



BRITISH BOLD CREATIVE

The BBC's submission to the Department for Culture,
Media and Sport's Charter Review public consultation.

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Contents

I Introduction

2 Executive Summary

- 2.1 An open BBC
 - 2.2 A world-class media sector
 - 2.3 Purpose and Remit
 - 2.4 Scale and Scope
 - 2.5 Funding
 - 2.6 Efficiency and Value for Money
 - 2.5 Independence
 - 2.8 Governance and Regulation
-

3 Answers to Consultation Questions

- 3.1 How can the BBC's public purposes be improved so there is more clarity about what the BBC should achieve?
- 3.2 Which elements of universality are most important for the BBC?
- 3.3 Should Charter Review formally establish a set of values for the BBC?
- 3.4 Is the expansion of the BBC's services justified in the context of the increased choice for audiences? Is the BBC crowding out commercial competition and, if so, is this justified?
- 3.5 Where does the evidence suggest that the BBC has a positive or negative wider impact on the market?
- 3.6 What role should the BBC have in influencing the future technological landscape including in future radio switchover?
- 3.7 How well is the BBC serving its national and international audiences?
- 3.8 Does the BBC have the right genre mix across its services?
- 3.9 Is the BBC's content sufficiently high quality and distinctive from that of other broadcasters? What reforms could improve it?
- 3.10 How should the system of content production be improved through the reform of quotas or more radical options?
- 3.11 How should we pay for the BBC and how should the licence fee be modernised?
- 3.12 Should the level of funding for certain services or programmes be protected? Should some funding be made available to other providers to deliver public service content?
- 3.13 Has the BBC been doing enough to deliver value for money? How could it go further?
- 3.14 How should the BBC's commercial operations, including BBC Worldwide, be reformed?
- 3.15 How should the current model of governance and regulation for the BBC be reformed?
- 3.16 How should Public Value Tests and service licences be reformed and who should have the responsibility for making these decisions?
- 3.17 How could the BBC improve engagement with licence fee payers and industry, including through research, transparency and complaints handling?
- 3.18 How should the relationship between Parliament, Government, Ofcom, the National Audit Office and the BBC work? What accountability structure and expectations, including financial transparency and spending controls, should apply?
- 3.19 Should the existing approach of a 10-year Royal Charter and Framework Agreement continue?

I INTRODUCTION

This document is the third in a series setting out the BBC's position for Charter Review. It responds to each of the nineteen questions raised in the Government's consultation paper.

It should be read alongside the BBC's proposals for programmes and services in the next Charter, 'British, Bold, Creative' that was published on 7 September 2015 (referred to here as the BBC Strategy Paper), and the paper on the BBC Studios proposal, published on 17 September. These provide an evidence base for answering some of the questions raised by the Government's consultation paper. This document cross-refers to that evidence rather than repeating it wholesale. It draws on a wide range of other evidence and analysis, some of which we have published as annexes alongside this document. They are:

- A report by PwC on the impact of a change in the BBC's licence fee revenue;
- A report by Frontier Economics on the BBC's contribution to the UK Creative Industries;
- A report by Mediatique on value for money;
- A summary of the BBC's latest audience research.

2 EXECUTIVE SUMMARY

Charter Review is an important opportunity to set the future direction of the BBC. Having agreed the BBC's funding framework for the next Charter period, we look forward to the debate. The Government's consultation paper raises important questions about the mission, scale and scope, funding, and governance of the BBC.

Our response shows that the BBC is working well today and helping to grow the UK's creative industries, but will need to modernise to preserve public service broadcasting. To that end, we are putting forward a radical programme of reform to create an open BBC that:

- Becomes Britain's creative partner and a platform for this country's incredible talent and the work done by its great public institutions;
 - Transforms our services to be internet-fit, while maintaining much-loved linear services;
 - Leads digital innovation with new investments such as the Ideas Service and iPlay for children, and widening choice for audiences by making our services more distinctive;
 - Increases competition from two thirds of our cost base to around 80%;
 - Saves close to 20% of our costs or an average savings target of around 3.5% a year over the next five years, having already saved over 40% of our cost base in this Charter period;
 - Is a leaner, simpler organisation and gets our overheads to less than 7%, inside the top 25% of private regulated companies, having already got to less than 8% this year;
 - Grows cumulative commercial returns to around £1.2 billion over the next five years, with BBC Worldwide maintained as an integral part of the BBC;
- and
- Removes key guarantees and quotas for BBC programmes, but setting up BBC Studios to maintain the BBC as one of the best programme-makers in the world.

At the same time, where things demonstrably work, we will argue for continuity and only for changes that strengthen, not weaken, the current model. Stability starts with the BBC's funding settlement. The Budget agreement should deliver a sustainable income for the long-term though it will not be without its challenges and difficult choices. We will not be seeking to re-open the Budget agreement. Our proposals to modernise the BBC depend on this funding envelope. The funding agreement means the BBC will continue to shrink in financial terms—but that will not stop us delivering a better, more open BBC.

Delivering the funding agreement also means not fragmenting the licence fee through new top-slicing or contestable funding. This policy would risk substituting public money for private, and it would be allocated by committees rather than commissioners. It would be subject to lobbying rather than audiences, and it would weaken accountability for public money and erode the BBC's independence. We welcome the Government's commitment to end the broadband ring-fence. We would regard any new proposal for top-slicing, or a reduction in our ability to make commercial returns to supplement licence fee income, as reopening the funding agreement.

Our strategy for an open BBC needs to be underpinned by a policy framework that supports the BBC's creativity, innovation and independence. The answers in this document are our suggestions for how that framework should evolve in the next Charter. We look forward to discussing them with Government, audiences and stakeholders, and working towards a White Paper that will make the BBC stronger in 2025.

It is hard to think of a country in better creative shape than the UK. The success of our media ecology has made our culture and our democracy stronger. The creative industries are also one of the most productive parts of the UK economy in terms of growth, jobs and exports. The UK has always had the best of both worlds—a thriving domestic sector and significant inward investment. There are not many industries where the UK goes toe-to-toe with the US—but the creative industries still do. British values and British identity have a special place in the world—and the BBC, alongside others in our creative industries, has a vital role in building the UK’s global brand and influence.

Britain’s competitive position has not come about by accident. We have created a media system in this country that works—it has been achieved through the careful regulation of broadcasting, combining the investment of the licence fee, the public service content of the commercial PSBs and the complementary spending of a large number of multi-channel services on pay-TV. Public funding—now at only around a fifth of total TV revenues—has supported rather than crowded out a vibrant UK media sector.

Britain can have a media ecology in the next decade that is even better than it is today. The Government’s consultation paper raises many detailed questions about the BBC, which we respond to in this document. The test that matters most is whether the outcome of Charter Review is a strong, open and

independent BBC in ten years’ time that serves audiences even better and is a creative powerhouse for the UK at home and abroad. A BBC that can play a unique, vital role in securing the conditions for future success, namely:

- A high level of investment in a wide range of high quality programmes and new digital content—home-grown for British audiences and exploited around the world;
- Programmes and services that make Britain a better place—by connecting audiences with their cultures and heritage, and enabling an informed conversation across the country;
- A growing and diverse production sector with strong skills and talent base across the UK, exporting even more than today;
- The widespread availability of public service content and prominence across platforms and devices to secure its cultural and democratic impact; and
- Thriving competition between networks and between free-to-view and pay platforms, with low barriers to entry for innovative services and low switching costs for consumers.

The internet and globalisation present huge opportunities for the UK media sector—if it continues to be a pioneer. This country has some of the best programme-makers in the world, and the internet gives us new ways to get our services to audiences, and the scope for new partnerships. We have the tools to deliver public service objectives in new ways and to serve audiences better than ever before. However, there are also risks to the reach and impact of PSB and so its benefits to the media sector, too. Ofcom's latest review of PSB has identified a number of them, including:

- The long-term decline in the amount of UK-originated content. From 2008 to 2013, investment in first-run, original television content in the UK fell in real terms from £2.6bn to £2.4bn. Over the same period, investment in original British programmes by our PSBs fell by around 15%¹. As the BBC's spending has fallen, overall investment in original British content has gone down. We welcome increased investment by Sky and other multi-channel providers. However, the market has not made up the gap and it is very unlikely to deliver the range and volume of British programmes on a universal basis that we as a society want;

- Audiences of all ages continue to value PSB. Yet younger and older people's consumption habits are increasingly different. More and more, younger people are watching less television than older people, and listening to much less radio. Where young audiences go now, older audiences will follow. If this trend continues, by the 2020s, a significant minority of the audience would no longer get the content they want from PSB, nor be a part of the shared conversation it supports. It is, therefore, essential that we preserve PSB by modernising it for the internet age;
- and
- It may become harder to ensure that the public can continue to access public service broadcasters. We would ask policy-makers to modernise the regulatory framework to ensure public service broadcasting is easy to find on future as well as existing platforms.

With an open, strong, and independent BBC alongside vibrant market institutions, Britain's share of the global market can grow, while audiences will get better programmes, for less, than under any other system.

¹ Investment in original television content figures exclude sport and are in 2013 prices.

The debate about the BBC should start with what it is for. The justification for the BBC does not rest on a model of 'market failure'. The case for the BBC starts from a different set of considerations about the sort of society we want. Access to culture, media and information should be a basic human right, ensured regardless of a person's ability to pay for it. The BBC has an intrinsic mission: to provide programmes and services that people love and enjoy, and which inform, educate and entertain them as individuals. It also has an instrumental purpose: to deliver external benefits to society through, for example, creating a richer culture, promoting democratic debate and building a stronger sense of community through shared experiences. The 'public purposes', set out in the Charter and Agreement, capture this wide-ranging role that retains widespread public support.

Universality is not about reaching all audiences *per se* but about reaching all audiences with high quality and relevant public services. As the benefits are significant it is justifiable that they should be available to all. In addition, there is a public interest in broad access, as the public value of the BBC's services increases with widespread consumption, for example as a result of the 'network' benefits of BBC news content in informing democratic participation.

The BBC also makes UK broadcasting and the wider creative sector stronger. The BBC's remit means it discovers and invests in the best British creative content and people, and connects them with audiences at home and abroad. We are the largest

single investor in British creative ideas and talent. The licence fee accounts for around 20% of TV revenues—but around 40% of the investment in original British programmes. Each year, we invest well over £2 billion of licence fee income directly into the UK creative sector. Around half that money is invested outside of the BBC, with £450 million in small creative businesses.

We agree with the Government's consultation paper that the media landscape has been transformed since the last Charter Review. But we do not accept that this explosion of choice means that the rationale for the BBC has diminished, or that a vibrant market is a reason to constrain the BBC. The case for the BBC, with a remit to inform, educate and entertain, is as powerful as ever. The BBC performs a unique, distinct function in our media ecology—great British content, a trusted guide, for everyone. The public continues to value trusted and impartial news and see the BBC as the best source of this, as shown by evidence in the audience research annex. The public's support for the BBC has risen over this Charter period. Far from crowding out commercial investment, the evidence shows the market is as strong as it is partly because of the BBC. Furthermore, there is no reason to believe that the market would fill the investment or universality gap left by the BBC. The evidence of the last five years shows the opposite.

If the size and market impact of the BBC was the focus of the last Charter Review in 2006, we believe the challenge this time should be how to secure the relevance and impact of the BBC at a time of rapid change.

The BBC has become much smaller relative to most parts of the market. Our share of broadcast revenues has fallen from c.40% to c.25% today. In online, the BBC accounts for 3% of the total time spent by UK audiences. In the past five years, our funding has fallen in real terms as the market has grown. Despite this, our share of TV and radio audiences has stayed broadly flat and we continue to reach 99% of UK households every week. This success is a function of audience satisfaction and trust not market power.

We have diversified our portfolio and innovated with new services like iPlayer to ensure we continue to provide something of value to everyone. The BBC is providing much more, for less. In the next Charter, we will again modernise what we do and how we do it to give audiences the public service broadcasting they say they want. The public is willing to pay for the BBC, they value the quality of our services and would not support any fundamental reductions in the scope or purposes of the BBC.

The Government's consultation is right to insist that the BBC should be distinctive. We propose a simple test: that every BBC service should be clearly distinguishable from its commercial competitors. But distinctiveness does not equal 'market failure' or stepping back from popular content. The BBC's services should be distinctive, not distinct. The BBC makes good popular programmes—if we withdrew, audiences would have less choice. The value of—and public support for—the BBC comes from the range and depth of its content. We achieve universality with distinctive services, and that universality is valuable because of the quality of those services.

We need to be able to commission the best programmes from wherever they come—from inside the BBC and outside. To maximise competition, the BBC must remain one of the world's great programme-makers. Owning intellectual property is more important to creative and economic success than ever before. It ensures that the commercial returns we generate are re-invested into services for licence fee payers. The BBC's current supply model is not fit for purpose, however. We have proposed a package of pro-competitive reforms—to create BBC Studios and, at the same time, remove the current in-house guarantee. BBC Studios will have the values and quality of the BBC—a mission to inspire audiences at home and around the world with bold British creativity. It will be a significant, distinctive presence in the supply market. But, with around a 15% share initially, it will not be dominant.

Every public service is being asked to deliver more for less, so the BBC needs to have a commercial strategy that delivers as much as possible back into public service programmes. The BBC has built a world-class and growing media business, BBC Worldwide, that showcases British creativity across the globe. As set out in the BBC Strategy Paper, we intend to work with global partners to grow Worldwide further, taking advantage of the demand for British programming and new digital opportunities. BBC Worldwide is an indivisible part of the BBC and so any proposal to carve out BBC Worldwide would not make economic sense.

2.5

Funding

As the BBC has a universal mission it is necessary and appropriate that it should be universally funded and made available to all. The licence fee is the best way to fund the BBC and the only mechanism that can maintain a universal, independent and accountable BBC, investing in British creativity and delivering high quality, distinctive programming at an affordable price. While no form of taxation is universally popular, long-term polling shows that public backing for the licence fee has grown over this Charter period. Support is higher now at close to 50% than it was in 2004 when 31% backed the licence fee, and higher than it was 25 years ago.

But whereas the principle of the licence fee remains right, it needs to be modernised to reflect changing technologies and audience behaviour, as proposed in the Budget agreement. We can see merit in the Government's option for medium-term reform of the licence fee by universally levying it on all households, as happens in Germany.

Subscription funding by contrast, either alone or as a partial substitute for the licence fee, is the wrong model for the BBC in principle and in practice. It would harm UK content investment and quality, restrict access for audiences, particularly the poorest, and increase the cost they pay—ultimately damaging the UK's media ecology which is based on competition for quality but not funding. Perhaps this is why public support for a subscription-funded BBC has been falling over the past 10 years and is now the least popular option.

The BBC is not a monopoly supplier of public service broadcasting. It operates in a market with intense levels of competition. On the input side, two-thirds of what the BBC spends is contested already, and we will increase this to 80% by opening up our TV, radio and online schedules to greater competition. The BBC has embraced contestability but through a model that works to improve quality and value for money—because spending decisions are made creatively by those who are close to the audience and held directly accountable for performance.

2.6

Efficiency and Value for Money

Over the past 20 years, the BBC has transformed its efficiency and productivity, delivering more services for less, and is now at least as efficient as comparable organisations. By the end of this Charter, we will have saved £1.6 billion in cumulative annual savings, over 40% of the BBC's addressable cost base. Under the funding agreement, we will need to make a total saving

of £700m a year by 2021/22. This represents close to 20% of our expected 2016/17 spend, or an average annual savings target of around 3.5% a year over the next five years. Our reform programme to create a leaner, simpler organisation and to introduce greater competition will help deliver this.

2.5 Independence

Charter Review is the opportunity to consider and debate the future of the BBC and determine its purposes, remit, scope and governance. Beyond this periodic process, the BBC must be as independent as possible from the political process. This is strongly supported by the public.

The last two funding settlements show that the BBC is vulnerable to being drawn into wider Government spending and policy decisions, rather than our funding being determined on its merits after consultation with audiences and the industry. The Charter model itself has many strengths but the process effectively allows for the Government of the day to make significant decisions unilaterally.

Charter Review presents an opportunity to consider how decisions about the BBC's role and funding are taken and consider changes to make the processes more public. There is a strong case for taking such decisions out of the electoral cycle in future. It is also critical that the voice of licence fee payers is formally heard in debates about the role as well as the funding of the BBC.

This Charter Review should deliver a much more reliable framework for assuring the BBC's independence. We look forward to considering the proposals that emerge in the debate, but believe that overall we now need to formalise parts of the framework that have relied on custom and practice, and introduce checks and balances so Charter Review decisions cannot be taken unilaterally.

2.8 Governance and Regulation

The BBC welcomes the Government's decision to establish the independent review into how the BBC is governed and regulated. The BBC will input to this process. This submission sets out initial thinking on reform of the BBC's current governance and regulation model, and the principles that should guide it. The new arrangements should be clear, flexible, proportionate, transparent, easy to understand and enable effective decision-making in response to a fast-changing environment. The new arrangements should fulfil the following core principles:

- Protect the BBC's independence;
- Uphold the interests of licence fee payers;
- Enable the BBC to remain distinctive and relevant in a fast-moving world;

- Take market impact considerations properly into account;
- Ensure the BBC operates in the public interest, with effective routes for redress when it does not; and
- Ensure a clear separation between corporate governance and regulation.

We support the creation of a new unitary Board, fully independent of Government. The corollary of a unitary BBC Board with its own non-executive Chairman is the move to external regulation of the BBC.

It is important that this Charter Review looks ahead to the challenges and opportunities of 2025 rather than just considering those of 2015. In summary, we believe that the following policy measures are necessary to secure a strong, open and independent BBC in the next decade:

- The flexibility to modernise the BBC's services to be internet-fit and take advantage of delivering public service objectives in new ways;
- The BBC to remain a producer-broadcaster with a secure, sustainable and affordable source of intellectual property across all genres;
- A commercial strategy, with BBC Worldwide as an integral part of the BBC, that delivers sustainable returns to licence fee payers and showcases British creativity across the globe;
- A new unitary Board to run the BBC with flexible, proportionate and targeted external regulation;
- A new 11 year Charter with the requirement for licence fee payers to be consulted on its future role and funding, with reliable safeguards for the BBC's independence;
- Continue with the approach agreed with the Government in removing the broadband ring-fence, by not introducing any further elements of top-slicing or contestable funding;
and
- Avoid changes to the public purposes or scope of the BBC that undermine universality and its ability to serve everyone with public service content.

3 ANSWERS TO CONSULTATION QUESTIONS

3.1 How can the BBC's public purposes be improved so there is more clarity about what the BBC should achieve?

3.1.1 We should retain the public purposes but make them clearer and more relevant

The debate about the BBC should start with what it is for. The BBC has a long-standing mission: to provide programmes that inform, educate and entertain people as individuals. It also has an instrumental purpose: to deliver external benefits to society through, for example, creating a richer culture, promoting democratic debate and building a stronger sense of community through shared experiences. The existing six 'public purposes', set out in the Charter and Agreement, delineate this wide-ranging public role that retains widespread support. The 'purpose remit' set out the priorities that the BBC should meet and how performance against them will be assessed.

As we explain at section 3.16 of this document, the BBC's Charter and Agreement should contain a clear and precise definition of the BBC's public service remit and the activities covered by it, including an articulation of the public purposes. The purposes should be retained in broadly their existing form, but there is a good case for making them clearer and more relevant. The BBC belongs to the public and so it is right that people should know what to expect from it. They also provide a useful framework for the BBC Executive to determine its strategy.

The BBC Trust has done some detailed work looking at public opinion about the purposes which shows that the public recognise and value the existing purposes but that there is scope to make them more meaningful.

Subject to further audience testing and discussion about exact wording, we agree with the revisions the BBC Trust has proposed to the first four public purposes². But we would like to see two purposes in addition to these:

- First, an updated version of the current digital purpose linked explicitly to the BBC's services. The BBC plays a critical role in delivering the benefits of new communications technologies to all licence fee payers through its new services and in the

form of its initiatives like Make it Digital on coding (we discuss this more at section 3.6). This purpose should not be used as a justification for top-slicing the licence fee for non-BBC activity as we argue in section 3.12

- Second, a new purpose that recognises the BBC's important and unique role in supporting the creative industries (see section 3.5). As with digital, this purpose should be a function of the BBC's public mission. In promoting its other purposes, the BBC should operate and spend the licence fee in ways that support the creative industries. This purpose should aim to capture the principal channels through which the BBC supports the growth of the creative sector. This could be combined with the BBC's existing global purpose, as proposed by the BBC Trust.

The way the public purposes are written should allow the BBC's performance to be assessed not only in terms of inputs and public perception but, wherever possible, actual social, educational, cultural and economic impacts. They should not be too detailed or prescriptive so that they can last the lifetime of the Charter and do not constrain inappropriately the BBC's ability to react to the changing needs of licence fee payers and evolving market and social conditions. The Charter and Agreement already includes measures to ensure that significant changes to BBC content and services are properly assessed (as we discuss at 3.16). If during this Charter the purposes had referenced genres of programming or 'set clear boundaries for what is or isn't appropriate output from the BBC' as the Government's consultation paper suggests, the BBC may not have been free to invest more in drama and the arts in recent years, or to launch the iPlayer. Moreover, such restrictions would be a significant encroachment on the creative independence of the BBC. Instead, the BBC should make those decisions within a purpose-based framework set down in the Charter and Agreement and overseen by an external regulator.

2 BBC Trust, 'Initial Response to the Government's Green Paper', July 2015. The BBC Trust suggests these public purposes: 1. Providing news and information to help people understand the world around them; 2. Supporting learning and education; 3. Showing the most creative ideas and the highest quality content; 4. Reflecting and representing the whole UK population; 5. Growing the creative industries and promoting the UK abroad.

