.

8.27 Plurality in commissioning: The many non PSB channels investing in original content offer a genuine range of commissioners for UK producers that goes far beyond what the four PSB groups could provide on their own. They provide opportunities in a wide range of genres, cater to specialist audiences, and many have commissioning strategies that are clearly distinct to those of PSBs. For example, as we have mentioned, many commission series in longer runs that are more suitable to overseas markets, facilitating the export of UK content.

[65] Independent Production Sector Financial Census and Survey 2014, Oliver & Ohlbaum Associates for Pact, page 14
[66] Building A Global TV Hub, Communications Chambers for COBA, page 7

8.28 Our contention, therefore, is that non PSBs support and enhance the public service system in numerous ways that go beyond what PSBs could, or are likely to, offer on their own. As we have outlined, non PSB broadcasters ensure there is a flow of new programme ideas reaching screens, a greater range of choice for audiences, a plurality of commissioners for producers, a stronger revenue base for funding UK content, and greatly improve access to global markets, amongst other contributions. Were there a transfer of revenues from non PSBs to PSBs, as is mooted in the consultation paper, many of these additional benefits would be lost or greatly diminished.

8.29 Ofcom raises the point that many non PSB services are available only via pay-TV, and that this therefore limits their contribution to public service objectives. Firstly, it is important to bear in mind that nearly half of the channels on the free-to-air platform are non PSB (indeed, well over half if the PSBs' portfolio channels are included). These channels have made an important contribution to the platform's success, as we have outlined above. Just as importantly, though, the limits of the non PSB sector in delivering public service objectives should not be allowed to mask the unique – possibly irreplaceable - ways in which they strengthen and enhance public service broadcasting for the benefit of the entire ecology, and of course audiences.

8.30 We also caution against easy assumptions that PSB investment in UK content is guaranteed, while that of non PSB services is not. There is every indication that, given the continuation of a reasonable legislative and regulatory framework, COBA members' investment will continue to grow. The UK has strong underlying factors that make investing in domestic content attractive: a strong production sector, a high level of skills, a large domestic market, the English language and, more recently, the introduction of tax reliefs for television production. Sky has recently publically committed to maintaining its strategy of investing in original content,[67] while further investment in UK content is coming from a diverse range of players in a wide variety of genres.

8.31 Conversely, PSB investment has declined, in real terms at least. Despite statutory commitments and the concerns of Ofcom, ITV1 has exited UK children's programming and was recently fulfilling 40% of its Out of London hours with just one show, a late night listings service.[68] Five's arrangement with the Secretary of State to maintain a children's strand has, to our knowledge, no oversight by Ofcom, and it is unclear how this will be enforced. Ofcom recently stated in its Section 229 report to the Secretary of State that the repeated revisions that have been made to the commercial PSB licences

---

[67] http://www.theguardian.com/media/2015/feb/04/sky-vows-to-ramp-up-spending-on-original-british-content
[68] http://stakeholders.ofcom.org.uk/binaries/broadcast/tv-ops/c3_c5_licensing.pdf

are not "in the public interest",[69] but we are unaware of any legislative means to stop this occurring again during the next licence period.

Question 9: How likely are we to see steady evolution and have we identified all of the potential alternative scenarios and risks to the system?

9.1 Independent research commissioned by COBA from Communications Chambers indicates that the commercial PSB licences remain eminently viable for the foreseeable future. The Communications Chambers report suggests that ITV receives a benefit of up to £295m a year from its licence, before mitigation, and up to £161m after mitigation. Factoring in costs, this translates into a net benefit of £87m.[70]

9.2 The key point here is that regulators and policy makers are dealing with a hypothetical scenario, i.e. what would be the impact were ITV to lose its licence? Communications Chambers' conclusion differs to independent analysis for Ofcom in that they believe that over time there would be <u>some</u> loss of viewing amongst even the most loyal viewers, were ITV to lose its position on the first page of the EPG (which in itself is a very realistic scenario on Sky and Virgin). We accept that Ofcom must err on the side of caution in assessing the value of the licence, but equally we believe that it is just as likely that ITV receives a substantial net benefit from its PSB licence, as it is that there is no surplus. This is borne out by ITV's regular renewal of the licence.