3.1.2 Partnerships are an important means to deliver the purposes

We welcome the intention behind the suggestion in the Government's consultation paper that 'the BBC could have more specific responsibilities for partnership working'. A BBC that is truly open to partnership is a major theme of the BBC Strategy Paper. We want to open the BBC to be Britain's creative partner, to become a platform and a catalyst for this country's incredible talent. We intend to put our technology and digital capabilities at the service of our partners and the wider industry to deliver the best to licence fee payers. To achieve this, we recognise we have to become a better partner working in a more genuinely collaborative way with like-minded institutions, with suppliers, individuals and competitors.

However, that ambition to thread partnership through what we do can be achieved without a new specific purpose. Instead, the Charter and Agreement should articulate clearly that partnership will be a critical means by which the BBC should deliver each of the public purposes in future.

To realise the full benefits of partnership, it will be necessary to revise the rules in the Charter and Agreement³ which restrict how resources other than the licence fee can be used in a BBC service and enable greater flexibility and editorial judgement in working with partners. We discuss this at section 3.17.

³ Clause 75 of the BBC Agreement (Alternative Finance)

3.2 Which elements of universality are most important for the BBC?

3.2.1 Universality is not about reaching all audiences *per se* but about reaching all audiences with high quality and relevant public service content

The BBC's public mission is universal—it is to inform, educate and entertain everyone, no matter who they are, no matter where they live. This mission justifies how the BBC is funded to ensure widespread access free at the point of use.

It is important to establish the proper priority of arguments. We do not want or need to reach all audiences as an end in itself, we want and need to reach all audiences with high quality and relevant public service content that informs, educates and entertains. That is how we fulfil our mission. The public value of the BBC is created when audiences engage with its content and services. A service with no audience is as ineffective as output with no public service value.

The point of the BBC striving to reach all audiences—including audiences that are more difficult to reach—is *not* so that we can hold up a reach figure which justifies a universal fee but rather so that we can deliver content which is valuable to them as individuals and has wider social benefits.

The test for output aimed at the young, at ethnic minorities, or at mainstream audiences is not one of marginal competitive success or of crude hours of consumption to justify the expense of the licence fee. It is the same as should apply to any service: how effective and efficient is this output at putting high quality public service content in front of the audience?

This ambition to reach everyone with valuable content is wholeheartedly supported by the public, nearly 80%⁴ of whom think that the BBC should provide something for every household.

There are therefore three tests of universality that the BBC must pass, in order to achieve its public service mission:

- 1 Making distinctive, high-quality programmes;
- 2 Making available that content on widely-used devices and platforms;
- 3 Reaching all audiences.

⁴ ICM Unlimited for the BBC Trust, 2,111 UK adults (online), Nov–Dec 2014. 77% think it is important that the BBC provides something for every household. Available at http://downloads.bbc.co.uk/bbctrust/assets/files/pdf/news/2015/audience_research.pdf

3.2.2 Our aim is to make a broad range of distinctive content that can inform, educate and entertain broad audiences

The BBC has a duty to serve everyone, but not with just anything.

Universality needs to be achieved through the sustained quality of our programmes, within a uniquely broad range of genres. We have improved the focus and the delivery of that mission over decades as we show in section 2 of the BBC Strategy Paper.

For instance, we have improved the quality and distinctiveness of BBC One, ensuring it takes more risks and offers a broader range than its commercially funded competitors.

The BBC displays this ambition throughout its services. Consider our commitment to music and music-making of every kind. We approach that commitment through a number of radio stations that share a public service ethos. They bring passionate and knowledgeable curation and context, new talent, live performance, points in the schedule where listeners are encouraged to confront music and artists they have never heard before, and so on. That mission unites, for instance, Radio 1 and Radio 3, despite their different audiences and music focus. Across the range of our music radio services we reach around three-quarters⁵ of the British public with that mission across a quarter.

In a similar way, the 80% of the British public that consume news from the BBC every week do so on a variety of platforms, through a wide range of services and from many different programmes.⁶

At times, we have to look at where there are gaps such as underserved audiences (e.g. BAME groups) and make sure our services adapt to remain relevant to these audiences. *Newsbeat*, for instance, reaches more young people each week than the *10 O'Clock News*.⁷ Both *IXtra* and the Asian Network are targeted services that allow us to reach under-served audiences.

Universality also allows us to bring people together for important national moments—whether they are predictably popular (a Royal Wedding) or brilliant ideas with surprisingly universal appeal (*Who Do You Think You Are?*).

The BBC turns things as diverse as ballroom dancing (*Strictly Come Dancing*), home baking (*The Great British Bake Off*), business (*The Apprentice*), classical and pop music (*The Proms*, *The Voice UK*, *Radio 1's Big Weekend*), as well as charitable causes (*Children in Need*, *Comic Relief*) and sport (*Wimbledon*, *The Olympics*, *The FA Cup*) into national events. They become shared pastimes everyone can experience and talk about.

This aspect of universality should not be taken for granted. It is particularly British and particularly a product of having the BBC. In the US, for example, such shared moments are much less widely shared and much rarer. Outside sport, the biggest US audiences are not much bigger than ours, though their population is five times bigger.

5 RAJAR

6 Kantar Media for the BBC, 12,000 UK adults per year, 2014/15

7 RAJAR, 15–29s, average weekly reach, Monday-Friday, 2014/15 (*Newsbeat* slots 1245-1300 and 1745-1800); BARB, 15-29s, all homes, average weekly reach 3+ mins consecutive, Monday-Friday, 2014/15 (BARB genres News: National/International, >10 minutes in duration and a start time within 1 hour of the usual start time of 22:00)

3.2.3 The BBC aims for every household to have convenient access to each relevant BBC service, free at the point of use

The second test of universality is that the BBC's programmes and services must be made widely available within the UK.

The way in which the BBC distributes its programmes and services is becoming increasingly complex. This is partly in response to audiences consuming content in new ways on a variety of new platforms and devices (e.g. BBC iPlayer on mobile phones), but also as a result of new developments in technologies and the media industry (e.g. digital radio on DAB, or broadband internet access bundled with TV and telephone services).

How the BBC ensures audiences benefit from these changes is critically important. It is how we will guarantee access to all audiences. It is important to set clear and simple expectations for licence fee payers about how the BBC will deliver the programmes and services they value in ways that are efficient, convenient and easy to access.

We have encapsulated this in one, overarching objective: the BBC should seek to ensure that every household has convenient access to each relevant BBC service, free at the point of use.

This is not straightforward to achieve. Geography has historically made 100% coverage prohibitively expensive, and the industry norm definition of 'every household' has settled at around 98.5% coverage for terrestrial TV⁸. New platforms and devices are proliferating and most pay platforms offer no completely 'free' option.

So the BBC also needs guiding principles that help it take decisions about how to pursue that ambition within the limitations of technology, practicality and affordability. Those principles are:

- Safeguarding accessible, open routes to BBC services;
- Sustaining high quality free-to-air platforms;
- Providing value for money to licence fee payers;
- Securing quality standards, brand attribution and due prominence;
- Meeting legal obligations and being technically feasible.

Universality is about BBC services as a whole, not individual programmes. The PSB model has been distributed effectively for decades by bundling information, education and entertainment into channels which could be curated and where programmes could be 'hammocked'⁹. This remains relevant to PSB in the internet age. The BBC's iPlayer service offers instant access to the full range of BBC programmes. It sustains the ability of the BBC to launch new programmes, cross-fertilise between genres and introduce audiences to programmes they would not otherwise have found. It is available on over 10,000 types of devices including over 1,700 types of connected TV devices in the UK¹⁰. We deliver bespoke versions of iPlayer when it is in the interests of audiences and we can deliver public value cost-effectively.

8 Digital UK, available at <http://www.digitaluk.co.uk/industry/Multiplexes>

9 'Hammocking' is where a programme with less popular appeal, but often new, or with high public service value, is scheduled between two more popular or established ones to introduce audiences to programmes they might not have chosen in advance

10 BBC, 'BBC iPlayer and our proposals for UK content aggregation', September 2015, available at <http://www.bbc.co.uk/blogs/aboutthebbc/entries/93f4b295-2559-4528-8403-0ed3d6481270>

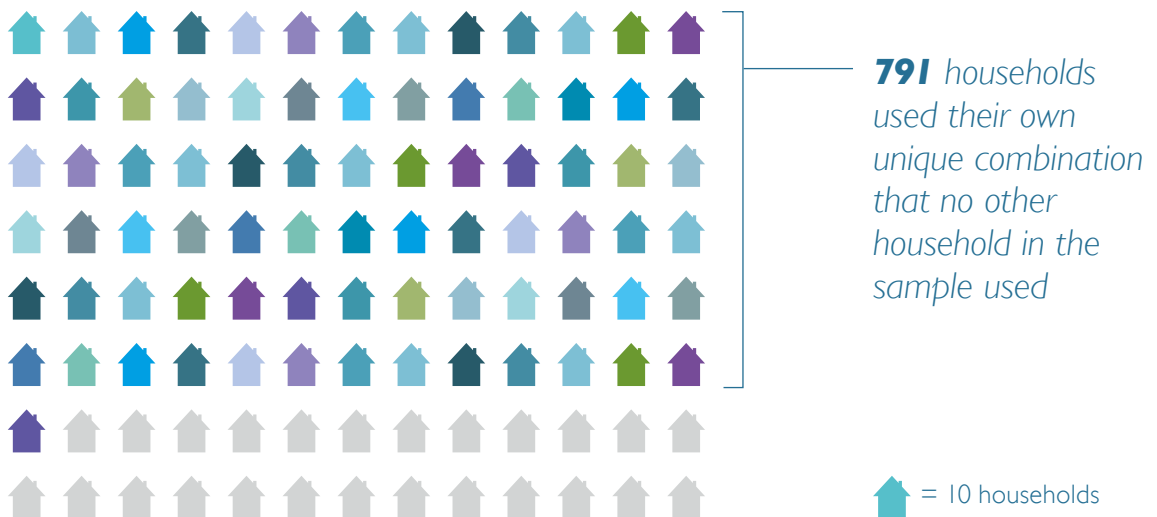
3.2.4 For the BBC, universal usage means valuable, memorable reach that delivers our mission to inform, educate and entertain

The public value of the BBC is created when audiences engage with its public service content. Making distinctive content universally available is not enough by itself. Our aim is for meaningful reach that delivers our mission to inform, educate and entertain.

In practice, the achievement of this aim looks remarkably different in almost every household. There are millions of different BBCs. Every listener, viewer and user can make up his or her own BBC from our services. Through those combinations we achieve our goal of universal delivery of our mission.

The BBC is different for everyone

From a sample of **1,038** households, we counted **825** different combinations of BBC services used in a week



No more than **3%** of households used the same combination of BBC services



Source: Kantar Media for the BBC, 1,038 UK households, July–August 2015

However, the media landscape around us has never been richer, more competitive or offered more choice. So we will have to be targeted and effective in order to continue to reach all audiences with content of public service value. New technology—such as personalisation—will help us do this in future.

Our aim is to ensure that every household, whether measured by deciles of usage or by demographic groupings, should use the BBC meaningfully every week. Each household should receive a balance of output from the BBC: a mix of genres that between them inform, educate and entertain.

By meeting this goal of universal usage, we would keep the BBC as a central part of British life, bringing everyone distinctive, high-quality British content that fulfils the BBC's public mission.

3.3

Should Charter Review formally establish a set of values for the BBC?

Recent evidence from the BBC Trust¹¹ shows that 85% of the public agree that the BBC should retain its current mission and that four in five people think the BBC achieves it. But the research also shows that people support a wider range of aims for the BBC as a public institution. Some of these—such as helping people understand what’s going on in the world—are already reflected in the public purposes. Others—such as value for money, being impartial and ensuring independence—are not but they are embedded elsewhere in the Charter and Agreement and shape what audiences expect of the BBC and how the BBC seeks to behave.

The list of potential values in the Government’s consultation document¹² fits with our ambitions for the BBC. In principle, there is a case for codifying these values. It will be critical, however, to be clear about the meaning and definition of the codified values. Subjective qualities such as ‘distinctive’ and ‘high quality’ will inevitably mean different things to different people, and so we would want to agree how they are best defined.

11 ICM Unlimited for the BBC Trust, ‘Future Priorities for the BBC, An Audience View’, 2111, November–December 2014

12 DCMS, ‘BBC Charter Review Public Consultation’, July 2015. The list of potential values for the BBC is: Independent; Impartial; High quality; Efficient/ Value for Money; Transparent; Distinctive; Diverse/representative.

3.4 Is the expansion of the BBC's services justified in the context of the increased choice for audiences? Is the BBC crowding out commercial competition and, if so, is this justified?

3.4.1 As the market fragments, there is more need for the BBC, not less

We agree with the Government's consultation document¹³ that the media landscape has been transformed since the last Charter Review. But we do not agree with the implicit conclusion that this explosion of choice means that the case for the BBC is diminished, or that a vibrant market is a reason to constrain the BBC. The public's support for the BBC has grown despite the alternatives now on offer and low switching costs between channels.

As Ofcom's third review of PSB shows, the importance of many of the PSB purposes to the public has increased in recent years. The level of public satisfaction with delivery of these purposes and characteristics as a whole has also risen; 69% were satisfied in 2008 while 79% were satisfied in 2014¹⁴. This preference in theory plays out in reality as well. The five main PSB channels still account for just over 50% of viewing¹⁵.

In the BBC Strategy Paper, we provided evidence that the BBC's performance has improved over the current Charter—not as a result of market power but because we innovated and improved audience satisfaction. We reach as many people as we did at the start of the period and they give us higher marks. The time people spend with us, and their appreciation for the quality of our content, has meant that support for the BBC has risen over this Charter period. They give us seven out of ten, on average, higher than in 2007/08. Eight out of ten people say that they would miss the BBC if it did not exist, considerably higher than any other broadcaster¹⁶.

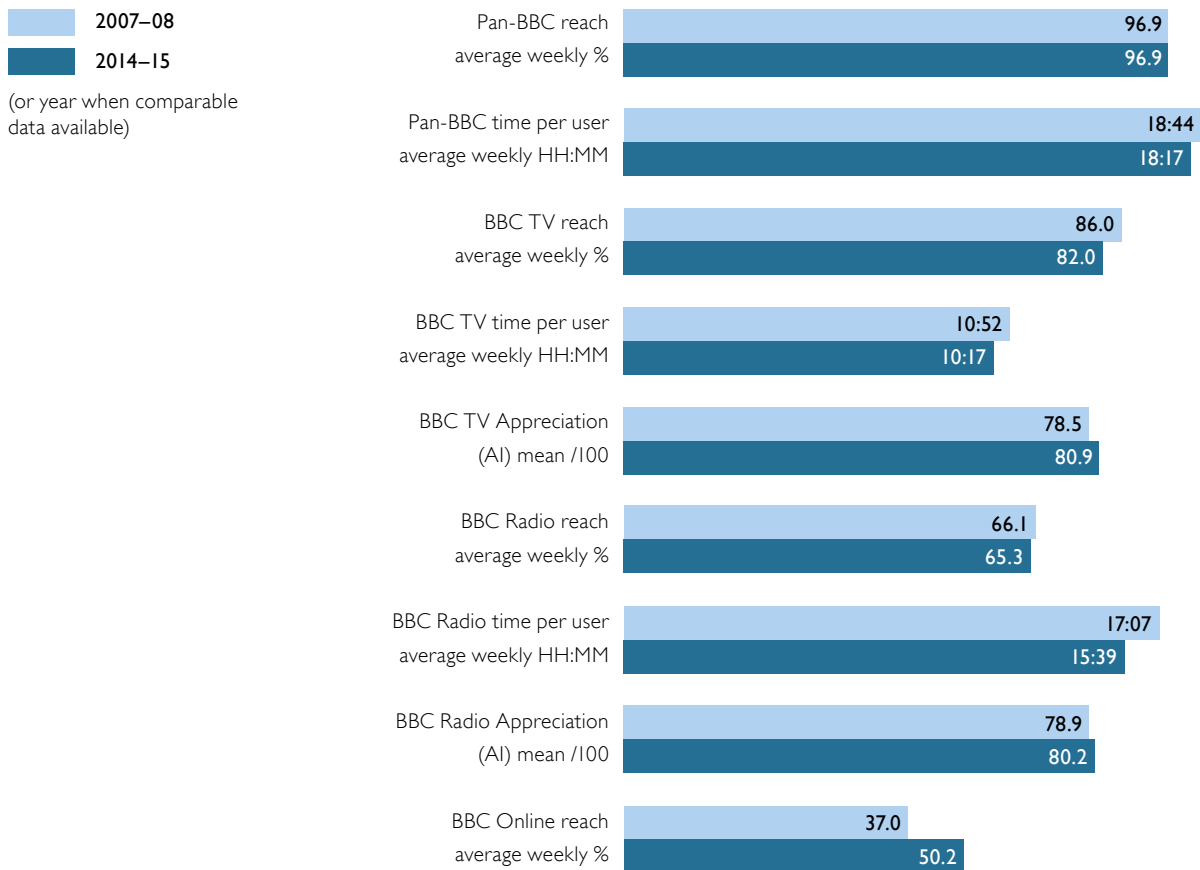
¹³ Foreword by John Whittingdale, Secretary of State for Culture, Media and Sport, DCMS, 'BBC Charter Review Public Consultation', July 2015

¹⁴ Ofcom, PSB Annual Report 2015: PSB Audience Opinion Annex, July 2015. Available at: http://stakeholders.ofcom.org.uk/binaries/broadcast/reviews-investigations/psb-review/psb2015/PSB__2015_audience_impact.pdf

¹⁵ Ofcom, PSB Annual Report 2015: TV Viewing annex, July 2015 (data for 2014). Available at: http://stakeholders.ofcom.org.uk/binaries/broadcast/reviews-investigations/psb-review/psb2015/PSB_2015_TV_Viewing.pdf

¹⁶ Purpose Remit Survey by NatCen for the BBC Trust, 2,298 UK adults, autumn 2014 available at http://downloads.bbc.co.uk/bbctrust/assets/files/pdf/review_report_research/ara_2014_15/uk.pdf

BBC audience performance over the Charter period¹⁷



Over the last two Charter periods we have diversified our services. We launched new services, but at a much slower rate than the rest of the market. They were aimed at audiences who were getting less from the licence fee. They were clearly distinctive, from the Asian Network to 6 Music to BBC Four. We did this for a smaller licence fee in real terms.

¹⁷ Pan-BBC reach and time per user / BBC Online average weekly reach: GfK for the BBC, Cross-Media Insight Survey, 6,000 UK adults, 16+ per quarter, 2009/10 and 2014/15; BBC TV average weekly reach 15+ mins and time per user: BARB, 4+, 2010/11 and 2014/15; BBC Radio average weekly reach 15+ mins and time per user: RAJAR, 15+, 2007/08 and 2014/15; Appreciation Index (AIs): Pulse by GfK for BBC, 2007/08 and 2014/15

The BBC is providing much more, for less¹⁸

The BBC 20 years ago

£153.21 per household (in 2015 prices)
0.23% of GDP



The BBC today

£145.50 per household
0.21% of GDP



Plus new obligations of c£500m

Limited competition:
46% share of TV and radio consumption

Extraordinary competition:
42% share of TV and radio consumption

20 hours per person per week
TV and radio

20 hours per person per week
TV, radio, online

18 BBC analysis

3.4.2 We need to look at the net economic impact of the BBC and the effects on competition, choice and investment

The question of whether the BBC crowds out the market raises a number of important and complex issues.

- First, what is the net economic impact of the BBC, taking account of the BBC's positive effects on the media sector and any crowding out of the market that may take place? Or to put it another way, we need to know what would likely happen to the UK media sector without the BBC or with a diminished BBC. There have been a number of recent pieces of analysis on this last question, from the Reuters Institute and Enders Analysis, and one commissioned by the BBC from PwC¹⁹.
- Second, and of equal importance, to what extent does the audience and wider social, cultural, educational and democratic value created by the BBC outweigh any negative effects on the market that may occur? Or are any negative impacts on the market necessary and proportionate to the fulfilment of the BBC's public purposes and remit? This test is embedded in EU state aid rules as applied to PSB across Europe and in the current Charter and Agreement, including in the Public Value Test (PVT) for service changes.

It is important to define the terms at the outset. 'Crowding out' is usually used to describe a situation where an increase (or decrease) in publicly funded investment results in a decrease (or increase) in privately funded investment. In the DCMS consultation document, the phrase is used more broadly as short-hand to refer to a range of potential negative impacts that the BBC could have on commercial providers.

The discussion needs to be grounded in rigorous analysis and evidence. The set of products and markets that might be affected are rarely defined in terms of, say, their geography or their scope. It is also important to be clear on exactly who might be crowded out. While any short run or 'static' negative impacts on commercial providers are relevant, what is more important is whether there are long run or 'dynamic' impacts on the development of competition, choice and investment in affected markets, and whether they might be contrary to the public interest.

¹⁹ Reuters Institute, 'What if there were no BBC Television', February 2014 available at http://reutersinstitute.politics.ox.ac.uk/sites/default/files/What%20if%20there%20were%20no%20BBC%20TV_Executive%20Summary.pdf; Enders Analysis, 'BBC TV—impact on investment in UK content', 10 September 2014; PwC, 'The impact of a change in the BBC's licence fee revenue', 26 August 2015 available at <http://downloads.bbc.co.uk/aboutthebbc/reports/pdf/bbcifpwc2015.pdf>

3.4.3 The BBC is a smaller part of a larger market

The BBC has become a much smaller part of the UK media sector and is small compared with the global competitors that operate in this country. With revenues of £4.8bn per annum the BBC is a relatively minor player when compared with, for example, BT (with revenues of £18.3bn), Disney (with revenues of £30.1bn), 21st Century Fox (with revenues of £18.6bn), Time Warner (with revenues of £17.6bn), NBC Universal (with revenues of £15.2bn) and BSkyB (with revenues of £11.3bn)²⁰.

BSkyB's operating profits in the UK are now broadly the same as the BBC's investment in original UK TV content.²¹

The DCMS consultation paper suggested that the BBC is the largest PSB in Europe²². Although PSBs are structured and funded differently in different countries, ARD in Germany is bigger in terms of public funding at £4.73 billion and total revenues at £5.50 billion²³.

Twenty years ago the BBC accounted for around 40% of TV industry revenues; today, it accounts for around 20%²⁴. On existing market trends and in light of the Budget funding agreement, it has been forecast that the BBC is set to make up around 12% of TV revenues by the end of the next Charter in 2026²⁵.

The licence fee has been frozen at £145.50 since 2010/11, and the BBC has been required to find c.£500m a year to fund the World Service, Monitoring, broadband, S4C and local television. As a result, licence fee funding for BBC's services fell from around £4.1 billion in 2010/11 to £3.5 billion in real terms²⁶ in 2014/15.

The BBC has gone from having two out of eleven TV channels in 1984 to having nine out of 536 channels in 2014, or from having 18% of the total number of TV channels to around 2%²⁷. BBC TV's share of viewing hours has fallen from 36% in 2004/05 to 33% in 2014/15. In radio, the BBC has gone from 50 out of 226 radio stations in 1995, to 56 out of 413 now.²⁸ So while the BBC has increased its number of TV and radio services, so has the rest of the market, responding both to audience needs and technology opportunities.

The BBC is a relatively small part of the UK online market. Share of time spent in the UK with BBC Online is 3%, compared with Google (5%), YouTube (9%) and Facebook (20%)²⁹. Having helped create the market for online news/information in the UK, the BBC's scale is reducing—the share of BBC News online (in terms of time spent) has fallen to 30% as the market for news/information has grown³⁰.

20 Latest full year revenue data used (March 2015–BBC; BT, December 2014—NBC Universal, Time Warner; September 2014—Walt Disney; June 2014–21st Century Fox; June 2014—Sky, including Europe revenues.)

21 In the 12 months to June 2015, BSkyB recorded operating profits of £1.35 billion.

22 DCMS, 'BBC Charter Review Public Consultation', July 2015 See Box 2 on p22

23 ARD, 2014 figures of 5.87bn EUR and 6.83bn EUR respectively. 2014 average annual exchange rate of IEUR to 0.806GBP (OANDA).

24 BBC analysis of TV revenues data in Ofcom, 'Communications Market Report', 2015 available here <http://stakeholders.ofcom.org.uk/market-data-research/market-data/communications-market-reports/cmr15/>

25 Enders Analysis, July 2015, 'BBC to pay for the over-75s'

26 BBC analysis

27 BFI / Ofcom

28 Ofcom / BBC

29 comScore MMX Multi-Platform, UK, Average Total Minutes, [P] BBC Sites, Jan- May 2015. The equivalent figure for desktops only is 1% for the BBC

30 comScore MMX Desktop only—does not include mobile or tablet viewing, [M], BBC, Average Total Minutes, Panel only numbers based on a custom deliverable

3.4.4 There is no evidence that the BBC is stopping entrants to TV, radio or online markets or that competitors would fill the gap left by a smaller BBC

At its simplest, if the BBC were crowding out the market you would not expect to see the level of competition, choice and market entry that is observable in the TV, radio, news and online sectors today. The UK has one of the strongest creative sectors in the world and, as described in section 3.5, the evidence suggests that this is partly the case because of the BBC, rather than despite it.

Investment decisions by commercial players clearly depend on a range of factors, including demand and supply-side conditions external to the BBC. In general, commercial operators might react to a change in BBC spending in one of two ways:

(a) Crowding out: If the BBC increases its revenues and/or content spend, commercial providers may be 'crowded out' of the market, i.e. the higher BBC investment replaces commercial investment; or

(b) Crowding in: An increase in BBC content spend could lead to an increase in others' spend if the BBC's spending boosts demand and/or stimulates competition for quality.

As described in more detail below, there is little evidence to support the view that the BBC crowds out commercial competition in the TV, radio and online news sectors.

Television

It is difficult to predict how other broadcasters would change their spending in response to a change in the size of the BBC partly because there is much disagreement about the impact of a change in public funding on commercial revenues and investment, including first run originated UK TV content.

3.4.5 Evidence on impact of a change in public funding on commercial revenues

McKinsey, cited in Ofcom (2004)³¹, suggested that *'the likelihood is that the funding of broadcasting would be considerably lower if public funding did not exist [... and] that the share of domestically produced output in the UK would also fall'*. A similar recent analysis by Inflection Point³², which examined the relationships between individual PSBs and commercial market characteristics, also found positive correlations between the health of public broadcasting and the health of private broadcasting, running counter to the theory that high levels of public funding crowd out private funding.

It is unlikely that additional BBC services crowd out commercial TV revenues to any significant extent. This will partly depend upon the relationship between changes in commercial channel viewing or 'commercial impacts' and TV advertising slot prices which, according to Ofcom³³, is complex and likely to involve a number of interactions over the longer term at both the firm and the market level. As a result, the exact 'elasticity' or linkages between changes in the volume of commercial impacts and changes in the price of TV advertising slots is highly contested. But a review of the literature in this area³⁴ suggests that the majority of estimates indicate that a small reduction in viewing for commercial TV channels only has a marginal impact on Net Advertising Revenues (NAR). Any reduction is roughly offset by an increase in the price of advertising slots.

There is little empirical evidence on the extent of any crowding out of subscription revenues. To believe that the BBC crowds out subscription revenues or investment to any significant degree, one or both of the following would need to hold. Firstly, consumers would need to downgrade or churn away from their pay-TV packages in response to an increase in the BBC's spending. Secondly pay-TV providers would need to significantly change their content strategy towards investment in first run UK TV content—and away from exclusive premium content such as sport and movies—in response to a reduction in BBC spending. Recent analysis by Ofcom in the context of the closure of BBC Three suggests that changes in the scope of the BBC would be unlikely to have an impact on subscription revenues for platforms such as Sky or Virgin Media, and subscriptions for VOD services such as Netflix.

32 BBC, 'Public and Private Broadcasters Across the World—The Race to the Top', December, 2013 available at http://downloads.bbc.co.uk/aboutthebbc/insidethebbc/howwework/reports/pdf/bbc_report_public_and_private_broadcasting_across_the_world.pdf

33 See Ofcom, 'Proposed changes to BBC Three, BBC iPlayer, BBC One and CBBC—Market Impact Assessment', 2015, p17 available at http://stakeholders.ofcom.org.uk/binaries/research/tv-research/bbc-mias/market_impact_assessment_report.pdf

34 See Ofcom, 'Proposed changes to BBC Three, BBC iPlayer, BBC One and CBBC—Market Impact Assessment', 2015, footnote 26 for a list of relevant studies.

3.4.6 Evidence on impact of a change in public funding on investment in content

As well as looking at whether the BBC crowds out commercial revenues, it is also important to consider the related issue of whether the BBC crowds out or crowds in commercially funded investment in UK original content.

In its third review of Public Service Broadcasting³⁵, Ofcom published data on investment in first run originated UK content by the PSB channels and the non-PSB channels. Their analysis shows that the level of BBC (and especially BBC One) investment in first run original programmes appears to be correlated with investment in ITV. Thus BBC investment is likely to be a contributory factor in stimulating ITV to spend more through competition for quality.³⁶ Ofcom's recent PSB review concluded that: *"the BBC remains the cornerstone of the PSB system and is the key driver of investment across the system."*³⁷

Ofcom's analysis of the impact of closing BBC Three also considered whether the BBC's retreat from the market would encourage commercial providers to increase their investment in TV content for this target audience. It concluded that this would be unlikely given that TV viewing for younger audiences is falling. Ofcom then went on to raise the possibility that commercial broadcasters may actually be incentivised to reduce their investment in content because they may find it easier to attract viewers in the absence of the BBC's presence.

A number of recent studies have looked at the question of what would likely happen to UK content investment without the BBC or with a much smaller BBC. The Reuters Institute³⁸ concluded that without BBC TV, investment in content (especially first-run UK content) would be significantly lower than at present. This was because TV revenues would be lower overall and a lower proportion would be invested in content, especially first run UK programmes.

The analysis acknowledges that there might be some crowding out of revenues, and in a later study, the author, Professor Barwise also allowed for the possibility that pay TV operators might increase the proportion of their future revenues invested in TV content if the BBC were smaller. Nevertheless despite the fact that these studies allowed for some degree of crowding out, they still concluded investment in UK TV content would be lower if the BBC were smaller or did not exist at all.

This finding is reinforced by recent work from Enders Analysis³⁹. They concluded that pay TV platforms could gain additional revenues if there were no BBC TV although their cost base would increase as the loss of free-to-view BBC TV programming (accounting for c.30% viewing share) would need to be replaced with paid-for content. However, because pay-TV operators invest less than 10p per pound of revenue in new UK originated content excluding sport, they would not fill the investment gap left by the BBC.

While the aforementioned analysis can go some way to providing an answer as to whether the BBC crowds out or crowds in the commercial sector, it can only be used as a broad predictor of what might happen under certain conditions. The last few years have provided us with a real-life experiment in what happens with a smaller BBC.

As the BBC's spending on UK services fell over the last five years, far from increasing, as a superficial view of crowding out would suggest, spending on original UK content actually fell, by £247m⁴⁰. The commercial PSBs also reduced their content investment, consistent with the competition for quality hypothesis. There is a real risk that a diminished BBC would reduce the competitive pressures in broadcasting, leading to a new equilibrium of investment that is lower than before.⁴¹

35 Ofcom, 'Public Service Content in a Connected Society', December 2014

36 See Ofcom, 'Public Service Content in a Connected Society', December 2014, figure 51

37 Ofcom, 'Public Service Broadcasting in the Internet Age', July 2015, p3

38 P. Barwise and R. Picard for Reuters Institute, 'What if there were no BBC Television', February 2014

39 Enders Analysis, 'BBC TV- impact on investment in UK content investment', 10 September 2015

40 BBC analysis of Ofcom data in Ofcom, 'Public Service Content in a Connected Society', December 2014. Figure quoted is in 2013 prices.

41 See Enders Analysis, 'BBC TV—impact on investment in UK content', 10 September 2015 and P. Barwise and R. Picard, 'What if there were no BBC Television', February 2014

Radio

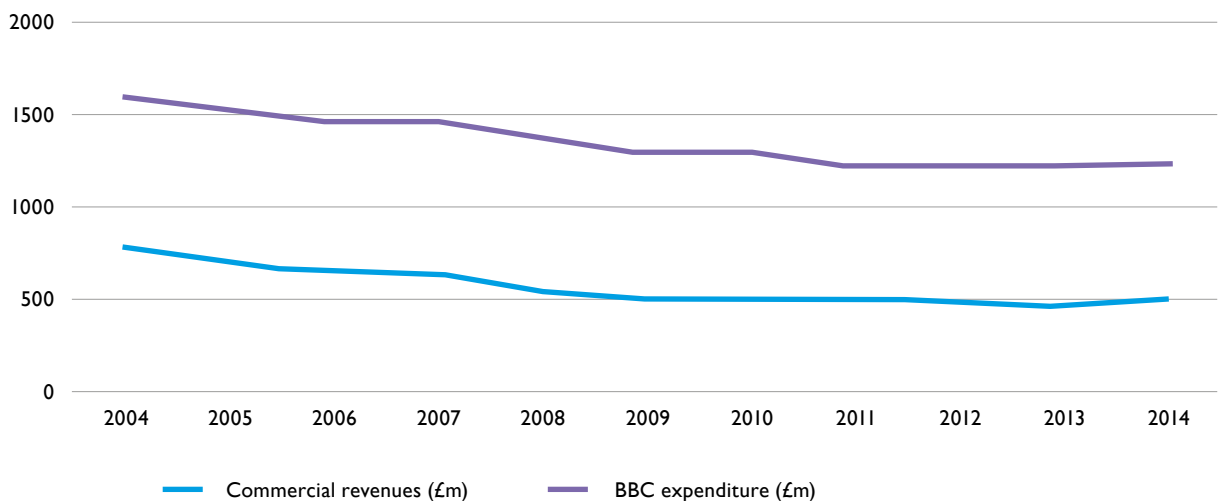
The gap between share of listening hours for BBC and commercial radio is at its lowest level for around 10 years, with the BBC taking a share of c.54%. Over the same period, expenditure on BBC radio has fallen by c.13% in real terms from c£830m to £725m⁴². Commercial radio revenues have fallen in real terms by over one-third from £756m in 2004 to £483m in 2014.

There are a wide range of factors which might explain this. The structural changes in the advertising market including the rapid growth in online advertising are likely to be an important contributory factor;

commercial radio's share of total advertising has fallen to 3% in 2014 from 18% in 2004⁴³. As a result, it would appear that commercial radio is earning less revenue per listener than before.

It is unlikely that the BBC has contributed to this decline. The BBC does not compete for advertising revenues. If the BBC had caused the decline, you would expect commercial revenues to increase in response to a decrease in BBC spending on its radio services. But the chart below shows that there is no evidence of this.

BBC expenditure on radio and commercial radio revenues (2014 prices)⁴⁴



Moreover, our analysis shows that BBC's radio services are distinctive from commercial radio (see the BBC Strategy Paper and section 3.8 and 3.9 below). This suggests that they are more of a complement to, rather than a substitute for, commercial radio.

⁴² Data from Ofcom CMR (various years) . Prices expressed in 2014 levels, adjusted for RPI. Ofcom does not publish data on expenditure by the commercial sector.

⁴³ BBC analysis of data from Ofcom, 'Communications Market Report' (various years)

⁴⁴ Data deflated by RPI

News Online

The DCMS consultation paper noted that the BBC has a variety of impacts on online markets. In particular it highlighted “suggestions that the scale of the BBC’s online offer is impeding the ability of other UK news outlets to develop profitable business models, such as paywalls and subscriptions, in existing and new markets”.⁴⁵

The well-documented challenges facing the news sector largely stem from the structural shift of advertising online. Overall online NAR went up from £1.2bn to £2.1bn over the period 2009–2013 compared with a decline in national and regional newspaper NAR from £2.8 billion to £2.1 billion over the same period.⁴⁶ As a result news providers worldwide are competing for revenues against a much broader set of competitors. The BBC is not responsible for these structural changes. The decline

in newspaper sales and in advertising can be observed in all major markets, irrespective of the existence or scale of PSB.⁴⁷ In the US, PSB is small (c1% TV share⁴⁸), but newspaper revenues still fell by around one-third and newsroom employment shrank by nearly one-fifth during 2000–2009.⁴⁹

The key question is not the scale of the BBC in online news. BBC News generates significant externalities through the universal availability and wide consumption of high-quality news, valued by licence fee payers as the most trusted and impartial. The question is rather the extent to which BBC’s usage or revenues substitute those of commercial news providers over time. The evidence for such a negative dynamic impact on the online news market is lacking.

45 DCMS, ‘BBC Charter Review Public Consultation’, 16 July 2015, page 25,

46 Mediatique for the BBC citing Zenith Optimedia, ‘The provision and consumption of online news—current and future’, December 2014, Slide 11 available at http://downloads.bbc.co.uk/aboutthebbc/insidethebbc/howwework/reports/pdf/mediatique_online_news_report_dec_2014.pdf

47 Mediatique for the BBC citing ZenithOptimedia, ‘The provision and consumption of online news—current and future’, December 2014, Slide 14

48 Ofcom, ‘International Communications Market Report’, December 2014, Section 3.3 available at http://stakeholders.ofcom.org.uk/binaries/research/cmr/cmr14/icmr/ICMR_2014.pdf

49 Pew Research Center, ‘State of the News Media 2015’, April 2015, available at <http://www.journalism.org/files/2015/04/FINAL-STATE-OF-THE-NEWS-MEDIA1.pdf>

3.4.7 Total consumption metrics do not suggest harmful substitution

The critical context for any analysis of substitution between consumption of BBC news and other providers is the growth of online usage. Time online among internet users has more than doubled since 2005⁵⁰ and this expansion has enabled a substantial increase in the number of people consuming online news, which has trebled in the last decade to over 60%.⁵¹ The online news market is not nascent; it is large and growing fast. All the trends suggest online time spent will continue to grow which will increase rather than diminish the opportunities available for online news provision.

Contrary to a one-sided 'crowding out' hypothesis, the evidence suggests that UK providers are seizing the opportunities of this growing market. If the BBC were having a negative impact on newspapers in the UK, we might expect UK newspapers to be performing poorly, in particular relative to their comparators in other markets. However, UK newspaper websites are successful.

Over the last six years, the *Mail Online's* daily page views have grown fourteen-fold and the *Guardian's* three-fold⁵², while Newsquest unique browsers were up 36% in the past year⁵³. The reach of UK newspaper sites suggests that the BBC's success is not at their expense. Indeed, the largest two UK newspaper sites (the *Mail* and the *Guardian*) actually have higher reach than the largest two newspaper sites in each of the USA, France and Germany⁵⁴. Similarly, if there was strong substitution between the BBC and newspapers, we might, for example, expect an increase in BBC reach to lead to a drop in *Mail Online* reach. In fact, there is no such pattern⁵⁵.

Total consumption metrics do not suggest harmful substitution. Similarly, nor do the realities of consumer behaviour when faced with growing online choice. News consumers tend to multi-source. comScore figures suggest that those using news and information sites typically use around five each month.⁵⁶ Many consumers will seek out multiple perspectives on the same story. According to a Mintel survey of online news consumers, 51% said they agreed they "often check more than one source to confirm news stories I've read"⁵⁷. In the case of the BBC, 75% of those who use BBC Online in a month also visit one of the other top 20 news and information sites.⁵⁸ This is, in part at least, because of the BBC's policy of linking to other news providers. The 8.6m monthly click-throughs in the UK from BBC News lead to more consumption of news on other news websites.⁵⁹ It is also in part because consumers turn to different news providers for different reasons. BBC news usage is associated with audience perceptions of its accuracy and impartiality; while newspapers lead on strong points of view, sometimes correlated with political attitudes.⁶⁰ This reflects the difference in the news offers themselves—not just in editorial tone, but in terms of the breadth and focus of the offer.

The BBC's online offer is distinctive—yet we want to explore the creative opportunities of making it even more distinctive. This challenge is being considered as part of the BBC's review of its online activities, set out in the BBC Strategy Paper.

50 Ofcom, 'Adults' media use and attitudes Report 2015', May 2015, page 28 available at http://stakeholders.ofcom.org.uk/binaries/research/media-literacy/media-lit-10years/2015_Adults_media_use_and_attitudes_report.pdf

51 ONS, 'Internet Access—Households and Individuals 2015', 6 August 2015, page 5 available at http://www.ons.gov.uk/ons/dcp171778_412758.pdf

52 ABC data, July 2010—July 2015.

53 Newsquest, 'Newsquest Delivers More Strong Growth in Local Online Audience', 26 August 2015 available at <http://www.newsquest.co.uk/news/view/newsquest-delivers-more-strong-growth-in-local-online-audience/>

54 Reuters Institute for the Study of Journalism, 'Digital News Report 2015', July 2015.

55 comScore MMX, UK, July 2012–June 2015, Unique Visitors, [C] BBC News, [P] Mail Online / Daily Mail, [C] Mail Online

56 comScore MMX, UK, June 2015, News/Information category, Unique Visitors

57 Mintel, Consumer Perceptions of News Media, September 2010

58 comScore MMX, UK, Jan-May 2015, Average Unique Visitors

59 BBC server data H115.

60 Ipsos Mori for the BBC, November 2011, reasons highlighted per provider are those cited for that provider significantly more often than the UK average.

3.4.8 The BBC does not compete directly with other online news providers for revenues in the UK

The BBC does not take a share of consumers' wallets for subscription fees, since the website is free at the point of use. Some have suggested that the BBC has conditioned the market to be 'free'—impeding the potential of successful paywalls. The corporate strategies and investor statements of the UK's newspapers do not support this claim. Nor does the international evidence. "Free" is the favourite model in all key jurisdictions, whether or not there is a publicly funded provider of scale.⁶¹

The BBC does provide ad-funded online news internationally as it is required to do by the Charter and Agreement. However, the incremental presence of the BBC is likely to make little difference, given the

BBC's tiny share of the global online ad market. And, in any case, the BBC's international websites do so without subsidy from the licence fee, so on equal competitive terms to others seeking advertising revenue.

The realities of online advertising markets also underline how marginal the BBC's consumption impact is on commercial online news. Even if the BBC's share of time online (3%) were deliberately constrained, any resulting uplift in advertising elsewhere would be small and likely to accrue to a range of ad-funded online businesses well beyond UK news providers.

61 Mediatique for the BBC, 'The provision and consumption of online news—current and future', December 2014, Slide 3

3.4.9 The evidence is against a dynamic impact of the BBC on the online news market

There is little evidence to suggest that the BBC is having a significant negative dynamic impact on the online news market. The success of commercial providers is reflected in the positive outlook in Oliver & Ohlbaum's recent report for the News Media Association that "*commercially funded news organisations remain strong and are on a path to sustainability in a 'digital-first' future.*"⁶² The report also found little evidence of BBC market impact and primarily recommended that the BBC look to develop new partnerships.