9.3 On a related point, Mediatique's report for Ofcom for this review concludes that drama still remains commercially sustainable on a standalone basis for ITV, and is likely to remain so despite high levels of time-shifted viewing and ad-skipping.[71]

9.4 More broadly, we agree that the most likely scenario in the market is a continued gradual evolution. Spending on traditional television spot advertising remains sound, growing by 4% in 2013 in nominal terms, as Ofcom notes.[72] We also think Ofcom's estimate that around 80% of viewing will be to live, linear broadcasting in 2020 is realistic.[73]

---

[69] http://stakeholders.ofcom.org.uk/binaries/broadcast/tv-ops/c3_c5_licensing.pdf

[70] The costs and benefits of the C3 licences, Communications Chambers for COBA, December 2014

[71] PSB Review: Investment in TV genres, Mediatique for Ofcom, December 2014

[72] Public Service Content in a Connected Society, Ofcom's Third Review of Public Service Broadcasting, section 5.15, page 98

[73] Ibid, section 5.7, page 97

Question 10: How might incentives to invest change over time?

10.1 Mediatique's analysis for Ofcom for this review indicates that there are only limited incentives on PSBs (other than statutory obligations) to invest in the least commercial types of public service content.[74] We are not convinced there is any gap in the provision of public service content, but the Mediatique analysis suggests to us that the only way to ensure increased delivery by PSBs in these less commercial genres is through specific genre quotas.

Question 11: Have we identified all the relevant ways in which the PSB system might be maintained and strengthened?

11.1 Ofcom recently acknowledged the value to PSBs' portfolio channels from their relationship to their main PSB channel, and committed to factor this into the value of the commercial PSB licences. As Ofcom stated:

> "We recognise that a cross promotional benefit may arise from operating multiple channels, a benefit that may be realisable whether or not a PSB licence is held. However, in the case of a PSB licence holder, the cross promotional benefit could be enhanced by virtue of the 'appropriate' EPG prominence accorded to the PSB channel. Any such enhancement will be reflected in our valuation of the right to appropriate EPG prominence."[75]

11.2 We ask Ofcom to clarify whether the cross promotional benefit that it is already factoring in encompasses PSBs' on-demand services as well as their linear portfolio channels, and if not to include these as well. Just as there has clearly been considerable value for the linear portfolio channels in their relationship to a PSB channel, so PSBs' on-demand services are performing strongly, fuelled in large part by similar cross-promotional benefits from their PSB parent. According to Ofcom's research, the BBC iPlayer is the most popular UK VoD service, followed by ITV Player on 22% and 4OD, with Demand Five coming after Netflix.[76]

11.3 Including the value to on-demand services will help ensure that the real value of the PSB licence is realized on behalf of the public. Ofcom should factor in the benefit to on-demand services and either reflect this in the price paid for the licence, or increase PSB duties accordingly.

11.4 In support of this, we note the findings of independent research commissioned by COBA from Communications Chambers on the value of the

[74] PSB Review: Investment in TV genres, Mediatique for Ofcom, December 2014, page 57
[75] Methodology for determining the financial terms for the Channel 3 and Channel 5 licences, Statement, Ofcom, July 2013, Section 3.61
[76] Communications Market Report 2014, Ofcom, page 145

ITV licence. The Communications Chambers report suggests that ITV receives a benefit of up to £295m a year from its licence, before mitigation, and up to £161m after mitigation. Factoring in the costs, this translates into a net benefit of £87m after mitigation.[77] As we have mentioned, we accept that Ofcom must err on the side of caution in assessing the value of the licence, but equally we believe that it is just as likely that ITV receives a substantial net benefit from its PSB licence, as it is that there is no surplus.

11.5 More broadly, in terms of its market analysis in this PSB Review, Ofcom has in many ways taken a forward thinking and welcome approach in its consideration of developments. As Ofcom acknowledges, the wider market beyond the PSB sector is increasing its investment in UK production to a significant degree.