UK news brands are among the strongest in the world in online news, replicating the success of British providers like the BBC World Service in exporting trusted news around the globe. Two thirds of the monthly unique users to the *Daily Mail* and to *The Guardian* are from overseas⁶³. The UK reaches a global audience, dominating the charts of the world's leading online news providers (the BBC, *Guardian* and *Daily Mail* are often mentioned but the *Telegraph*, *Independent* and *Mirror* Groups are also in the world's top 15 newspaper sites.⁶⁴ This is based on strong demand for British journalism and on a willingness to embrace new digital business models by incumbents and new entrants alike.⁶⁵

This is also the case for new entrants. Were the BBC 'crowding out', you would not expect new and overseas providers to be attracted to the UK market. However, lower barriers to entry have enabled a big expansion in choice of news outlets in the UK. Moreover, news providers such as BuzzFeed and Huffington Post are growing more quickly than traditional newspaper sites did⁶⁶ and generating new digital revenues (roughly £90m in 2013 from the UK⁶⁷).

While some have argued that the BBC has caused the decline in the local newspaper sector, the evidence does not support the claim. The pressures on local newspapers derive from a digital transition which has allowed new competitors for content and advertising to emerge, from specialists like Jobsite, Auto Trader and Zoopla to social media and search. The BBC is not responsible for these structural advertising changes and there is no evidence that it has a dynamic impact on their news provision online. Over the past five years, traffic to a number of major local news groups has grown five-fold. Digital advertising spend on local news brands increased by 23% in 2014 alone—substantially higher than the growth rate for UK internet advertising overall.⁶⁸ Similarly, were the BBC to be 'crowding out' local news online, you would not expect new entrants like BuzzFeed to be hiring a number of regional reporters, as they announced they would in September 2015.⁶⁹

While the BBC is not the source of the problem, we want to be *part* of the answer to the challenges facing local journalism. This is why we have set out new partnership proposals for discussion with the sector⁷⁰.

62 Oliver & Ohlbaum Associates for the News Media Association, 'UK news provision at the crossroads The news market in the 21st Century and the likely implications for the BBC's role', September 2015, page 5, available at [http://www.newsmediak.org/write/MediaUploads/PDF%20Docs/OandO_NMA - UK_news_provision_at_the_crossroads.pdf](http://www.newsmediak.org/write/MediaUploads/PDF%20Docs/OandO_NMA_-_UK_news_provision_at_the_crossroads.pdf)

63 Mediatique for the BBC, 'The provision and consumption of online news—current and future', December 2014

64 comScore MMX, Worldwide, June 2015, Unique Visitors

65 Overall, UK online news revenues are close to £500m pa, up 65% in 2 years. Mediatique for the BBC, 'The provision and consumption of online news—current and future', December 2014, slide 17

66 The rapidity with which they reach \$50m revenues doubles roughly every 5 years. Mediatique for the BBC, 'The provision and consumption of online news—current and future', December 2014, slide 18

67 Mediatique for the BBC, 'The provision and consumption of online news—current and future', December 2014, slide 38

68 Enders Analysis, Local Media: New Emerging Structures, estimate based on WARC data for Q1–Q3 which show overall UK internet advertising to have grown at 14%, April 2015

69 BuzzFeed, advertisement for jobs advertised in September, available at time of publication at http://www.buzzfeed.com/about/jobs?gh_jid=102487

70 BBC, 'British Bold Creative, The BBC's programmes and services in the next Charter', September 2015, Section 5.5,

3.5 Where does the evidence suggest that the BBC has a positive or negative wider impact on the market?

3.5.1 Investment in the BBC strengthens the wider economy

As argued above, the BBC's primary purpose is to provide universal access to services that educate, inform and entertain. At the same time, the BBC's public service remit requires it to invest in new, home-grown creative ideas and talent, and the licence fee enables it to do so at scale. Economic value is therefore a significant added benefit of the BBC's public mission.

The evidence supports the view that the BBC makes UK broadcasting and the wider creative sector stronger. It has a net positive effect. Frontier Economics⁷¹ has identified the principal channels through which the BBC supports private sector growth. The BBC is densely connected to many parts of the sector through its investments, supply-chain linkages and positive spill-overs. It is these inter-connections that ensure its economic benefit reaches further and wider than other players. By opening up the BBC to be Britain's creative partner and delivering the new proposals announced in September, we have an opportunity to do even more to support the creative sector in the next Charter.

First, the BBC is a major investor in the creative industries. In 2013/14 the BBC invested around £2.2 billion of licence fee income into the creative industries. This included c.£1.2 billion outside the BBC, with around £450 million in small and micro-sized creative businesses. The BBC supported over 2,700 creative suppliers and over 80% of those were small or micro-sized. A further £1.5 billion was invested

outside of the creative industries in the UK, much of which was in the digital and high-tech industries on activities which support content creation and content distribution.

Second, the BBC provides a shop window to the UK's creative industries, generating second-round benefits through the commercial exploitation of intellectual property and stimulating additional demand and output in connected industries like music and publishing.

On TV, the BBC's *Dancing with the Stars* (the international version of *Strictly Come Dancing*), for example, is now licensed to over 50 countries and in the US it is one of ABC's highest rating programmes. BBC Worldwide represents content from over 250 British independent production companies and is the largest distributor of finished TV programmes outside the major US studios.

The BBC is recognised as being indispensable to the UK's position as a global music leader⁷². Radio 1 and Radio 2, in particular, discover and promote new music talent and exposure on their airwaves has resulted in increased record sales. For example, the naming of Sam Smith—now a global star—as 'BBC Sound of 2014' in early January of that year led to a spike in his album sales—they rose from 1,000th on Amazon to 6th in the following twenty-four hours.

Online, the invention of the BBC iPlayer helped to build the market for online VoD services⁷³, to the benefit of all market participants.

71 Frontier Economics, 'The contribution of the BBC to the UK creative industries', April 2015 available at http://downloads.bbc.co.uk/aboutthebbc/insidethebbc/reports/pdf/bbc_report_contribution_to_the_UK_creative_industries.pdf

72 Music Week cover, 27th July 2015

73 Ofcom 'Proposed changes to BBC Three, BBC iPlayer, BBC One and CBBC—Market Impact Assessment', 2015, para 1.10

BBC iPlayer case study

iPlayer acted as a catalyst for the development of VoD and generated demand for broadband connectivity. Back in the mid-2000s, the BBC was able to overcome the uncertain investment conditions and co-ordination problems associated with VoD. Its mission to 'bring new digital technologies to everyone' gave it a mandate and its funding model, expertise and trusted brand gave it the means. The success of BBC iPlayer increased demand for VoD services to the benefit of all market participants. Reed Hastings, Chief Executive of Netflix, recently said: "The iPlayer really blazed the trail. That was long before Netflix and really got people used to this idea of on-demand viewing."⁷⁴ Simon Morris, Chief Marketing Officer of Lovefilm, credits iPlayer for bringing catch-up TV services to mainstream audiences: "With the iPlayer, the BBC did a great job of changing consumer behaviour and we have benefited from that—they normalised the idea of catch-up TV. The service went a long way to explaining to middle England that streaming content was normal".⁷⁵

Out of Europe's top five economies, the UK has both the broadest free-to-air catch-up viewing and the strongest commercial revenues—more than two-and-a half times greater than the next biggest.

As the VoD market has grown, BBC iPlayer's market share has declined. While claimed usage of BBC iPlayer is the highest of all long-form, on-demand TV services, year-on-year growth in BBC iPlayer programme requests has slowed in recent years, growing 16% between 2013 and 2014, compared to 26% growth for ITV Player and 23% growth for All4.⁷⁶

74 See The Telegraph, 'Netflix chief Reed Hastings takes on telcos, cinemas and global expansion', 5 October 2014 available at <http://www.telegraph.co.uk/finance/newsbysector/mediatechnologyandtelecoms/media/11141864/Netflix-chief-Reed-Hastings-takes-on-telcos-cinemas-and-global-expansion.html>

75 See Techradar 'Lovefilm: iPlayer changed the streaming game', 28 November 2011 available at <http://www.techradar.com/news/internet/lovefilm-iplayer-changed-the-streaming-game-1043855>

76 BBC figures for iPlayer performance pack January 2015 and ITV and C4 figures from company annual reports for 2014

Third, the BBC's activities generate spillover impacts that strengthen the productive capability of the creative industries across the UK. These are hard to directly quantify in monetary terms but important nonetheless. It does this by discovering and championing the next generation of British on-screen and back-stage talent. In the past 12 months, BBC Introducing has discovered over 30 artists that have subsequently signed to major and significant indie record labels. Oscar-winning directors such as Danny Boyle and Tom Hooper, or global acting stars such as David Oyelowo, Martin Freeman and Daniel Craig, all had early breaks on the BBC. Similarly, the BBC's huge role in training and in creative and technical skills development—when combined with high labour mobility—benefits the digital and creative industries. In 2013/14 the BBC trained 13,500 BBC staff members and 8,000 from the industry.

The BBC also strengthens the creative sector by acting as an 'anchor tenant' for media/digital clusters across the UK—in Salford and Manchester with MediaCityUK, in Bristol with the Natural History Unit, in Cardiff with the drama village and in Glasgow with Pacific Quay. The BBC will play a key role in the transformation of central Cardiff as anchor tenant in Central Square.

We asked PwC to quantify some of these effects by modelling the impact on the creative economy and the whole economy of changes in licence fee investment. The analysis took into account the fact that a change in licence fee income will not only change the BBC's expenditure with knock-on impacts across the creative sector, but could also affect other broadcasters' spending and household expenditure. It therefore measured the net economic effect of the BBC.

PwC⁷⁷ considered a hypothetical 15% nominal increase over a five year period in the BBC's licence fee income. Its analysis suggested that the increase would boost creative sector GVA by £435m, total economy GVA by £319m and create 16,200 extra jobs in 2021/22, compared to the counterfactual where the BBC's licence fee revenues remained unchanged.

This growth is driven by a number of factors. First, the rise in licence fee income results in a net increase in investment in original TV content (£221 million by 2020/21) and the wider creative industries which has a multiplier effect. As outlined above, PwC acknowledges it is difficult to predict whether a higher licence fee would 'crowd out' or 'crowd in' commercial activity. To be prudent, they assume that an increase in BBC spending would reduce other broadcasters' revenues and expenditure to some degree. Second, an increase in the licence fee would mean that households have slightly less income to spend on other goods and services.

The analysis concludes that increased licence fee investment would far outweigh either of the downside effects. This is because the licence fee channels resources into one of the most productive parts of the UK economy, the creative industries, and the BBC's linkages are wider and deeper than other players. Every £1 increase in licence fee income generates an extra 60 pence of economic value. Thus far from increasing the deficit, this is an area where public investment reduces it.

PwC's analysis also demonstrates that the effects work in reverse, too. The second hypothetical scenario involved a 25% nominal decrease in licence fee revenues over the five year period. This would likely reduce creative sector GVA by £997m, total economy GVA by £630m and lose 32,000 jobs in 2021/22, compared to the counterfactual where the BBC's licence fee revenues remained unchanged.

77 PwC, 'The impact of a change in the BBC's licence fee revenue', August 2015

3.6

What role should the BBC have in influencing the future technological landscape including in future radio switchover?

3.6.1 The BBC plays an important part in shaping the technological landscape

Throughout its history the BBC has helped shape the technological landscape in the UK to the benefit of both licence fee payers and the wider industry. The combination of a public mission, secure funding and technical expertise means we have been able to invest at scale in open technology and standards that benefit licence fee payers, commercial organisations and the wider sector. While hard to quantify in monetary terms, the positive technology spill-overs generated by the BBC are important. The BBC has been behind a range of technology firsts from FM radio to DAB; from colour TV to Ceefax to Freeview; and from iPlayer to Interactive TV.

The BBC's role here should be the same as always. It is to use technology to find new and better ways to inform, educate and entertain and deliver the public purposes. In addition, we want to put our technology and digital capabilities at the service of partners and the wider industry to deliver the best to audiences. We will do this in the next Charter in the following ways:

- **BBC investment in, and development of new technology, will bring licence fee payers great new services.** As described above, the iPlayer, launched almost ten years ago, was the result of significant technical investment and development at the BBC. In 2012 BBC innovation brought UK audiences the first digital Olympics. Most recently, the BBC has worked closely with Digital UK, other broadcasters and the wider TV industry to develop and launch Freeview Play, which combines catch-up, on-demand and live TV on the Freeview platform. The BBC Strategy Paper sets out our ideas for the next Charter period.
- **The BBC provides capital-in-kind in technology.** The BBC works on technology concepts well before they are commercially viable, enabling the industry to explore and develop new technologies. For example, at the recent Commonwealth Games in Glasgow, BBC R&D exhibited its new IP Studio system, that will pave the way for greater agility and capability of IP-based production systems to carry new types of services.
- **The BBC catalyses media markets.** Because of licence fee investment and its public service remit, the BBC can take the lead even where business models are unclear, helping develop the market and stimulate demand. As set out in section 3.5, the BBC iPlayer, which launched in 2007, helped create a thriving on-demand market in the UK.
- **The BBC provides world-class expertise to the UK.** BBC R&D leads the world in broadcast technology innovation. By working closely with world-class universities such as Imperial College, R&D is able to leverage a modest investment to deliver research and engineering that sets standards that are used around the globe. Without BBC R&D, the UK's broadcasting ecology would risk being defined by interests that are outside the UK, primarily Asia and the USA. Further, the BBC continues to be a leading training centre for broadcast engineering expertise and digital technology skills.
- **The BBC helps develop the standards that underpin modern media.** BBC work led to the creation of the standards that enable High Definition TV to be transmitted on terrestrial TV. The use of this DVB-T2 technology has improved DTT spectrum capacity by 50%. The BBC is a key player in the Digital Production Partnership (DPP), establishing standards for the transfer of completed programmes between broadcasters and independent producers and post-production houses, reducing costs across the industry. As Sony has recently said: *"Without doubt the BBC was and continues to be the prime mover in the DPP as it alone has the scale, vision and deep technical competence to promote the dialogue across the fullest range of topics."*⁷⁸

78 In correspondence from Sony Professional, September 2015

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- **The BBC supports the eco-system of free broadcast platforms in the UK.** The BBC has been instrumental in launching and supporting Freeview, Freesat and Youview; ensuring UK viewers have a broad range of free-to-view ways to consume live, catch-up and on-demand TV and thereby sustaining healthy inter-platform competition. During the last Charter period the BBC led Digital Switchover on time and to budget.

The BBC helps the public make the most of emerging communications technologies. Earlier this year, with 29 partners we developed and launched the BBC micro:bit to support coding and the computing curriculum. A pocket-sized codeable computer, the BBC micro:bit, will be given to every child in the UK in their first year of secondary education. It demonstrates the BBC's ongoing commitment to bring new technology to the public and address important skills gaps.

3.6.2 We support a fully digital future for radio but the timetable must be set by listeners

Radio plays an important part in everyday lives around the country—90% of the UK listens to radio each week⁷⁹. It is an important part of what people value about the BBC. BBC Radio average weekly reach is 65%⁸⁰. We continue to invest more than any other broadcaster—£653m, 16% of licence fee income⁸¹ in 2014/15—in distinctive, sometimes unique radio services, that offer a wide breadth of content from news to drama to sport and, of course, music.

Audiences have enthusiastically taken up digital and internet-enabled ways of consuming music and speech services. The BBC has a strong portfolio of digital-only services whose audiences have grown significantly, with BBC Radio 4 Extra and BBC 6 Music each receiving more listeners than any other digital-only station in the UK. iPlayer Radio and Playlister have given audiences new ways to access and get even more value from the BBC's content. And we have worked with industry to make it easier for all UK licensed radio broadcasters to reach online audiences through the Radio Player. We support a digital future for radio and will innovate further to exploit the potential of different platforms to offer audiences great listening experiences.

The Government has been clear that its decisions about any analogue switchoff will be led by listeners. We agree. While there has been positive growth, digital listening remains work in progress. 40%⁸² of listening is now digital and on current trends we would expect the 50% target to be met around 2018 to 2019. 14%⁸³ of radio listeners listen exclusively to digital radio; the vast majority either listen to a mix of analogue and digital (47%), or analogue only (35%). In-car listening is growing, but is far from universal—only one in four cars have a digital radio—leaving 29m cars on UK roads with no means of receiving digital radio.

Digital listening has become more diverse in recent years. Nearly 8 million people access digital radio via their television every week⁸⁴ and online listening is growing faster than DAB (albeit from a lower base). Since 2012 overall internet listening has increased significantly and young audiences listen to almost as much radio over the internet as over DAB⁸⁵. Internet services offer new creative opportunities, choice and convenience alongside broadcasting; our new music ideas for the next Charter, for example, while retaining links with our broadcast services, can only be fully exploited with an internet connection.

79 RAJAR, 15+, Q2 2015

80 RAJAR, 15+, Q2 2015

81 BBC Annual Report and Accounts 2014-15

82 RAJAR, 15+, Q2, 2015

83 RAJAR, 15+, Q2 2015

84 RAJAR, 15+, Q2 2015

85 RAJAR, 15-24, Q2 2015 Online hours = 14.3m; DAB hours = 17.9m

The Government has set a target of 50% digital listening to be reached before it determines the future of radio distribution and any timetable for a possible switchover. Until then, and likely for some time afterwards, a hybrid model—combining FM, DAB, DTV and IP—will be needed to meet our obligation to ensure our radio services are widely available in a cost-effective way. The BBC's committed level of DAB expansion will be reached in 2016. At that point pan-UK coverage will exceed 97%, with coverage for local services around 90%. We propose to meet these commitments, and continue to support DAB at this level, as long as we are funded to do so.

Further build out of the DAB networks to reach the same coverage as FM would be a major undertaking, likely to increase radio distribution costs by between £40-£45m a year exclusive of any work to maintain the existing networks. We are not convinced of the value for money case for any further such investment, particularly while digital listening remains below 50%, with DAB listening only a proportion of that.⁸⁶

When the 50% listening target is met, the planned review of digital switchover by Government should look at the right mix of platforms. If the Government proceeds with switchover, this will likely impose cost on some consumers and likely require marketing and communications effort by industry. The beneficiaries include commercial broadcasters, transmission providers, equipment manufacturers and other parties who may benefit from the analogue broadcast spectrum released. Within the Budget funding agreement, the BBC cannot fund the costs of such a switchover without significantly impacting services. It would be counter-productive for the BBC to be required to help fund switchover to a digital world from which it was simultaneously removing much-loved digital radio services.

86 BBC analysis

3.7

How well is the BBC serving its national and international audiences?

3.7.1 The BBC serves all of the UK

Section I of the BBC Strategy Paper shows how almost everyone in the country—97% of adults and 99% of households—uses the BBC every week and, on average, adults spend around 18 hours and households over 40 hours a week with the BBC.⁸⁷ 82% of the TV set-owning population watch BBC TV each week; close to two-thirds of the population listen to BBC Radio per week and half of all adults and over 60% of those online access BBC Online every week.⁸⁸ At a time of growing choice, people still choose to

make the BBC central to their lives. This is achieved through the range of services that the BBC offers as we show in section 3.2 of this document. Yet, while there may be great variety in how different households choose to access BBC content, there is much more similarity in the outcomes.

82% of UK households feel that overall the BBC informs, educates and entertains them well. Even among groups that use the BBC less, that support does not fall below 75%.

The BBC serves UK households well⁸⁹

How well do you think the BBC informs, educates and entertains your household?



The BBC caters for a wide range of tastes



The BBC helps people in my household understand what is happening in the UK and the world today



The BBC has high quality programmes and services for my household



The BBC has a wide range of enjoyable and entertaining programmes and online content for my household



The BBC helps people in my household to learn new things



As good as these outcomes are, are they simply akin to what the commercial PSBs in the UK achieve or the same as publicly funded broadcasters in other countries? On both counts, the evidence shows that what the BBC provides to UK audiences is special.

When Ofcom asks viewers to rate the performance of PSB in the UK, BBC One or BBC Two lead the commercial PSBs on delivery of virtually all of the 13 public service purposes and characteristics.⁹⁰ Further, BBC television has greater impact than commercial PSBs with more BBC One viewers and BBC Two

viewers reporting that they have learned something new as result of watching the channel compared with ITV viewers and Channel 4 viewers respectively.⁹¹ And, in international studies where audiences rate the main publicly funded and commercial channels in their country, BBC One emerges top out of over 60 channels for quality and is also rated the highest for helping people to learn new things and joint highest for helping people understand what is happening in the world and their country today. See the audience research appendix to this document for further details.