11.6 It is of concern, however, that this insightful approach to analysis of the market is not reflected in the subsequent policy discussion in Ofcom's consultation document. We are deeply concerned that the consultation gives little consideration to the possible negative impact on the wider market of Ofcom's proposals for strengthening PSB.

11.7 Certain proposals may well have such a negative impact. In so doing, they would risk undermining revenues for the non PSB sector and dampening incentives for channels to invest in content. This is a crucial point for policy makers. The trade-off here is, at best, a relatively constrained boost in revenues for PSBs (that they may or may not use to increase their investment in PSB content), compared to potentially damaging what Ofcom has confirmed is the only source of growth in UK commissions, i.e. non PSBs. As such, the potential negative impact on non PSBs would apply not just to current investment, but the long-term incentives for non PSBs. This creates a risk of slowing the rate of growth in commissioning from non PSBs, with a potentially further reaching impact on overall investment over time.

11.8 In addition, while this consultation is of course concerned with public service objectives, it must be acknowledged in any assessment of market impact that a negative impact on PSBs will not only be likely to damage their ability to meet public service objectives such as investing in content, but also their significant contribution to the wider broadcasting economy. The non PSB sector has been a key driver of growth in the UK broadcasting sector as a whole over the last decade. Cable and satellite sector broadcasters have doubled their direct employment in the UK over the last decade, according to Skillset.[78] In addition to jobs, multichannel broadcasters are investing heavily in broadcasting infrastructure and facilities. To offer one example, in 2012, QVC

[77] The costs and benefits of the C3 licences, Communications Chambers for COBA, December 2014
[78] Skillset, Television Sector – Labour Market Intelligence Profile

moved into a £33.6m, purpose-built facility in West London, from where it produces 17 hours of original television content per day and supports 2,000 UK jobs, in London and in its distribution and call centre near Liverpool.

11.9 This ambitious – and risk-taking - investment is occurring across the multichannel sector, driving growth in the UK broadcasting sector. Last year, according to Ofcom's international market report, the UK outpaced growth in global TV revenues and recorded the strongest increase in turnover out of any European market.[79] PSB broadcasters remain fundamental, but growth was driven by non PSBs.[80]

11.10 This growth is creating a virtuous circle, building the critical mass that the UK needs to attract more investment from domestic and multinational players. Damaging this virtuous circle of investment risks undermining the UK's global competitiveness.

Question 12: Does universal availability and the easy discoverability of PSB remain important and how might it be secured in future?

12.1 We see no pressing need to extend PSB prominence and availability rules into the on-demand world. Despite the absence of any statutory requirement, PSBs' on-demand services are widely and prominently available on key on-demand platforms (and where those PSB on-demand services are not available, this may be due to PSBs withholding their content into order to drive audiences to their own platforms). Partly as a result, audiences are not, in our view, experiencing any problems finding PSBs' catch-up services. Out of all on-demand services, the PSBs are for the most part the most used, with the BBC iPlayer used by 38% of people surveyed, followed by ITV Player on 22% and 4OD on 20%, with Demand Five coming after Netflix.[81]

12.2 In our view, PSBs' on-demand services have de facto prominence and availability benefits from the strength of their main PSB channels. Just as these have fuelled the growth of their portfolio channels – through cross promotion, brand awareness, and flowing audiences from the parent PSB channel – so they have provided their on-demand services with a significant advantage in attracting audiences and in securing their presence on on-demand platforms. This is quite apart from PSBs having ownership of on-demand platforms themselves.

---

[79] International Communications Market Report 2014, Ofcom, Figures 3.1 and 3.3

[80] Communications Market Report 2014, Ofcom, Figure 2.2

[81] Ibid, page 145

12.3 Furthermore, the greater majority of PSB viewing remains to linear channels. We do not believe that permitting the fulfilment of PSB duties through other services such as on-demand would necessarily be in the interests of the public if this led to that PSB content being unavailable on linear services. The "digital divide" is a crucial factor in this debate: it is not appropriate to confer PSB status to services that are not available to all members of the public due to either the cost or the availability of superfast broadband.

12.4 In addition, policymakers should consider the possible impact on innovation and incentives to invest in new on-demand services. We question whether it is proportionate or desirable that emergent platforms should be required to provide the same content prominently that is available on larger or more established ones.

12.5 This is quite apart from questions over the practicability of defining platforms and enforcing these rules, particularly when some may not be based in the UK.

12.6 We therefore see no need to strengthen current arrangements. Ofcom says in its consultation paper that radical extension of prominence rules to all devices "appears to be somewhat disproportionate, as PSB is currently widely available in unregulated spaces." The same rationale should be applied to Option 2 (incremental change): before any intervention in this area, it should be established that there is a problem in the take up of PSB on-demand services. Instead, we believe Ofcom should examine the benefit to PSBs' on-demand services from their relationship to a PSB channel and factor this into its valuation of the PSB licence, as we have mentioned previously.

Question 13: Should we explore the possibility of giving greater flexibility to PSB institutions in how they deliver public service content, including examining the scope (in some or all cases) for regulating by institution, not by channel?

13.1 We are deeply concerned about the potential negative impact on the market of introducing PSB benefits, such as EPG prominence, for the PSBs' portfolio linear channels. This could have profound consequences for the rest of the market, potentially making it impossible to compete with the four PSB groups.

13.2 The PSBs' portfolio channels are already in a very strong market position, in large part due to their relationship to a PSB channel. Based on Ofcom's figures, they have in recent years demonstrated exceptional growth, growing from 10.2% market share in 2008 to 15.8% in 2013. This has nearly entirely offset declines at the main PSB channels, and means that PSBs have a market share of 72.5% in all homes once their portfolio channels are included[82] - or nearly three quarters of the market.

13.3 Ofcom recently recognised that this growth is already fuelled by their corporate relationship to the main PSB channel, stating:

"We recognise that a cross promotional benefit may arise from operating multiple channels, a benefit that may be realisable whether or not a PSB licence is held. However, in the case of a PSB licence holder, the cross promotional benefit could be enhanced by virtue of the 'appropriate' EPG prominence accorded to the PSB channel."[83]

13.4 Communications Chambers' recent report for COBA on the value of the PSB licence for ITV looked at this relationship in some detail. The report noted a number of benefits including: cross promotion, both explicitly (e.g. trails) and implicitly (the parent brand); the ability to flow audiences from the PSB channel to the portfolio channel with themed content (e.g. The Xtra Factor on ITV2 immediately following ITV1's The X Factor); and raised awareness of repeats on the portfolio channel following their broadcast on the PSB channel.

13.5 Communications Chambers concluded that this has clearly helped drive growth for the portfolio channels. Since 2001, Communications Chambers found that PSB portfolio channels had increased viewing share in multichannel homes from 5% to 21%. Over the same period, other non PSB multichannel services had lost share, falling from 38% to 28%. Communications Chambers stated:

"The importance of a strong parent is evident in the performance of various portfolios. Competition in the multichannel environment is primarily between portfolios. However, likely because of the strength of their parent channels, the PSB portfolio channels have enjoyed substantial growth at the expense of other multichannels."[84]

13.6 We believe it is therefore clear that the PSB relationship has already conferred significant advantages on the PSB portfolio services, enabling them to build market share. Granting them further benefits, such as prominence, could potentially have a hugely significant impact on the rest of the market, giving the PSBs and their portfolio services a dominance that would stifle growth in investment and potentially lead to a substantial contraction amongst their competitors. This could have potentially disastrous consequences not just for

[82] Public Service Content in a Connected Society, Ofcom's Third Review of Public Service Broadcasting, Section 2.52, page 24, section 4.12, page 80
[83] Methodology for determining the financial terms for the Channel 3 and Channel 5 licences, Statement, Ofcom, July 2013, Section 3.61
[84] The Costs and Benefits of the C3 Licences, Communications Chambers for COBA, December 2014, page 16

non PSBs' revenues and investment in UK content, but also their crucial role in driving wider economic growth in the broadcasting sector.