87 BBC reach and time per adult: GfK for the BBC, Cross-Media Insight Survey, 6,000 UK adults 16+ per quarter, 2014/15. BBC reach and time per household: reach = Kantar Media for the BBC, 1,038 UK households, July-August 2015; time = BARB, 4+, 2014/15, RAJAR, 10+, 2014/15; GfK Cross-Media Insight Survey (as above), ONS

88 BBC TV: BARB, 4+, 2014/15; BBC Radio: RAJAR, 15+, 2014/15; BBC Online: GfK for the BBC, Cross-Media Insight Survey, 6,000 UK adults 16+ per quarter, 2014/15

89 Kantar Media for the BBC, 1,038 UK households, July-August 2015. Agree / disagree: disagree: 1-4, agree 6-10 on a ten-point scale

90 Ofcom, PSB Annual Report 2015: Audience Opinion Annex. Available at: http://stakeholders.ofcom.org.uk/binaries/broadcast/reviews-investigations/psb-review/psb2015/PSB_2015_audience_impact.pdf

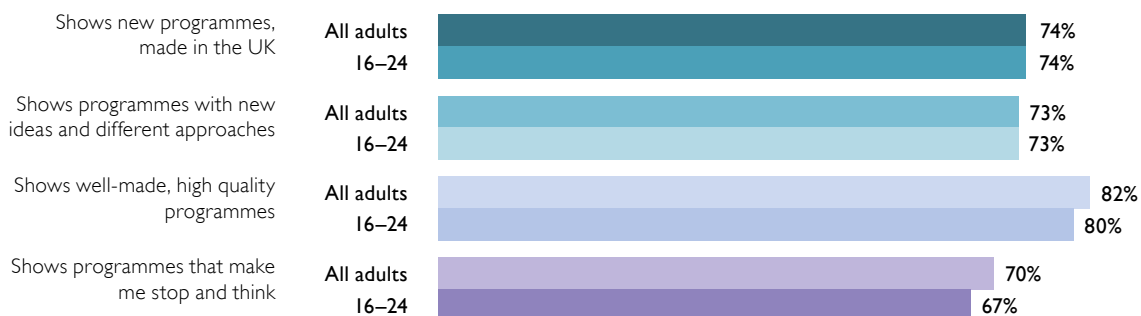
91 Pulse by GfK for the BBC, panel of 20,000 UK adults, quarter 1 2015

3.7.2 We are facing challenges in serving all audience groups

While the BBC's audience performance is very positive overall there are some challenges. Younger and BAME audiences say they value the purposes of PSB, but their consumption of PSB services is falling⁹³. This reflects, in part, fundamental differences in types of consumption, as well as the intensity of competition in these audiences' media landscapes (e.g. the range of specialist channels for BAME audiences).

We should not get this trend out of proportion. 94% of 16-24s use the BBC every week compared with 60% for YouTube and 15% for Netflix.⁹⁴ Yet, as these audience groups move online or to specialist or new entertainment, opportunities to engage with PSB could reduce.⁹⁵ The BBC's proposals for the next Charter are designed to ensure that we remain relevant to these audiences and deliver our remit in new ways.

Importance of PSB characteristics (selected, % rating seven or more out of ten)⁹⁶



Changes in the UK are also affecting expectations of what the BBC needs to deliver to audiences in the Nations and regions. We start from a strong position. In each Nation of the UK 95% of adults consume the BBC each week.⁹⁷ In this Charter period, increases in BBC TV share in Wales, Northern Ireland and Scotland mean that the BBC is moving closer to serving all Nations more equally on TV.⁹⁸ However, performance still differs by Nation.

In Northern Ireland, for example, the contrast between network and local performance is clear. While BBC network services underperform against the UK average, BBC Radio Ulster and Radio Foyle deliver high weekly reach.⁹⁹

In Scotland, time spent across BBC TV and Radio is down less than the UK average.¹⁰⁰ Yet, there is clearly a growing demand for programming that serves the distinctive needs of Scotland and reflects Scottish life better.¹⁰¹

In Wales, BBC network services continue to perform strongly but the provision of local English-language programming across the BBC and ITV has declined at a faster rate than in any other Nation.

93 BARB, based on TV set, total TV average weekly time per head and BBC TV average weekly time per head, 2014/15 indexed on 2010/11. RAJAR, total radio average weekly time per head and BBC Radio average weekly time per head, 2014/15 indexed on 2004/05

94 GfK for the BBC, Cross-Media Insight Survey, c.6,000 UK adults per quarter; BBC average weekly reach 15 mins or more claimed; YouTube and Netflix average weekly reach 3 mins or more claimed, Q1 2015. N.B. YouTube reach varies depending on source; Netflix weekly reach not number of subscribers

95 Ofcom, 'Public Service Content in a Connected Society', December 2014

96 Ofcom, 'PSB Annual Report' 2015, July 2015

97 Cross-Media Insight Survey by GfK, average weekly reach, 2014: Wales 97%, Northern Ireland 95%, Scotland 95%, UK 97%

98 BARB, BBC TV share, 2010/11—2014/15

99 RAJAR, 2014/15

100 BARB, 4+, Scotland and UK, average weekly BBC time per head, 2010/11—2014/15; RAJAR, 15+, Scotland and UK average, average weekly BBC time per head, 2007/08—2014/15

101 Purpose Remit Survey by NatCen Social Research for the BBC Trust, Wales 364, Scotland 359, Northern Ireland 358, England 1,217, autumn 2014

3.7.3 We are committed to doing more to increase diversity and representation on and off screen

The Government's consultation raises the BBC's track record on diversity—one of the suggested values. This is an area where we face challenges.

We have already made some good progress. On screen, we have seen improvements in the portrayal of the Black, Asian and minority ethnic (BAME) community on BBC One and BBC Two. For example, we won four awards at the latest Creative Diversity Network Awards. Across the BBC, portrayal of disabled people on screen doubled between 2012 and 2014. Since September 2014 we have invested over £1.5m out of a new £2.1m Diversity Creative Development Fund on TV projects with talented BAME writers and producers. On air, the Women in Local Radio initiative has seen the number of breakfast shows with female presenters rise from 15% to 49%. The Business in Community campaigns on gender, race and diversity name the BBC as one of the top ten public sector organisations thanks to senior leadership programmes to increase diversity, including the DG's leadership programme and our mentoring scheme. Last year, we opened our doors to young people from the widest range of backgrounds with over 350 trainees and apprentices starting their media careers with us.

We will go further with a new BBC Diversity Strategy for the next five years. For example, we want to work with the independent production sector to reach our targets and ensure diversity is at the forefront of programme-making. We will be arranging a consultation in the autumn, in partnership with PACT, to bring the sector together and explore this further. We aim to introduce new diversity guidelines for our productions in 2016. Earlier this year Ofcom identified that there was an immediate issue with audiences about how public service broadcasting reflected and portrayed British society.

Across the Nations and regions we know that the public want us to do more to portray the full diversity of life in the UK throughout our programmes and services. The UK is changing and it is not straightforward to represent or portray every aspect of British life across all of our services. However, the BBC has a major role to play here, and in the next Charter we will evolve our programmes and services to meet these changing audience demands. We now spend the same proportion on network television in each Nation as their share of the population. But we recognise that spend is not everything—we need to do more, and better, to reflect the lives and experiences of all licence fee payers. During the next Charter, we will remain committed to investing in programming across the UK and ensure that the drama and comedy we produce for BBC One and BBC Two better reflect the diversity of the UK's Nations and regions. As we said in the BBC Strategy Paper, strengthening BBC news provision in Northern Ireland, Scotland and Wales is central to our plans for improving how we serve the Nations in the next Charter. We want to consult audiences across the country on whether we currently have the right balance between UK-wide and Nations news bulletins on television.

The BBC is also fully committed to providing services in the UK's indigenous minority languages. We will continue to work closely with our strategic partners, including S4C, MG ALBA and NI Screen. In response to the growing audience challenges faced by these services, we want to work closely with our partners to move faster online to reach younger, digital audiences. We will use—and share—myBBC technologies to enable more personalised services that can better reflect differing passions and levels of fluency.

While the BBC has made positive steps in terms of diversity and representation, we should still be asking what more can be done.

3.7.4 The BBC is used and trusted worldwide

Globally, the BBC reaches 308m people per week. Of this, the majority (283m) use the BBC's international news services and 39m use services via BBC Worldwide. The BBC has adapted its services to keep pace with changing technology, which is reflected in high and growing reach across all platforms. BBC Global News currently reaches 148m people via TV, 133m on radio and 53m online. Outside the UK, there are also over 4m engaged Facebook users and YouTube viewers of BBC News content.¹⁰²

The BBC is recognised by international audiences as the most trusted global news provider, and also for providing the highest quality news.¹⁰³ Based on the trust and respect it has earned, nearly three-quarters of international BBC News users say that the BBC helps to shape their opinions on important issues.¹⁰⁴ Research conducted by Pew found that the BBC is one of the news sources more likely to be trusted by people across the political spectrum in the USA, illustrating that its impartiality is recognised abroad.¹⁰⁵

3.7.5 We want to enhance the World Service to serve international audiences even better

Britain's media increase its global influence. We came first in a recent ranking of different countries' 'soft power', thanks in large part to the creative industries.¹⁰⁶

One of BBC's public purposes is to 'bring the world to the UK and the UK to the world'. Global users feel that the BBC is a great ambassador for the UK (scoring the BBC at 7.2 out of 10 on this measure)¹⁰⁷. The success of *Doctor Who* (the 50th anniversary special was simulcast to 94 countries) and *Sherlock* (the third series was watched by 77 million people in China) make those brands powerful expressions of British culture and creativity.

The BBC World Service is one of Britain's best sources of cultural influence: out of eight options, 68% of opinion-formers think it does the most to serve the UK's interests around the world, far ahead of the country's diplomats in second place (38%) and its membership of the EU (37%).¹⁰⁸ The World Service was also ranked second by the public, after the armed forces.¹⁰⁹

There is an opportunity to build the authority of BBC World Service to reach half a billion people each year, and strengthen it in parts of the world where there is a democratic deficit in impartial news. We will discuss with Government their interest in investing more in the World Service from outside the licence fee.

102 BBC Global Audience Measure, 2014/15. Engaged users are defined as those that liked or commented on BBC content in the last week and YouTube reach is based on unique users in the last week

103 BBC Global News Brand Tracker by Kantar Media, 4,274 international news users in 10 countries, December 2014

104 BBC Global News Brand Tracker by Kantar Media, 4,274 international news users in 10 countries, December 2014

105 Pew Research Centre, American Trends Panel, March-April 2014. Available at <http://www.journalism.org/2014/10/21/political-polarization-media-habits/>

106 Portland Communications, 'The Soft Power 30, A global ranking of Soft Power', July 2015. Available at <http://softpower30.portland-communications.com/ranking>

107 BBC Global Brand Tracker by Research Now for BBC Worldwide, December 2013

108 YouGov for Chatham House, 704 UK opinion formers, survey conducted July-August 2014 and published January 2015. Available at https://www.chathamhouse.org/sites/files/chathamhouse/field/field_document/20150130Raines.pdf / https://www.chathamhouse.org/sites/files/chathamhouse/field/field_document/20150129YouGovOF.pdf

109 YouGov for Chatham House, 2,059 GB adults 18+, survey conducted August 2014 and published January 2015. Available at https://www.chathamhouse.org/sites/files/chathamhouse/field/field_document/20150129YouGovGP.pdf

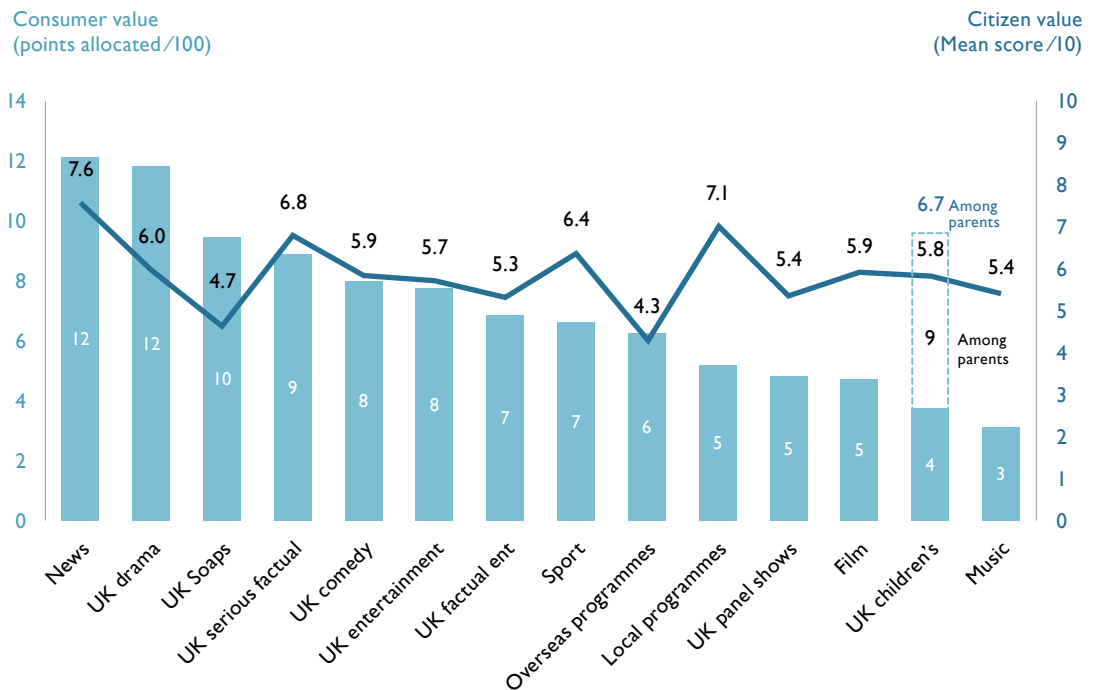
Does the BBC have the right genre mix across its services?

As the Government’s consultation says the BBC’s ‘decisions about genre mix are a critical component for the value it provides to the public’. There is good evidence that, in the view of audiences, we are getting the decisions broadly right. Not only, as we showed in the BBC September Strategy Paper, do audiences feel we fulfil their expectations to be informed, educated and entertained, they also overwhelmingly believe that the BBC “caters for a wide range of tastes”.¹¹⁰

3.8.1 BBC TV offers audiences a wide range of genres and a more balanced mix than competitors

According to research for the BBC by Ipsos MORI people attach significant value as consumers and as citizens to the BBC’s provision of a wide range of genres on TV¹¹¹.

People place value on a range of BBC TV genres



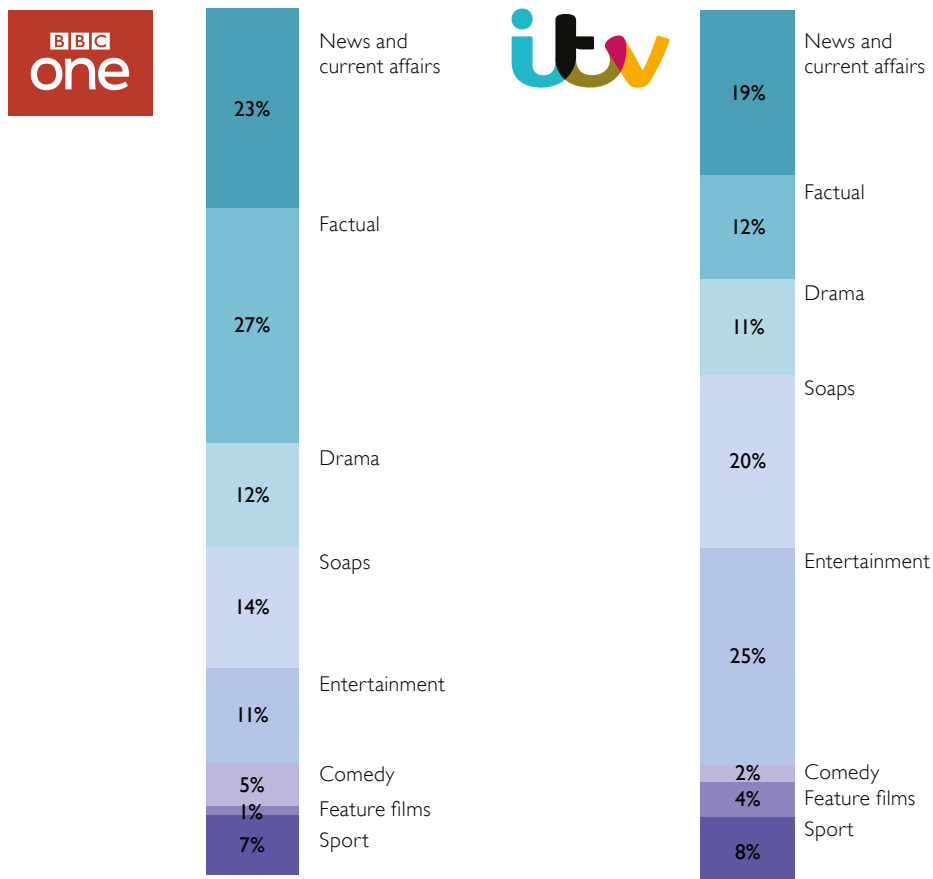
In considering whether we meet these expectations we need to look at the BBC’s actual output. First, the BBC’s services have numerous formal commitments to certain levels of output. These are set and regulated through a combination of Ofcom Tier 2 quotas and Service Licence hours commitments. The BBC has consistently met and often exceeds these commitments. Detailed information on the BBC’s performance is published as part of the BBC’s annual report and accounts¹¹².

¹¹⁰ Kantar Media for the BBC, 1,038 UK households, July-August 2015. 78% of households agree that the BBC “caters for a wide range of tastes.”

¹¹¹ Ipsos MORI for the BBC, 2,118 UK adults 15+, June 2013. Consumer value: ‘Please divide these 100 points between the types of programmes you and your household watch on BBC TV based on the amount you value watching them’; Citizen value: ‘Thinking about the good of society as a whole, how important do you feel it is that the BBC broadcasts each type of programme?’ Please give a score from 1 to 10 where 1 means not important at all and 10 means extremely important

¹¹² Available at <http://downloads.bbc.co.uk/annualreport/pdf/2014-15/bbc-papc-2015.pdf>

Genre mix on BBC One and ITV: peak-time



Second, the BBC offers a more balanced mix of genres than other PSBs¹¹³. Within factual, the BBC's channels offer a richer mix of programmes including a higher level of religion, arts and music. The BBC is the primary broadcaster of new UK children's programming but the focus of our children's output is on the two dedicated channels, CBBC and CBeebies.

Importantly, the public value entertainment programming on the BBC; it is the role that the public most associates with the BBC¹¹⁴. Although the public want entertainment from the BBC, it occupies a significantly smaller proportion of the schedule on

BBC One and BBC Two together than ITV, Channel 4 or Five¹¹⁵. We spend just 2% of the licence fee on TV entertainment programmes.

In addition to the mix of genres for network TV content, the BBC broadcasts significantly more Nations and regions programming to UK audiences than ITV does¹¹⁶ adding to the distinctiveness of the BBC's offer.

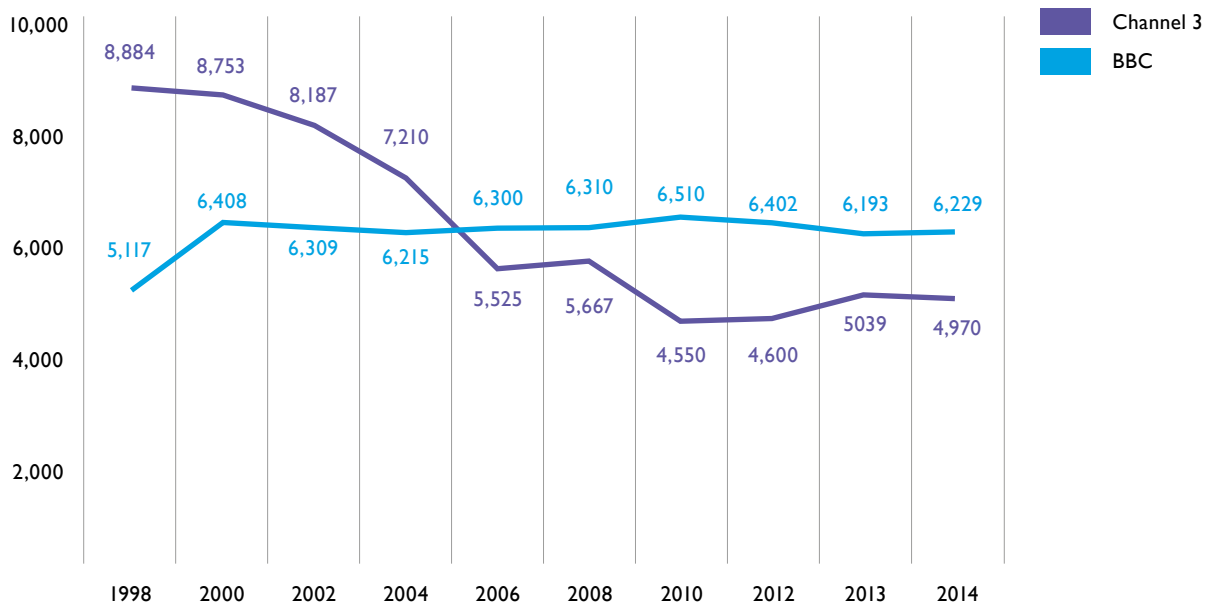
113 Ofcom, 'PSB Annual Report 2015 Output and Spend Annex', July 2015 available here http://stakeholders.ofcom.org.uk/binaries/broadcast/reviews-investigations/psb-review/psb2015/PSB_2015_Output_and_Spend.pdf

114 ICM Unlimited for the BBC, 2,111 UK adults (online), November/December 2014. 64% of people chose 'entertain' as a word to describe what they feel the BBC should do. The next two were 'inform' (59%) and 'educate' (43%).

115 Ofcom, 'PSB Annual Report 2015 Output and Spend Annex', July 2015; Entertainment represents 6% of all hours of output for BBC One and BBC Two. For ITV it is 21%, Channel 4 32% and Five 13%

116 Ofcom, 'PSB Annual Report 2015 Output and Spend Annex', July 2015

PSB first-run UK originations hours; Nations and regions programming



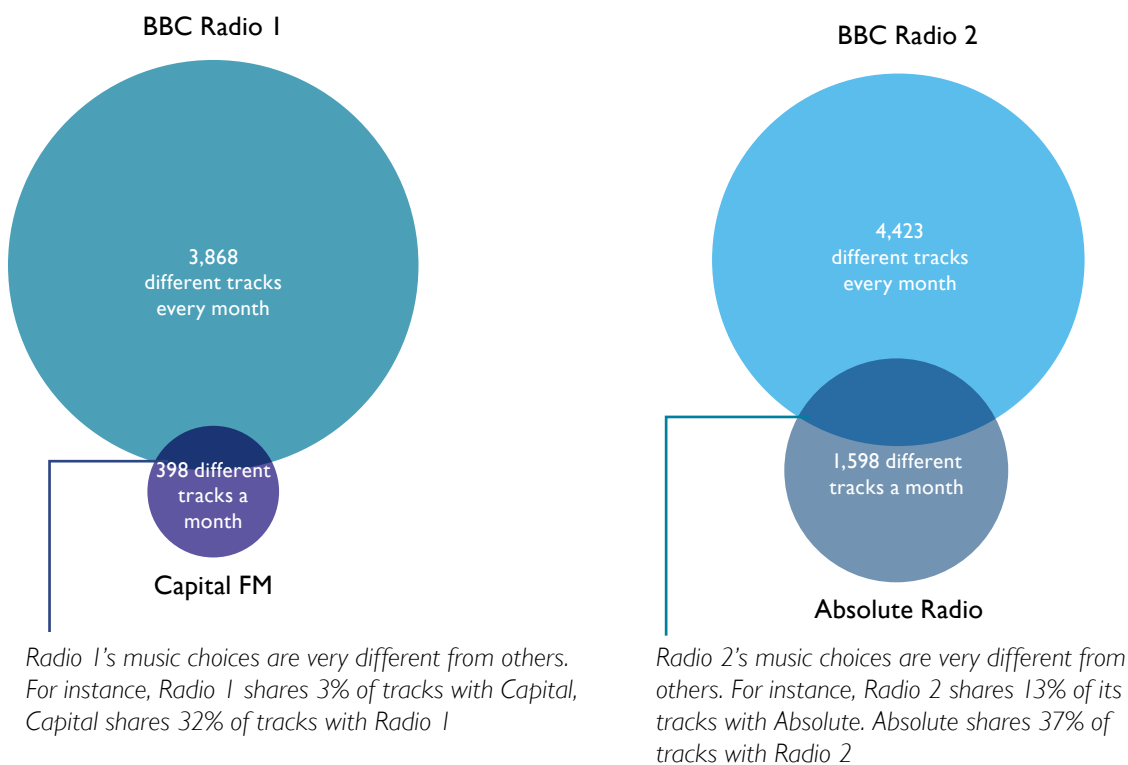
Source: Ofcom. First-run originations only, excluding BBC Alba. Channel 3 figures consist of ITV, STV and UTV.

3.8.2 BBC Radio provides distinctive music and speech programming which is highly valued by audiences

Some of the BBC's radio services are clearly unique. On Radio 4 and 4 Extra the BBC delivers world-class speech programming across a wide variety of genres, from arts, culture, drama and comedy to news, current affairs and documentaries. No other station in the UK covers such a rich range of content with the same depth and quality. 5live is a unique combination of news and sport—75% of the station's output is news, but it also represents 51 different sports (together with 5live sports extra). The BBC Trust's review of speech radio services showed 8 out of 10 listeners are happy with the variety of programmes on offer on BBC speech radio¹¹⁷.

In other cases, where there are commercial competitors, BBC services are distinctive both in offering a wide variety of musical genres and a mix of speech and music. The BBC provides a broader range of music than any other broadcaster. Every year, 50% of any UK music television and radio airplay is only heard on BBC services¹¹⁸. Speech content accounts for a significant portion of airtime on all BBC stations, including our most popular music stations: there is more than 20% speech content on Radio 1 and about 40% on Radio 2.

Each of the stations demonstrates a commitment to a wide range of musical genres and a distinctive approach to new British music. Radio 1, for example, is a champion of new and live music: 65% in daytime is new and 61% by UK artists. Radio 2 plays a greater variety of music than any other radio station in the UK and this includes over 1,100 hours of specialist music programming every year, including Jazz, Folk and Country. Both services play significantly more different tracks every month than their commercial competitors, as illustrated by the comparisons below.

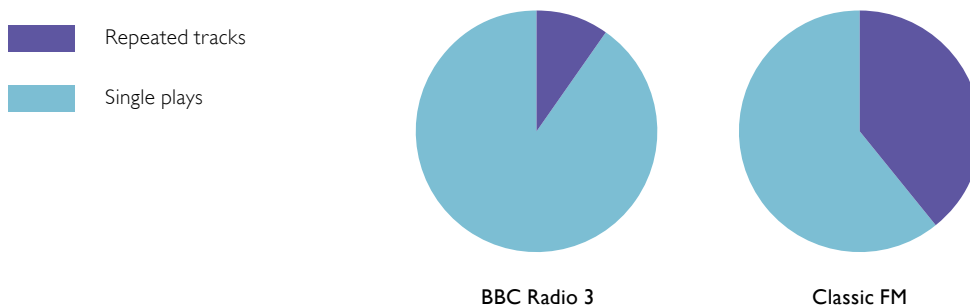


117 BBC Trust, 'Review of Radio 4, Radio 4 Extra, Radio 5 live and Radio 5 live Sports Extra' (2015) available here http://www.bbc.co.uk/bbctrust/our_work/services/radio/service_reviews.html

118 PPL analysis of BBC 2013 airplay

Similarly, Radio 3 offers a far wider range of classical music than other stations. Radio 3 repeats 10% of its tracks every week, while Classic FM repeats 40%. The large majority of music on Classic FM is orchestral; but on Radio 3 60% of pieces played are other types of classical music.

Music output by uniqueness (Radio 3 and Classic FM)

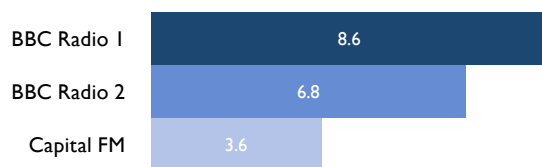


BBC playlists are more open and refreshed, giving greater opportunities to new and UK artists to reach mass audiences. Radio 1 has the largest and most rotated weekly playlist, and is substantially more supportive of new music than competitors such as Capital.

BBC stations feature a greater range of new music and support less familiar artists on their daytime playlists

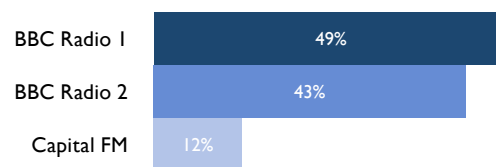
Weekly Playlist adds

Radio 1 and 2 add around twice as many tracks to their playlist each week than are added by Capital FM



% Playlist for artists without Top-10 Single

Radio 1 and 2 are also more supportive of emerging talent



Source: BBC analysis based on weekly published playlists in 2014 for Radio 1, Radio 2 and Capital

Is the BBC's content sufficiently high quality and distinctive from that of other broadcasters? What reforms could improve it?

This section sets out the BBC's view on how distinctiveness should be defined, how distinctive the BBC's services are and where they can be made meaningfully more distinctive. It should be read in conjunction with section 2 of the BBC Strategy Paper.

3.9.1 Distinctiveness should be judged at the level of services, not programmes

The Government's consultation is right to insist that the BBC should be distinctive

The BBC Agreement states that: "The content of the UK Public Services taken as a whole must be high quality, challenging, original, innovative and engaging", closely reflecting Ofcom's characteristics for wider PSB. As discussed at section 3.3 of this document, there is a case for adding 'distinctive' to this list of service characteristics.

Distinctiveness is an important characteristic of the BBC and all its services. It is one of the things that justifies the BBC's public funding. But it can have different meanings for different people, whether they are audiences, broadcasters or policy-makers. In the BBC Strategy Paper, we set out what we mean by distinctiveness and provided evidence to show that the BBC services are distinctive and have become more distinctive.¹¹⁹

Distinctiveness should be judged at the level of services rather than programmes. It does not mean that the BBC should focus on 'market failure' programming or never make a programme that the commercial sector might make. Individual programmes should be judged on their own merit; their quality is not about popularity or uniqueness. It does not make practical sense to say that the BBC should only make a programme if another broadcaster never would. That would mean that when ITV made *Broadchurch*, the BBC would have to stop making *Happy Valley*. Or it would mean that we should stop doing *EastEnders* because ITV does *Coronation Street*. Nor does it make creative sense. The BBC should not start with a gap in the market, and try to fill it. It should start with its public remit and the creative idea and then deliver programmes that fulfil them.

The fact that the BBC makes some of the same types of programmes as the commercial sector means there is 'competition for quality' that benefits all sides and audiences. The test should be that every BBC programme aspires to be the best in that genre, and that overall the range of programmes in every BBC service should be clearly distinguishable from its commercial competitors. In order to serve licence fee payers efficiently, BBC services should also be distinctive from each other.

Any framework for defining and assessing the distinctiveness of BBC services should, therefore, include four key criteria:

- **Creative and editorial ambition**—the licence fee gives the BBC freedom to take creative risks and deliver services that are high quality, challenging, innovative and engaging;
- **High editorial standards**—meeting the public's high expectations of fairness, accuracy and impartiality;
- **Range and Depth**—providing a wide range of genres and the best programmes in each genre, in order to serve all licence fee payers; and
- **High level of first-run UK originated content and supporting home-grown ideas and talent.**

We would welcome a dialogue with the Government on how to best define and assess distinctiveness.

¹¹⁹ BBC, 'British Bold Creative, The BBC's programmes and services in the next Charter,' September 2015, Section 2.1.

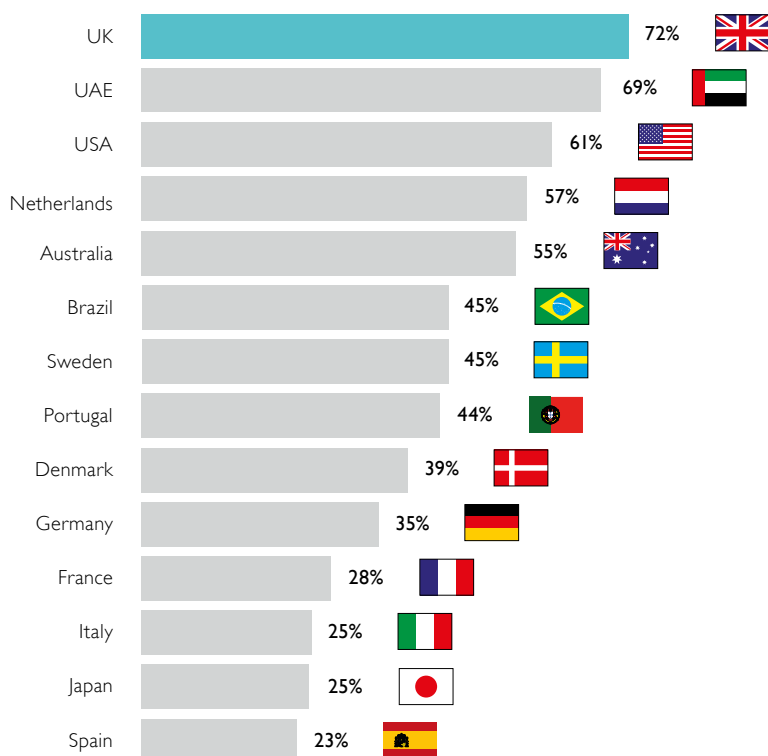
3.9.2 A comparison against competitors shows that the BBC's services are distinctive

We have measured all the BBC's public services against their competitors and set out the results in September¹²⁰. Overall the BBC's services are more distinctive than they have ever been. For example, 30 years ago, a fifth of BBC One's peak-time schedule consisted of foreign series like *Dallas*, *The Rockford Files* and *Kojak*. Today it is zero. Many services, through the process of BBC Trust service licence reviews, have become more distinctive during this Charter. The BBC Strategy Paper sets out plans for how the BBC's services could become even more distinctive in the next Charter.

3.9.3 The UK is a global leader and the BBC sets standards

Populus undertook an international study asking people from around the world to rate their country's overall TV output on quality and then to rate the quality of each of the biggest channels in their country. The UK emerged as the global leader on overall TV quality, with 72% of UK adults saying TV programmes overall in the UK are good quality—the highest out of the 14 surveyed countries¹²¹.

Perceptions of overall TV quality per country rated by respondents in the country (% Very / fairly good quality)

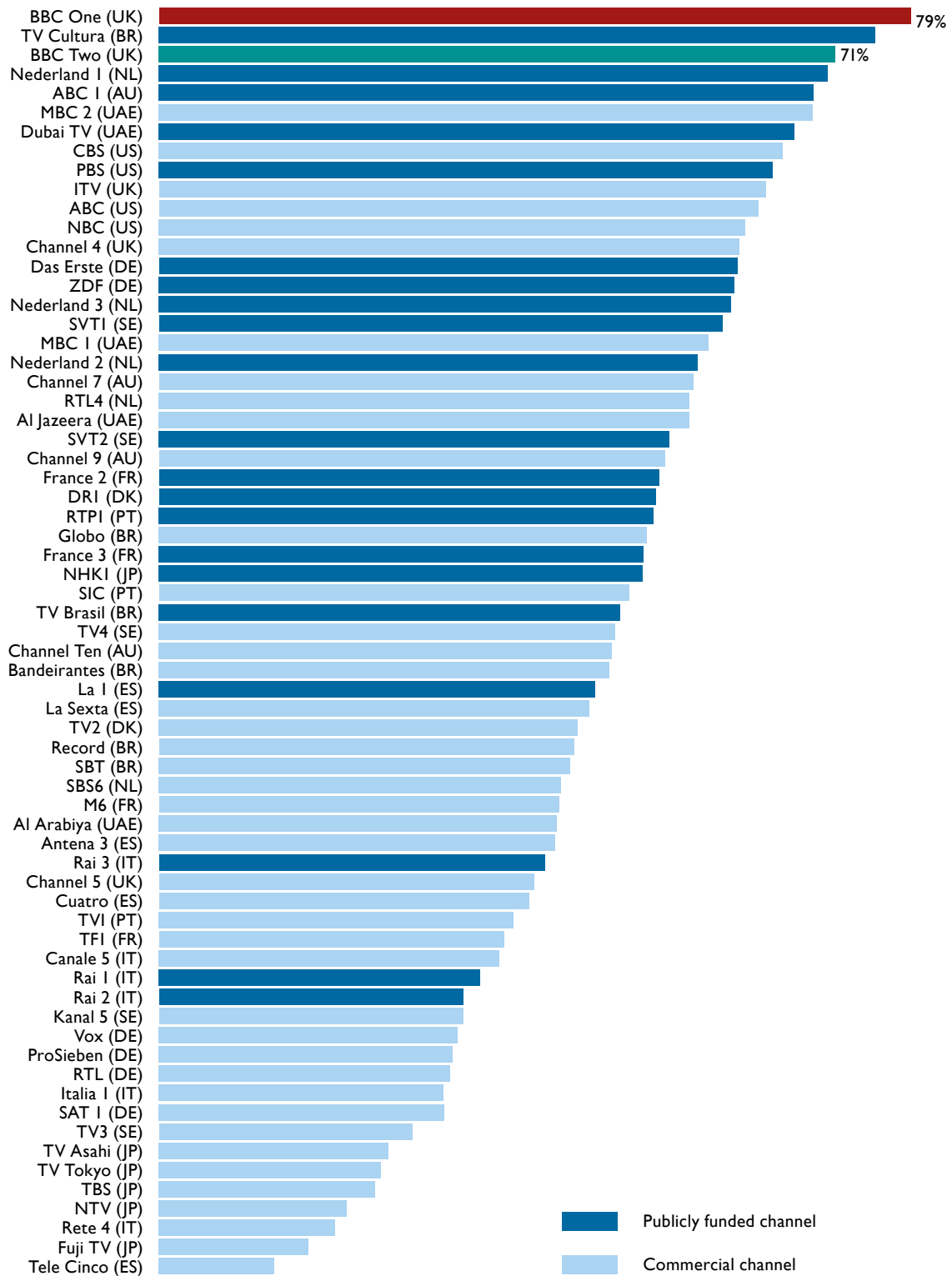


Out of 66 channels, BBC One received the highest quality score of all—with 79% of UK adults rating it as good quality—while BBC Two came in close behind in third place.

¹²⁰ BBC, 'British Bold Creative, The BBC's programmes and services in the next Charter,' September 2015, Section 2.2

¹²¹ Populus survey for the BBC, conducted September–October 2013 in 14 countries (representative sample of 500 adults 18+ per country). Survey question: 'What do you think of the quality of television programmes overall in [INSERT COUNTRY NAME]?'

Perceptions of TV channel quality per country rated by respondents in the country¹²²
 (% Very / fairly good quality)



¹²² Populus survey for the BBC, conducted September-October 2013 in 14 countries (representative sample of 500 adults 18+ per country). Survey question: 'To what extent do you think the quality of programmes on the following television channels in [INSERT COUNTRY NAME] is good or poor?'

How should the system of content production be improved through the reform of quotas or more radical options?

The Government's consultation paper sets out three options for changing the BBC's content production arrangements: amending the existing supply quotas, scaling back in-house production, or the BBC Studios proposal. The BBC believes that only the BBC Studios proposal can deliver these key policy objectives: the best programmes on-screen and the secure supply of a range of high quality British content for audiences; a sustainable and diverse UK production sector; and long term value for licence fee payers. We believe these policy objectives are best met through promoting greater competition between the BBC and external producers, not by quotas and guarantees that restrict competition and restrict the best ideas being commissioned. Our proposal to end in-house guarantee and create BBC Studios is designed to do this.

The alternative options would have the reverse effect: they would undermine one of the world's greatest programme makers and so reduce the level of competition in the UK supply market, as well as the flow of value to licence fee payers.

It is important that the options for reforming the BBC's content supply arrangements are considered in the context of the overall policy and regulatory framework for the sector, including the 25% independent quota and the Terms of Trade. We will, therefore, engage with Ofcom's forthcoming review.

3.10.1 The BBC's mixed model of supply delivers important audience, creative and economic benefits

Today, the BBC's content supply framework requires that it commission 50% of network programme hours from BBC production, 25% from qualifying independents, and the remaining 25% from any supplier, through the Window of Creative Competition (WoCC).¹²³ In 2014, the BBC sourced 56% of its programmes from BBC production, and 44% from the wider market, spending over £400m with external suppliers.¹²⁴

This mixed model has worked well for audiences and for the market. Both in-house and external suppliers compete to deliver high quality programmes at good value for money. Both attract revenue from commercial investment and content sales—helping programmes like *Life Story* and *Wolf Hall* get made. The scale and diversity of the market—with over 500

companies ranging from micro businesses to global conglomerates¹²⁵—ensures a breadth of treatments and perspectives, while exposure to other broadcasters and media companies in the UK and internationally helps drive innovation and the flow of ideas around the sector. Any model of content supply needs to maintain the ability of commissioners to choose ideas from a diverse and vibrant external production sector, while ensuring that the framework within which those choices are made is fit for purpose in a changing market.

¹²³ <http://www.bbc.co.uk/commissioning/tv/articles/who-we-are-how-we-commission#quotas>

¹²⁴ BBC internal figures based on eligible network television spend, excluding News.

¹²⁵ Based on estimates in Pact's Independent Production Sector Financial Census 2015

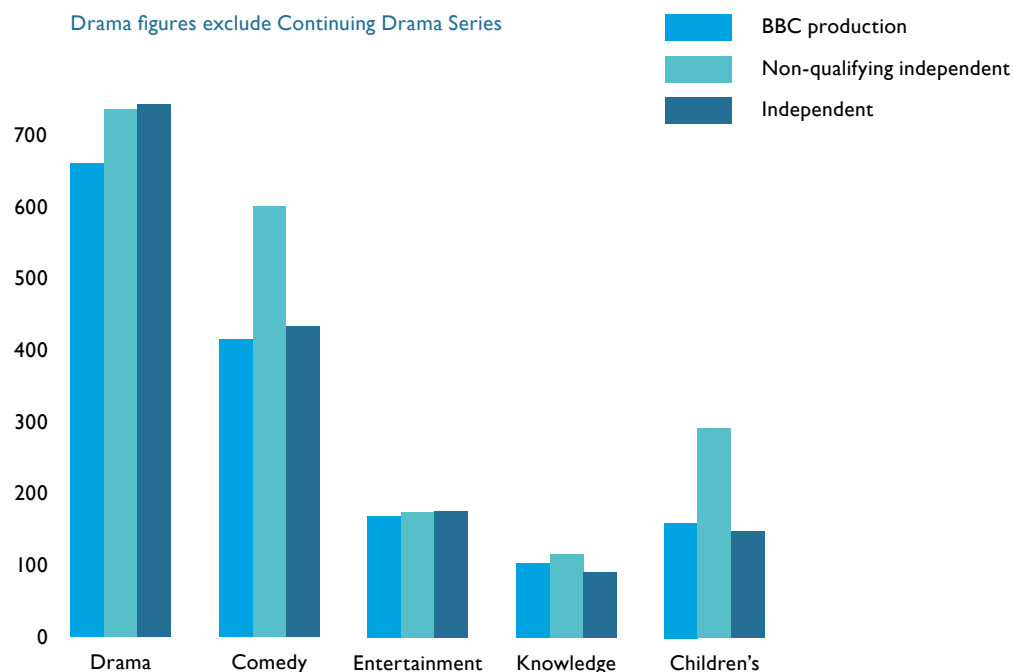
3.10.2 BBC production plays a critical and distinctive role in this mixed model

BBC production keeps programme-making at the heart of the BBC's mission. It ensures a deep and constant relationship with programme makers that encourages creativity and innovation. It offers an unrivalled range and depth of expertise and experience across every specialism, a commitment to making programmes across the Nations and regions of the UK, and the highest standards of training and production craft. It provides the BBC's only source of wholly-owned intellectual property rights, which offers security of supply and generates financial returns that can be re-invested into content.