13.7 Furthermore, were PSBs allowed to fulfil certain duties in a different way, then any additional benefit to their main PSB service would have to be reflected in the valuation of their PSB licence. We do not support doing so, but were Ofcom to further explore extending PSB status to other channels, we would expect this to be subject to a full public consultation, including the specific objectives and market impact.

Question 14: Do the current interventions in relation to the independent production sector need to change in light of industry developments?

14.1 We have addressed this point in response to Question 1, but in summary we see no reason to change existing intervention. Crucially, as Ofcom notes, multinational ownership often creates a relationship to a UK broadcaster that means the producer does not qualify as an independent producer on a statutory basis. This means they are not entitled to the Terms of Trade and may not make programmes under the PSB quota for independent productions. Therefore concerns expressed around the applicability of the Terms of Trade to large, consolidated companies are premised on a false argument.

14.2 At the same time, as Ofcom points out in Section 2.37, the production supply sector remains competitive, with growth in commissioning from mid-tier companies in particular.

14.3 In addition, policymakers should question arguments that producers owned by multinationals somehow exercise power in the UK programme supply market due to the global scale of their parent companies. This is based on a misunderstanding of the supply market. The UK commission, and the platform it provides for reaching domestic audiences, is usually vital to the production happening in the first place. The scale of a producer's owner on an international level is irrelevant to a producer's ability to win a UK commission.

14.4 In addition, it is crucial to bear in mind that the commissioning broadcaster determines whether the commission goes ahead and will be closely involved in determining the nature of the programme – often down to signing off on production personnel. The ownership of the producer therefore does not determine the cultural specificity of the programme.

14.5 Above all, there remains a high level of public intervention in the UK market, with the remits of the PSB channels overseen by the Government, Parliament and Ofcom in various ways. Ultimately, this means there is public oversight of channels with a market share of 72%, providing a range of checks and balances to ensure that content meets public service objectives.

Question 15: Have we identified the right options when considering potential new sources of funding, are there other sources of funding which should be considered, and which are most preferable?

Changing rules for TV advertising volume and scheduling

15.1 Ofcom concluded an extensive review of this issue in December 2011. Having weighed up consumer, competition and public service broadcasting issues, the regulator found no basis on which to proceed with any changes to the current regime. Ofcom stated:

"We believe that the interests of consumers are delivered effectively through the rules as currently set out. We have not found or been presented with evidence that suggests a change to the existing rules would necessarily better deliver against these interests and the overall goals of regulation in this area."[85]

15.2 COBA welcomed this conclusion. We previously commissioned independent analysis from Oliver & Ohlbaum Associates that indicated that the harmonisation proposals could reduce advertising revenues for non PSBs by around £80m per year – revenues which support broadcasters' commissioning strategies and which have a direct relation to levels of investment in UK content. We are happy to supply a copy of this analysis on request.

15.3 It should be noted that the current arrangements partly reflect the dominant position of the PSB broadcasters in the advertising sector, where the three commercial PSB channels control 60% of advertising income. The mass reach of commercial PSBs via their privileged access to spectrum and guaranteed carriage remains an attractive selling point and such broadcasters are able to command a premium that reflects their market power.

15.4 This dominance was confirmed in the Competition Commission's 2010 investigation into ITV's Contracts Rights Renewal (CRR) undertakings, which concluded that ITV1 continues to have a dominant position and stated that:

"We found that, as in 2003, ITV1 continues to have unique features which limit its substitutability...Media buyers continued to believe that ITV1 was able to offer unique benefits in terms of the size of its audiences and the 'quality' of

[85] http://stakeholders.ofcom.org.uk/broadcasting/broadcast-codes/advert-code/ad-minutage

its impacts. We found that, as in 2003, difficulties remain in switching advertising expenditure away from ITV1."[86]

15.5 It is also important to bear in mind that minutage restrictions are a clear opportunity cost that PSBs accept when taking a PSB licence, which of course provides them with a range of advantages such as spectrum, EPG prominence and the ability to cross promote to portfolio channels. These advantages reinforce their dominant market position.

15.6 Furthermore, COBA members licensed in the UK are already subject to an average of nine minutes of advertising per hour, which is a stricter regime than in some other European markets.

15.7 We believe that events since Ofcom's decision mean there is even less of a case for changing the advertising minutes regime than there was at the time. The commercial PSBs have performed well, with ITV posting record profits and Five moving into profit. In addition, since 2011, non PSBs have significantly increased their investment in UK content, as Ofcom has highlighted in the consultation paper. Reducing the advertising revenues for non PSBs would risk damaging their investment in content.

Relaxing wider TV advertising rules

15.8 COBA supports further consideration of this providing any resulting benefits do not unduly favour PSBs over non PSBs. Indeed, any changes should ensure all investors are incentivised.

New tax breaks

15.9 We welcome the introduction of the new tax reliefs for high end television, children's and animation, which are already attracting investment in UK production. The BFI recently reported that drama production worth £615m made use of the tax reliefs for high-end television last year, the first full year of the relief. While the new television animation tax relief came into effect relatively recently, it has already supported 22 animation productions in the UK production, worth £36.8 million. Many of these are original commissions by the PSB broadcasters, as well as non PSBs.[87]

Exempting PSBs from future AIP charges

15.10 As we have previously outlined, any exemption for DTT should not be discriminatory and favour PSBs. Nearly half of the channels of the DTT

---

[86] Competition Commission, Review of ITV's Contracts Rights Renewal Undertakings, Final Report, May 2010

[87] http://www.bfi.org.uk/news-opinion/news-bfi/announcements/new-bfi-stats-show-record-year-uk-film-2014

platform are non PSB, not including PSB's portfolio channels, and their investment has contributed to the platform's success.

<u>Introduce contestable funding</u>

15.11 We are not convinced of the merits of making the licence fee contestable. Of course our members would be likely to consider using such funding to augment their investment in content were it available. However, were funding available for programming that met with non PSBs' content strategies – which is by no means a given - we would expect conditions attached to it, such as additional reporting to Ofcom, the BBC Trust, the Government and Parliament, to reduce its attractiveness. We would also be highly concerned that, in creating a precedent, funding would potentially become contestable for areas other than content creation, damaging the commissioning budgets for which COBA members with production interests compete.

<u>Transfer funds from one part of the industry into the PSB system</u>

15.12 As we have argued in response to Question 11, damaging the non PSB sector in order to support the PSB system would have a number of consequences, including:

- Undermining the only source of growth in original commissions.
- Risk of losing often unique, potentially irreplaceable benefits from non PSB investment, including a high level of investment in new ideas, access to additional sources of funding for content such as pay-TV and global markets, and plurality in commissioning.
- Damaging non PSBs' investment in the wider economy, such as jobs.

15.13 This is quite apart from the lack of any guarantee – without further intervention - about whether PSBs would use any additional funds to invest in areas of PSB content that are supposedly underserved, or even whether they would re-invest them in production at all.

15.14 In terms of the question of the balance of payments between platforms and PSBs, this is a potentially major change in intervention, with possibly highly disruptive and negative effects for non PSB broadcasters, platforms and of course audiences. Indeed, even PSBs may be impacted negatively: according to Mediatique's 2012 report for the DCMS, a commercial negotiation might lead to payments worth £110m a year being made by PSBs to platforms.[88]

[88] Carriage of TV Channels in the UK: policy options and implications, Mediatique for DCMS, July 2012, page 7

15.15 Based on Ofcom's analysis of the PSB system for this consultation, we are not convinced that there is a problem in the delivery of PSB, and certainly not one of sufficient scale that justifies such uncertainty and disruption.

15.16 Furthermore, it is difficult to see how any alternative solution could improve on the current system, or how a genuine commercial negotiation could be allowed without putting at risk the principle of universal availability. Sky already has an effective "must carry" duty in being required to be an open platform that cannot refuse to make available any service under FRND terms, on top of the requirement that it gives the PSBs prominence on its Electronic Programme Guide. Coupled with PSBs' obligations to make their channels available as part of their PSB licences, this ensures universal availability (and accessibility) of PSB content for the public.