The critical mass of in-house programming also provides the foundation for launching digital innovations like the iPlayer and BBC Store.

The Government's consultation paper notes that "the regulatory framework for the BBC's supply of content affects the efficiency with which the licence fee is spent".¹²⁶ It also raises the question of whether BBC production delivers value for money compared to independent producers, in light of the external sector's increasing share of the WoCC. However, the fact that hundreds of production companies in the UK collectively win a greater share of commissions in the WoCC than BBC production is not evidence of greater value for money but of a highly competitive and creatively buoyant market. BBC production's share of the WoCC has held relatively stable overall since its introduction.¹²⁷ Analysis of commissioning prices suggests that the cost to the licence fee payer for comparable programmes is similar whether from BBC production or external producers.

Commissioning cost per hour for BBC programmes, 2013/14 (£000s)



Source: BBC internal data supplied to BBC Trust

¹²⁶ DCMS 'BBC Charter Review: public consultation', July 2015, p.40

¹²⁷ BBC Trust 'Review of BBC content supply arrangements', June 2015, p.24 available at http://downloads.bbc.co.uk/bbctrust/assets/files/pdf/our_work/content_supply/2015/content_supply_review.pdf

More importantly, an assessment of value for money must go beyond the initial commission. When BBC Worldwide generates secondary revenues from in-house programmes the BBC Group retains 100% of the net profit, compared to typically 15% where programmes are made and exploited by external suppliers. Titles such as *Doctor Who*, *Strictly Come Dancing*, *Frozen Planet* and many more are valuable to licence fee payers not simply because they are great

shows, but because they were made in-house, giving the BBC the greatest flexibility in promoting and exploiting them in the UK and around the world. The contract with BBC production is central to BBC Worldwide's business model, enabling it to build channels and brands and compete globally on behalf of the UK. The value of this activity is returned to licence fee payers and the UK creative industries through reinvestment in content.¹²⁸

¹²⁸ BBC Worldwide invested £94.4m in BBC-commissioned content in 2014/15, BBC Annual Report and Accounts, p.131

BBC production provides distinct benefits to the BBC

All suppliers deliver important benefits...

	BBC Production	The UK production sector
Produce high-quality programmes	Average AI (programme quality) score of 83	Average AI (programme quality) score of 83
Cover a range of genres and specialisms	Range in one entity concentration of specialisms	Range across many companies breadth of choice
Deliver programmes at a fair price	£129,000 Average price per hour for in-house programmes	£139,000 Average price per hour for indie programmes
Attract commercial investment to contribute to programme costs	15% 3rd party upfront contribution to total funding	14% 3rd party upfront contribution to total funding
Generate returns to the creative industries through secondary exploitation	15–20% of total revenues* generated from secondary sales	15–20% of total revenues* generated from secondary sales

...but BBC production plays a unique role

A single entity focused on the BBC's public mission	1 entity of scale, enabling coordinated focus on BBC priorities	500+ companies with variety of incentives, objectives and priorities
Operated on behalf of the British public in a global content market	100% UK-owned	59% owned by international groups
Sustainable support for Nations & Regions production ecologies	58% of spend on BBC Production is outside London across seven bases	46% of BBC spend on external suppliers is outside London often on single projects
Maximising BBC control and flexibility over use of content	Transmission use and future rights use in perpetuity , allowing for innovation in services	UK licence for 5 years . Rights use beyond Terms of Trade requires negotiation and extra payment
A pipeline of wholly-owned IP to generate secondary value for the licence fee payer	100% of net profits, allowing it to generate maximum return for licence fee payers	BBC Group typically receives 15% of net profits, reducing the returns to licence fee payers

* BBC production figure based on net secondary revenues generated via BBC Worldwide from in-house content. Production sector figure based on UK and international programme sales and other exploitation revenues.

3.10.3 Consolidation and globalisation is changing the supply market

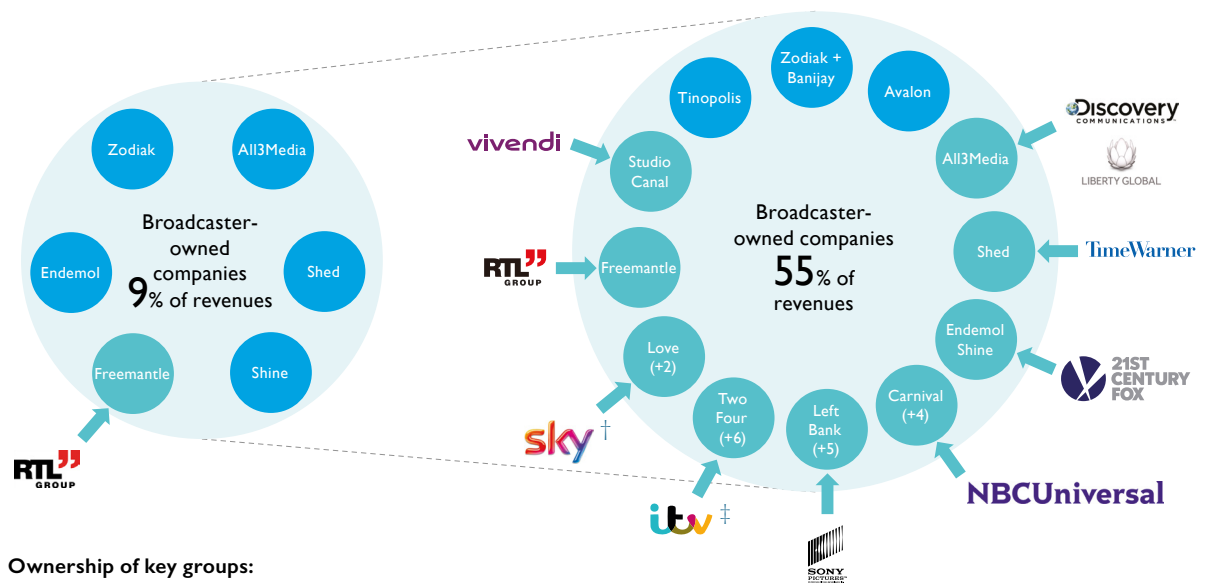
The content production sector is changing. In a global and digital media market, more providers are competing for viewers on more platforms across more distribution windows. Access to content and ownership of IP rights are now vital strategic assets for organisations seeking to differentiate themselves and capture value which has become increasingly fragmented.

Broadcasters and global studios have responded by driving up in-house content investment and by acquiring production companies, to the point where over 50% of the UK 'independent' sector's revenues are now generated by companies owned by broadcasters.

The changing nature of the UK production sector over the last ten years

The UK independent production sector in 2003
£1.3bn total revenues*

The UK 'independent' production sector today
£2.3bn total revenues*



Ownership of key groups:

- Independent
- Broadcaster-owned

Source: Broadcast; company accounts; BBC analysis

Notes:

- * Total excludes revenues from companies' overseas operations;
- † Numbers in brackets indicate number of other UK production companies owned by the broadcaster;
- ‡ Revenues of UK indies acquired by ITV Studios included in total sector revenues; other ITV Studios revenues excluded

These developments have brought benefits: investment into the UK creative industries; stronger, more sustainable companies; and a bigger market for those producers to play into.

But they also raise new challenges to the UK supply model. Ofcom's third review of Public Service Broadcasting noted that *"There is a growing risk that consolidated companies focus on the most commercially attractive genres, leading to a lack of innovation in the less commercially attractive genres."*¹²⁹ As audience demand evolves, some content needs, such as premium drama, are well served by the global English language production sector; but in other areas supply may become weaker or less effective. It may become harder for PSBs to access the most desirable content for their audiences at an affordable price. Ofcom, again, notes that *"there is the potential risk that greater vertical integration between broadcasters and production companies could reduce the number of companies competing for PSB commissions and so limit commissioner choice, particularly in genres which can achieve substantial international revenues."*

A strong BBC-owned source of supply is vital to ensuring choice and competition. If we want to continue to create great programmes and experiences for audiences, we need to be able to choose the best ideas—from inside the BBC and outside. We rely on the wider sector for some of our best-loved programmes. But we also need to keep the BBC itself as one of the world's great programme-makers to ensure proper competition and real choice. This is what motivates our proposal to create BBC Studios.

Under the current arrangements, BBC production faces growing challenges. Its unique set-up, with a level of guaranteed business, has protected areas of specialism but prevented it from supplying to other broadcasters. BBC programme-makers can only offer their ideas to one customer—the BBC—and if they lose commissions they cannot make up business elsewhere. BBC production is finding it harder to attract and retain the very best talent, who sometimes feel that the independent sector offers them greater creative freedom and a fairer share of reward for their success. These challenges are making it a less effective source of competition and choice for the BBC, and so major change is needed to secure its long-term creative health.

129 Ofcom, 'Public Service Broadcasting in the Internet Age', July 2015, p10

3.10.4 BBC Studios is the best option to secure the supply of original UK content, create long-term value and stimulate the UK production sector

The BBC has announced its proposed strategy for reforming its content supply arrangements. The details of the BBC Studios proposal are set out in the recent publication “BBC Studios: Strengthening the BBC’s role in the creative industries”.¹³⁰ The proposal is designed to secure the long-term creative health of the BBC’s production unit by giving it greater freedom to operate in a growing global market. It is designed to stimulate the sector with more competition, and give commissioners greater freedom to choose the best ideas for audiences—whether from the BBC or external producers. This will involve two major changes to the BBC’s existing supply model:

- Opening around 80%¹³¹ of the BBC’s network slate to competition from all suppliers in a typical year by removing the guarantee for BBC production across the genres included in this proposal; and
- Transforming the majority of BBC production into BBC Studios, a wholly-owned commercial subsidiary of the BBC Group producing programmes for the BBC and other broadcasters in the UK and internationally.

BBC Studios will have the values and quality of the BBC—a mission to inspire audiences at home and around the world with bold British creativity. It will find and nurture the next generation of British on-screen and back-stage talent in drama, comedy, science, natural history—and more. It will be distinctive in the market. It will delight in range and specialism, making the full range of genres and not just those with the most commercial appeal. It will operate across the UK. It will ensure the full value of BBC-made content is returned to the licence fee payer.

This is a pro-competitive move that should have a positive impact on the market overall. Removing the in-house guarantee for the genres that move into BBC Studios would over time make £250–300m of additional commissioning spend open to competition.¹³² Based on its current business, BBC Studios would have total revenues of around £400m at

launch (comprising primary revenues and co-production and upfront investment), and would have a share of below 15% of total UK commissioning spend.¹³³ This would make it one of the largest producers by UK revenues, but not a dominant player. When international and secondary income is factored in, ITV Studios has total global revenues of almost a billion pounds, and FremantleMedia and Endemol-Shine of well over a billion. The parent companies of some leading UK producers are even larger: 21st Century Fox has a global turnover of £19bn, Time Warner of £18bn, and Liberty Global of £12bn.¹³⁴ In addition, BBC Studios would be focused on supplying the BBC and would be expected to gain only a modest share of commissioning spend from other broadcasters.

The Government’s consultation paper mentions concerns raised about the market impact of BBC Studios and the risk of infringing state aid law.

The proposals are designed to fully comply with UK and EU state aid and competition law, and the BBC’s Fair Trading frameworks. This is not a new issue for the BBC—we have well-used and understood ways of making sure that commercial subsidiaries can operate without cross-subsidy or market distortion. To ensure compliance, our approach will adhere to the following core principles:

- No cross-subsidy from the public service to BBC Studios, ensuring that there is no use of the licence fee to subsidise the costs or inflate the prices paid to BBC Studios;
- Demonstrable separation between the management, finances and operations of BBC public service and the new BBC Studios so that BBC Studios does not gain any unfair advantage in the market as a result of its links to the BBC;
- Arm’s length commissioning, with any commissions offered to BBC Studios by the BBC subject to the same range of tariffs and terms as are available to external producers.

¹³⁰ Available at http://downloads.bbc.co.uk/aboutthebbc/reports/pdf/bbc_studios_2015.pdf

¹³¹ Based on retaining an in-house guarantee for those genres remaining within the Public Service (Children’s, Current Affairs and Sport), equating to approximately 20% of the BBC’s network slate in a typical year

¹³² This represents the approximate value of business currently guaranteed to BBC production that would in future be contestable; the precise figure will depend on BBC funding and commissioning slates when changes come into effect

¹³³ Based on BBC Studios’ projected share of total spend on original content by UK commissioners (PSB and multichannel); data from Ofcom and the BBC

¹³⁴ Revenue figures based on latest available company reports and internal data

The separate Studios paper sets out the mechanisms that will be in place to deliver these requirements. In addition to the ex-ante approval process by the BBC Trust and the BBC's Fair Trading Policy, we are proposing a periodic ex-post review of the new arrangements. This could be conducted through an external regulatory process, with the first to begin within 12–24 months of operation. The exact scope of the review should be defined at the appropriate time by the regulator, but it could look at pricing, range of commissioning opportunities available, and access to commissioning, as well as recommending changes if the new arrangements are not ensuring fair treatment and working in the interests of licence fee payers.

3.10.5 Directly scaling back in-house production would risk damaging the UK creative economy

The Government's consultation paper states that: *"There is... a need to consider the extent to which the BBC needs to operate as the country's largest single content provider"* and questions *"whether there are arguments for scaling back the BBC's production capabilities."* It is not made clear what this would entail or what the likely benefits would be for licence fee payers. For the purpose of responding, we assume that a spectrum of policy options may be under consideration, ranging from limiting the BBC's production capabilities to certain genres to dismantling the BBC's production capability entirely and moving to a 'publisher-broadcaster' model.

As set out above, there is no evidence of a lack of creativity or efficiency in BBC production that would justify directly scaling it back. To artificially constrain one of the world's greatest programme-makers would mean fewer ideas for commissioners and less revenue for the BBC to reinvest in content for licence fee payers. It would reduce rather than expand the level of competition and choice in the UK supply market. Rather than prescribing the size of BBC production, a level playing field and competition—as proposed under the BBC Studios model—would mean its size would be determined by how many ideas are commissioned.

The consequences of restricting competition and choice by scaling back BBC production would be as follows.

First, the supply of high-quality public service content for UK audiences would likely diminish. Without a production unit as part of the Group, the BBC would become wholly reliant on negotiations with external suppliers to secure all its content. Although there is no widespread evidence today that the BBC is struggling to access the content it needs from the market, as we

saw earlier, Ofcom has set out the risks: that as trade ownership and vertical integration increases, producers in the more commercial genres may choose not to bring their best ideas to the BBC; or alternatively that the BBC would have to pay artificially high prices to secure the quality of ideas it needs. BBC production's scale and public service remit allows it to commit to the full range of genres and specialisms, and promote cross-fertilisation between them, in a way that most suppliers cannot. The BBC Studios proposal would aim to preserve these benefits.

Second, this option would result in a less vibrant UK production ecology. Owning a production unit of scale focused on the BBC's mission and values has enabled the BBC to make long-term investments for the benefit of the sector. These include BBC production's creative hubs in the Nations and regions of the UK, its commitment to production standards and training, and its focus on nurturing new home-grown talent. Although the rest of the market plays an important role in all these areas, there is a risk that diminishing BBC production would reduce the overall focus on UK skills and talent. In the long term this could, in turn, reduce the attractiveness of the sector to inward investment.

Finally, it would risk reducing the overall value that the BBC delivers to licence fee payers and the creative economy. The BBC Studios proposals are predicated on the growing importance of IP ownership in a more global, digital market. Scaling back BBC production would take the BBC in the opposite direction. The BBC would no longer own the rights to new content, reducing its ability to innovate. It would also generate significantly less commercial revenue via BBC Worldwide for re-investment in programming.

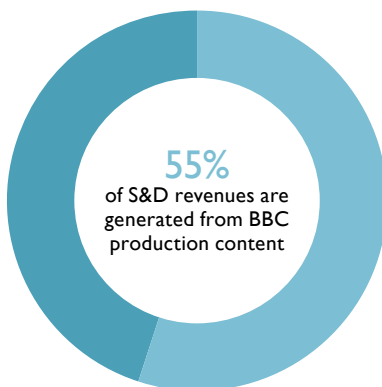
3.10.6 A smaller BBC production unit would have a significant impact on BBC Worldwide's business model

BBC Worldwide works with many suppliers, but it is the stable supply of content from BBC production that defines it as a business. Around 80% of BBC Worldwide's profits and 60% of its revenues are generated from the exploitation of BBC in-house content. It obtains the rights to this content by investing in it at market rates, and partners, customers and audiences in turn come to BBC Worldwide because they know it is the home of programmes commissioned by the BBC. The critical mass of content from BBC production underwrites the scale

and ambition of its activities across sales and distribution, channels and consumer products. BBC Worldwide is only able to use the BBC brand on its international channels and platforms (like BBC Earth and BBC First) if more than 50% of the content on them is commissioned by the BBC. Many of its partnerships rely on supplying a certain volume of BBC content. (See section 3.14 for further detail on how the relationship between BBC production and BBC Worldwide delivers important benefits to licence fee payers.)

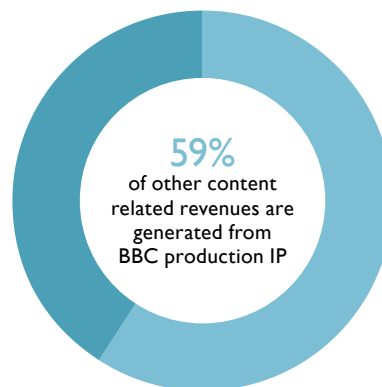
The scale of supply from BBC production is central to BBC Worldwide's business lines—and therefore to its ability to compete globally on behalf of the UK's creative industries

SALES & DISTRIBUTION¹



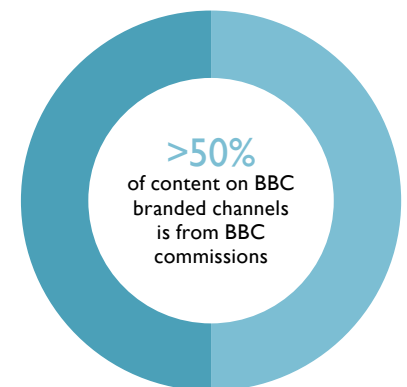
This allows BBC Worldwide to bring the best of Britain to the world. 700 international buyers attended BBCW's Showcase event in Liverpool in 2015

OTHER CONTENT-RELATED REVENUES²



BBC Worldwide does business in over 200 territories around the world helping to bring the UK's creativity to the world

JOINT VENTURES AND CHANNELS



Supply from BBC production underpins BBC Worldwide's ability to operate over 40 channel feeds in over 120 territories, bringing the UK's creative industries direct to global audiences

¹ TV & VOD sales

² Includes DVD, DTO, Merchandising, Live Events, Other.

If BBC production were diminished or dismantled, BBC Worldwide would lose access to its biggest source of content. Crucially, BBC Worldwide's ability to respond by replacing its major contract with BBC production with an alternative source of content is very limited. Although BBC Worldwide is already active in seeking to acquire content from independent producers, the increasingly consolidated supply market means that a majority of commercially valuable BBC-commissioned content is tied up in the distribution arms of vertically integrated producers.

In this scenario we would therefore see a severe risk of decline in BBC Worldwide's business. In the

short-term, the channel joint ventures that it operates in the UK and internationally would be put at risk, since these rely on a minimum threshold of BBC content. In the medium-term, the value of its content sales catalogue in key markets would decline as the flow of new content diminished and it became increasingly reliant on library titles.

This would, in turn, have a significant impact on the value that the BBC can generate for licence fee payers and the wider industry. A dramatic contraction in BBC Worldwide's business would mean lower returns to the BBC for reinvestment in public service content.

3.10.7 Reducing the in-house guarantee without creating BBC Studios would likely result in similar risks in the longer term

The Government's consultation paper proposed a number of possible policy changes under the option of 'amending existing quotas'. It notes that it "would be particularly interested in views on whether to lower the in-house guarantee." We focus on this first and address the other proposed changes below.

The changing market is putting direct pressure on the regulatory framework, with the result that the present system of quotas is no longer fit for purpose. The BBC has proposed two main changes to address this:

- To remove the in-house guarantee and WoCC for the genres that will become part of BBC Studios, if the proposal to launch BBC Studios¹³⁵ as a commercial entity is approved. This will make up to 80% of the BBC's overall network commissioning schedule open to competition in a typical year¹³⁶, increasing the opportunity for external suppliers;
- To preserve the overall 25% independent quota but remove the separate independent quotas for BBC One and BBC Two as part of Charter Review, since as independent producers continue to lose their qualifying status through acquisition, it is becoming harder to meet numerous targets without compromising commissioning decisions.

Importantly, the BBC's proposals for content supply are a package. The BBC does not believe that it can deliver against the policy objectives, outlined above, if BBC Studios is unable to operate in the market. In particular, the policy option of reducing the in-house guarantee by increasing the WoCC or independent quota, while not launching BBC Studios, would have a number of negative consequences.