15.17 In our view, this creates a balanced relationship where both parties benefit: PSBs receive a number of advantages, including valuable premium EPG positions and significantly increased advertising revenues as a result of their larger audiences. Platforms also benefit of course, but they incur costs in several ways. There is a substantial opportunity cost in being unable to sell those EPG positions to the wider market or use them for their own channels: as the bidding for ownership of Channel 5 indicated last year, there is considerable appetite amongst non PSBs for ambitious development of their businesses, and we would expect any available slots to be keenly contested. In addition, platforms have invested significant amounts in marketing, infrastructure and technology to develop their businesses (in turn creating more value in the EPG positions which they are required to surrender).

15.18 With both sides benefiting, and the UK PSB system, and indeed the entire UK broadcasting ecology, performing well, we see no reason to alter the balance in regulations in this area. We agree that a more granular approach that potentially led to the Government or Ofcom setting prices would be likely to be unworkable in practice (and in our view undesirable in principle).

15.19 Were platforms required, either directly or indirectly, through regulation, to pay PSBs more than they would reasonably be expected to in a commercial negotiation, this could have a number of serious negative consequences. Firstly, platforms may well pass on some or all of additional costs to audiences, effectively making them pay twice for PSB content.

15.20 Secondly, Ofcom notes that any proposed changes would need to consider the effect on "competition between PSBs and other non-PSB broadcasters."[89] We believe this is potentially significant. COBA members compete on a daily basis

[89] Public Service Content in a Connected Society, Ofcom's Third Review of Public Service Broadcasting, Section 2.52, page 24, section 6.77.3, page 122

for audiences and revenues, and fully embrace fair competition as a prerequisite for a healthy market. Competition between channels and platforms has underpinned growth, incentivising investment from domestic and global players in content, jobs and infrastructure and helping create the "mixed ecology" that Ofcom refers to in the consultation paper. As one CEO responded in a 2012 survey for COBA on the key factors incentivising investment in the current UK market:

"There is meaningful competition between platforms and willingness to pay market rates for the rights to distribute the best content."[90]

15.21 There is, in our view, a significant risk of dampening competition by imposing rules that force platforms to make undue payments to PSBs. Were platforms required to pay significant sums to PSBs, they may well seek to recoup at least some of any additional costs by reducing their content budgets elsewhere, including the fees they pay for third-party channels. As Ofcom is aware, subscription revenues are hugely important not just for the platforms, but also for the channels carried on them in return for a fee. Indeed, the growth of those revenues over the last decade has been nothing less than crucial in enabling many non PSBs to increase their investment in original production, as well as in establishing the UK as a leading global television hub.

15.22 Furthermore, we are not clear why any payments should be restricted to pay-TV platforms and not equally applied to those where PSBs have a commercial interest, i.e. Freeview and Freesat. This surely increases the risk of market distortion.

15.23 We also remain unclear as to how any additional revenues for PSBs would be guaranteed to be channelled into areas that are underserved – or even whether there are any areas that need additional funding. In our view, specific genre quotas would probably be necessary to ensure investment is appropriately targeted.

15.24 Finally, on the comparison with the US model, there are a number of fundamental differences to the UK market that make this analysis somewhat desultory. Firstly, US networks are offered on an exclusive basis to local cable operators, increasing their value. Secondly, a key argument behind the benefit of retransmission fees in the US is that without these fees, the margins of broadcast TV stations would be 3.1% as opposed to 14.8%. However, ITV's

[90] Building A Global TV Hub, CEO and senior multichannel executive survey, Communications Chambers for COBA, page 10

broadcast margin is 25.7% without retransmission fees and on a group-wide basis it is 26.0%.[91] This suggests it does not need further support.

[91] http://www.berenberg.de/cgi-bin/content/content.cgi?rm=show_doc&session_id=f7b990124ce7ccff76aaf9b6fd0a18ed&sb_userid=31265138&sb_eventid=90477