The challenges that BBC production faces today in a more competitive global market, in particular in retaining talent, would be exacerbated by a reduction in creative opportunity. With a lower guarantee and no opportunity to make programmes for other broadcasters, the range and volume of content produced by BBC production would shrink, especially in the more competitive genres such as drama and entertainment. As in the scenario above, this is likely to have a negative impact on BBC Worldwide's business model by reducing the pipeline of content. Although the impact would not be as sudden as in a publisher-broadcaster scenario, this option would materially reduce the BBC's return on its content investment.

In addition, a BBC production entity with no real opportunity for growth would require the BBC to make tough choices about what programmes and activity to prioritise for the remaining in-house guarantee. It would be very difficult to sustain the depth of specialism, range of genres, pan-UK presence and commitment to training and standards that BBC production has today. As with the option above, this would risk damaging the production ecology of the UK and the diversity of British content. At the same time, retaining an in-house guarantee at a lower level would do less to increase competition than the BBC's proposal to remove the in-house guarantee altogether for Drama, Comedy, Entertainment and Factual programmes.

¹³⁵ Network Drama, Comedy, Factual and Entertainment

¹³⁶ Based on retaining a guarantee for those areas remaining in-house (Children's, Sport, Current Affairs). The removal of the guarantee for the genres becoming part of BBC Studios makes an additional 30% of the slate open to competition in addition to the 50% already contestable today.

3.10.8 Other proposals for amending quotas would not deliver additional benefits to audiences, licence fee payers or the creative economy

The Government's consultation paper proposes a number of other options for amending quotas. These include: expanding the independent quota or WoCC for radio content; expanding the independent quota or introducing a WoCC for online content; reviewing the arrangements for regional production; or assessing quotas by value rather than hours. As set out above, the BBC wants solutions that expand competition rather than guarantees or quotas.

Television quotas

Regarding regional production quotas, the existing targets for out of London and Nations spending have already led the BBC to spend more than 50% of network television budgets across the Nations and regions of the UK.¹³⁷ The BBC also has a commitment to ensure there are appropriate opportunities for competition between in-house and external producers for the provision of local (non-network) television programmes, which by definition are made in the Nations and regions. The BBC Trust confirmed in its recent review of the BBC's content supply arrangements that the BBC has met all targets and obligations to date.¹³⁸ The BBC's matrix of production quotas already requires complex management; introducing new quotas is likely to hamper creative decisions and increase administrative burdens. In the BBC's view there is no clear evidence of market failure or issues for the sector that would require the introduction of further corrective quotas.

Assessing quotas by value rather than by hours for television content could in fact result in a smaller share of the schedules being available to external suppliers than today, since the value of programming in the WoCC and independent quota tends to be slightly higher on average than that commissioned within the in-house guarantee. The BBC does not, therefore, see any merit in pursuing this policy.

Online quotas

Today, the BBC makes significant use of third parties to provide content for BBC Online. We currently have a quota for external spend of 25% and a clear approach to the procurement of both technical and editorial activity from the market. This approach has been developed and improved over a number of years and has been very successful in bringing innovation into BBC Online and ensuring we support the broader market. Last year c.30% of Online spend was with third parties.

We are keen to do more to support the broader market in the next Charter period. However, there are good reasons why expanding the quotas for independent production to online would be inappropriate. First, while the BBC is a large player in the UK TV and Radio production markets, we are a relatively small player in a rapidly growing and increasingly global online market. The issue of the PSBs' buying and negotiating power that led to the introduction of 25% indie quota and terms of trade in TV sector do not apply in this sector. Second, there is no common unit of measurement for online content equivalent to the 'programmes' used for the TV quotas. Third, BBC Online activity encompasses both technical and editorial activities and much activity is co-dependent—where technical activity develops in light of editorial use and vice versa.

As part of our 'compete or compare' strategy, we believe the better policy solution is to maximise the volume of competition and choice in editorial output. We will aim for 60–70% of online content spend (i.e. almost all non-news and non-sport spend) to be open for competition by the end of the next Charter period. The licence fee has helped create a world-beating TV production sector and there is an opportunity to help do the same for online and connected content.

¹³⁷ In 2013 the BBC spent 52.5% of its TV network programming budget outside London, compared to 45.8% in 2012. Review of BBC content supply arrangements, BBC Trust, June 2015, p.55

¹³⁸ Review of BBC content supply arrangements, BBC Trust, June 2015, p.16

Radio quotas

The BBC has developed a reform programme which we have agreed with the industry. Our proposals are subject to approval from the BBC Trust. BBC Radio is the largest single supporter of the independent production sector for radio in the UK. It is responsible for over 95% of the radio indies' revenues for broadcast output. The BBC's support for independent production has grown over the years, from a minimum 10% quota for independent production in 1992, to an additional 10% Window of Creative Competition (WoCC) for Radio 4 in 2007. The WoCC was extended to all network output in 2012/13 after a BBC Trust review of Content Supply in 2010.

So far, independent radio producers have performed well in the Radio WoCC, winning 75% of the hours available in 2013/14 and 80% of available hours in 2012/13. Despite this, the view of the BBC Trust is that it would be premature to judge the success of the WoCC as it is at such an early stage. It is also clear that the WoCC has not resulted in significant change in the independent radio production market. Given that independent radio production remains a small market, the BBC Trust concluded in its 2015 Review of Content Supply that any proposals to reform radio content supply would focus on potential benefits to licence fee payers of opening up the BBC to competition, "rather than as a response to any market imperative".¹³⁹

To that end, we are now proposing a radical new approach. We will open up around 60% of eligible network radio hours to competition from independent companies within six years—triple the current total of 20%.

This means that the amount of output the UK radio indies could win would increase threefold, from the current 9,000 hours to around 27,000 hours. The expansion would be phased in over a six-year transition period. A steady transition reflects the slower rate of change in radio schedules and audience expectations than in television, and also allows for the independent production community to grow sustainably, subject to the outcome of competition.

This transitional period would see the end of the mandatory 10% independent production quota. A move away from quotas to competition would provide independent producers with opportunities to grow but provide no certainty of success. The proposal offers no guarantees.

The remainder of eligible hours—where putting out to competition offers little or no value—would be made in-house and go through a process of external comparison to assess efficiency. This would include talent-led daytime output on Radio 1 and Radio 2 in which the music is centrally controlled and core to the programme, and a small number of long-running titles on Radio 4, including *The Archers*, *Woman's Hour* and *Desert Island Discs*, which are unlikely to be refreshed in the foreseeable future.

¹³⁹ BBC Trust, 'The supply arrangements for the production of the BBC's television content, radio content and online content and services', June 2015 available here http://downloads.bbc.co.uk/bbctrust/assets/files/pdf/our_work/content_supply/2015/content_supply_review.pdf

How should we pay for the BBC and how should the licence fee be modernised?

The licence fee is the best way to fund the BBC and the only mechanism that can maintain a universal, independent and accountable BBC, investing in British creativity and delivering high quality, distinctive programming at an affordable price. Because of the licence fee, people get greater choice of media: from a distinctive BBC, from the support the licence fee provides to Britain's creative economy and from a bigger overall pot for investment in programmes. The licence fee ensures that the public gets better programmes for less than under any other approach. Because everyone pays, the cost to the individual falls to the lowest it can be for the best and most universal service.

The BBC therefore welcomes the Government's 2015 Budget commitment to update the current definition of the licence fee and to introduce legislation by July 2016. We can see merit in the Government's option for medium-term reform of the licence fee by universally levying it on all households, as happens in Germany. Subscription funding in contrast, either alone or as a partial substitute for the licence fee, is the wrong model for the BBC in principle and in practice. It would harm UK content investment and quality, restrict access for audiences, and increase the cost they pay—ultimately damaging the UK's media ecology which is based on competition for quality, but not funding.

3.11.1 The licence fee is the best way to fund the BBC

As the Government's consultation sets out, the BBC's funding model must be simple and efficient to operate, sustainable in light of technology and behavioural change, technically and legally feasible, and both stable and sufficient in coverage to provide the required revenue for the BBC's public services. It must be fair in its treatment of licence fee payers (with due consideration we believe to the BBC's universal reach and to affordability), consistent with an efficient BBC that delivers value for money for licence fee payers, and acceptable to the public. In addition, it must support the BBC's independence and accountability. The licence fee—particularly when updated to include on-demand TV consumption—performs well against these criteria and better than the alternative funding options could.

Universality

The BBC's purpose is to inform, educate and entertain people as individuals, also benefiting British society, culture and democracy. As these benefits are significant it is justifiable that they should be available to all. In addition, there is a significant public interest in broad access, as the public value of the BBC's services increases with widespread consumption, for example as a result of the 'network' benefits of BBC news

content in informing democratic participation. As the BBC has a universal mission it is necessary and appropriate that it should be universally funded and available to all.

Furthermore, as the BBC's range of services is broad—to fulfil its universal mission—in practice some 97% of UK adults and 99% of households use one or more BBC service each week¹⁴⁰, eliminating any gap between those who benefit directly from the BBC and those who pay. This is despite the array of alternative services now available and low switching costs between different TV and radio channels. Compared to many other public services therefore, the level of cross-subsidy from low users to high is low for the BBC.

Affordability

As the licence fee spreads the cost of the BBC across a broad base of households, it keeps down the cost for each individual household, promoting affordability and free-to-air access. This ensures value for money for licence fee payers—an 'all you can eat' bundle costing 40 pence per day for households¹⁴¹ in return for 8 network TV channels, 10 network radio services, Nations' services, regional TV opts and local radio and

¹⁴⁰ Based on the current colour TV licence fee of £145.50 per annum and 365 days in the year.

¹⁴¹ Mediatique for the BBC 'Index of Cultural Inflation', August 2015

the BBC's online services. This is compared, for example, to an average cost of £27 for a Premier League single match-day ticket, around £5 per visit to a museum or art gallery, and around £40 for the theatre. The comparison holds also with other areas of the TV sector; where for each hour consumed, programmes on BBC TV cost about five times less per household than those on pay TV. Affordability also helps ensure that TV content is used widely. As the cost of providing content to each additional user is negligible once the content has been produced this is economically efficient.

High quality programmes and risk capital for investment in British creativity

The licence fee ensures a mixed funding model for UK broadcasting as a whole, delivering a bigger overall pot for content investment than if the BBC competed for subscription or advertising funding. This is crucial in the context of the pressure on overall investment in original British programming¹⁴², and is investment which would not be replaced from advertising and subscription if the licence fee were abolished¹⁴³. The licence fee also delivers better, more varied programmes, because of competition for quality—but not funding—between the BBC and other providers. As highlighted above, 72% of UK adults said that TV programmes overall are good quality in the UK—the highest rating out of 14 countries surveyed¹⁴⁴.

The licence fee also performs a crucial role within this overall mix of funding. As it is levied on all TV users and at an agreed level for established periods of time, it is relatively stable, allowing the BBC to invest for the long-term, to take risks, and support new British talent. While it accounts for around 20% of UK TV revenues, it is converted into around 40% of the investment in first-run, originated UK TV content¹⁴⁵. The UK's pay-TV sector in contrast accounts for c.45% of TV revenues but only around one fifth of total UK original investment.¹⁴⁶

The licence fee also gives the BBC space to be distinctive in the range and depth of content it provides, as set out in section 2 of the BBC Strategy Paper. The BBC could not provide the same choice of content if it were subscription-funded, as there would need to be more of a focus on commercial returns. For example, whilst BBC content is UK originated and broad-ranging, the UK pay-TV channels have tended to focus investment instead on exclusive access to content with highest willingness to pay, particularly premium genres like sport, movies and US drama.¹⁴⁷

Independence and accountability

The licence fee allows the public to make a simple, direct link between the benefits they receive from the BBC and the outlays they make. In turn, it connects those providing the services to those paying for them and allows the BBC to be held to account for how the licence fee is spent. The licence fee is also necessary (though not on its own sufficient) to safeguard the BBC's independence from political control. In contrast to tax funding where Governments almost always lead on allocation, the licence fee is collected directly from audiences, providing the opportunity for funding decisions to be made directly, according to audience need.

Effective in practice

While no form of taxation is universally popular, long-term polling shows that there has been an increase in public backing for the licence fee over this Charter period. Support is higher now at close to 50% than it was in 2004 when 31% backed the licence fee, and higher than it was 25 years ago. The licence fee is the top choice for funding the BBC across socio-economic grades, age groups and type of TV ownership (e.g. Sky and Virgin subscribers prefer the licence fee as the means of funding the BBC)¹⁴⁸.

142 Ofcom, 'Public Service Content in a Connected Society', December 2014, p5

143 Reuters Institute for the Study of Journalism, February 2014. 'What if there were no BBC?'

144 Populus survey for the BBC, conducted 14 countries (500 adults 18+ per country), September-October 2013. Survey question: "What do you think of the quality of television programmes overall in [INSERT COUNTRY NAME]?"

145 BBC analysis of Ofcom data in 'The Communications Report', 2014 and 'Public Service Content in a Connected Society', December 2014,

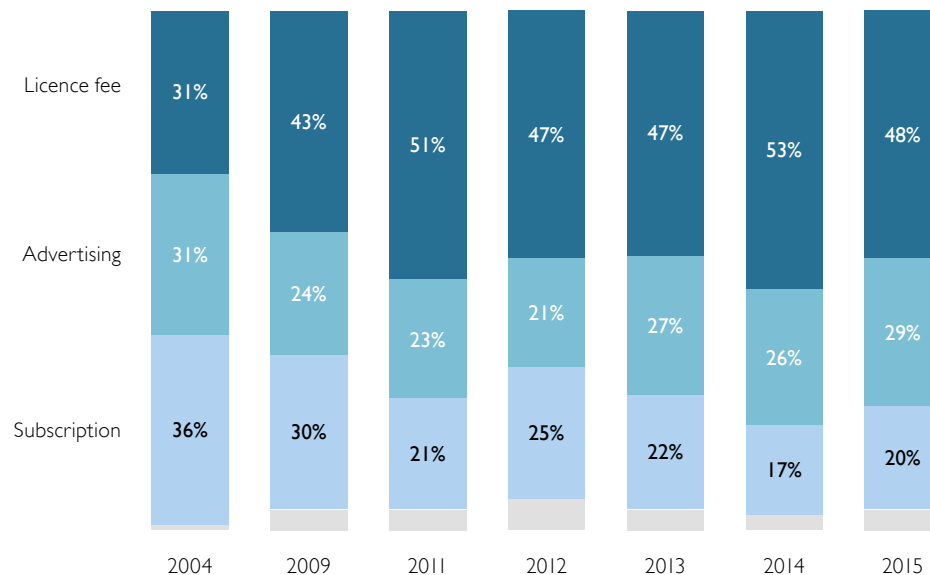
146 BBC analysis of Ofcom data for 2013: 'The Communications Report', 2014, and 'Public Service Content in a Connected Society', December 2014.

147 In 2013 over 80% of non-PSB channel spend on first run UK originations was on sport. Ofcom, 'Public Service Content in a Connected Society', December 2014

148 Ipsos MORI for the BBC, 2,062 UK adults 15+, May 2015

Long-term polling shows an increase in public backing for the licence fee since 2004¹⁴⁹

Which of the following would you like to see as the main source of BBC funding?



Indeed if we calculate the mean level of support across the 12 big surveys of the last two years (three for the BBC and nine for other organisations¹⁵⁰)—a so-called ‘poll of polls’—the licence fee emerges as the model of funding the BBC with the single most support at 42%, ahead of advertising on 34% and subscription on 19%, which is the least popular of these options in all of these surveys.

Willingness to pay the licence fee is high, with some 73% of households willing to pay the current level or more, a figure which rises when households spend time without the BBC¹⁵¹.

The evasion rate and collection costs are also relatively low, at 5%–6% and 2.7% of income¹⁵². The cost of collecting the licence fee is much less than the likely cost of the BBC operating a subscription model. This is clear from a comparison with Sky, for example, which spends c.£1.2bn on marketing across all its products (not just TV), equivalent to c.20% of costs, and c£680m on subscriber management and supply chain, equivalent to c10% of costs¹⁵³. Sky spends the equivalent of half the total value of the licence fee on these functions, suggesting that any move to subscription for the BBC would likely significantly reduce the funding available for investment in UK original content.

¹⁴⁹ 2004: ICM Unlimited, 1,037; 2009: ICM Unlimited, 1,001; 2011: ICM Unlimited, 1,034; 2012: Ipsos MORI, 2,078; 2013: Ipsos MORI, 1,034; 2014: Ipsos MORI, 1,015; 2015: Ipsos MORI, 2,062. All UK adults except 2009 which is GB

¹⁵⁰ Based on the following polls: YouGov for Prospect, 1,712 GB adults 18+, February 2013 (online); ICM Unlimited for the Daily Telegraph, 2,021 GB adults 18+, October–November 2013 (online); Ipsos MORI for the BBC, 1,034 UK adults 18+, November 2013 (telephone); Ipsos MORI for the BBC, 1,015 UK adults 15+, January 2014 (face-to-face); YouGov for the Sunday Times, 1,868 GB adults 18+, February 2014 (online); YouGov for Sunday Times, 1,946 GB adults 18+, March 2014 (online); ComRes for Whitehouse Consultancy, 2,049 GB adults 18+, June 2014 (online); YouGov for The Times/Red Box, 702 adults, December 2014 (online); YouGov published in The Times, 26 December 2014 (online); Ipsos MORI for the BBC, 2,062 UK adults 15+, May 2015 (face-to-face); YouGov for Sunday Times, 1,535 GB adults 18+, June 2015 (online); ComRes for Whitehouse Consultancy, 2,035 GB adults 18+, August 2015 (online). ICM/Daily Telegraph (November 2013) and YouGov/The Times/Red Box (December 2014) did not ask about advertising and subscription so are not included in the means for these potential methods of funding

¹⁵¹ Kantar Media for the BBC, 1,038 UK households, July–August 2015. MTM Research, ‘Life without the BBC: household study’, 70 UK households, fieldwork July 2014–March 2015 and published August 2015, available at <http://downloads.bbc.co.uk/aboutthebbc/reports/pdf/lifewithoutthebbc.pdf>

¹⁵² BBC, ‘TV Licensing Annual Review 2014/2015’, slide 3, available at <http://www.tvlicensing.co.uk/ss/Satellite?blobcol=urldata&blobheadname=content-type&blobheadvalue=application%2Fpdf&blobkey=id&blobtable=MungoBlobs&blobwhere=1370006281969&ssbinary=true>

¹⁵³ Sky, ‘Annual Report 2014’, p37, available at <https://corporate.sky.com/documents/annual-report-2014/annual-report-2014.pdf>

3.11.2 The licence fee is a low cost, high value for money way to fund a universal service

The consultation paper sets out a number of criticisms of the licence fee. We address these in this section.

Regressive

Under a subscription model, households continuing with the BBC would pay more than at present for a less distinctive service, whilst others who value BBC services but could not afford to pay the higher subscription price would be excluded entirely—and so from an important element of shared culture in the UK. These changes would be regressive, particularly for poorer groups.

In contrast, at 40 pence per day per household, the licence fee is still about 1% of spending on average for households¹⁵⁴. And whereas the cost of licence-fee-comparable goods and services¹⁵⁵ increased in the range of 10–40% in nominal terms from 2009 to 2014, the licence rose by only 2%—and fell materially in real terms. It is matter for Government as to whether the licence fee should be made progressive or whether the Government's objectives in relation to the distribution of income are better met through the social security system.

The licence fee is compulsory even if you don't watch BBC TV channels and the level is not correlated to usage

The licence fee ensures that, just as the BBC's mission is to serve everyone and its services benefit society as a whole, the BBC is universally funded. This is appropriate and in line with the treatment of other public services. Moreover, a universal licence fee ensures a broad payment base for the BBC, helping to keep the cost per household low and promoting widespread usage. As the cost of making BBC services available to each additional household once produced

is low, widespread usage is economically efficient. In any case, unlike most other public services, there are very few households that pay the licence fee but do not consume the BBC. Virtually everyone in the UK uses the BBC's services (some 99% of households use the BBC each week¹⁵⁶) and usage is high (the average time spent with the BBC's services per household per day is six hours¹⁵⁷). The licence fee is a shared investment in a public service but with lower levels of cross-subsidy than elsewhere. In theory and in practice, therefore, the compulsory nature of the licence fee is not a significant public policy problem.

Criminal enforcement

The BBC welcomes the conclusions of the Perry Review that licence fee evasion should not be decriminalised and that the current system is broadly fair, proportionate and provides good value for both licence fee payers and taxpayers. The BBC is implementing the Review's recommendations on how to improve TV Licensing's current enforcement policies and looks forward to discussing with Government the recommendations which fall to it. A move to civil enforcement would likely result in a financial impact on licence fee payers of around £200m a year¹⁵⁸. Were decriminalisation to be introduced in the absence of any compensating measures, it would therefore require significant cuts to BBC content and investment in the creative sector.

¹⁵⁴ BBC analysis of 2013 income data in ONS, 'Family Spending 2014'. In 2013 the lowest 10% of the household income distribution corresponded to household income of up to circa £9000 per annum.

¹⁵⁵ Mediatique for the BBC 'Index of Cultural Inflation', August 2015 Across transportation, communications services, subscription video services, physical media, and other cultural and recreational services.

¹⁵⁶ Kantar Media for the BBC, 1,038 UK households, July-August 2015

¹⁵⁷ Mediatique for the BBC 'Index of Cultural Inflation', August 2015.

¹⁵⁸ BBC, 'TV Licence Enforcement Review: Submission from the BBC in response to consultation', April 2015, available at https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/445844/45_2015_04_24_-_BBC_RESPONSE_TO_CONSULTATION.pdf

3.11.3 The licence fee has evolved over the years—we now need to modernise it for the digital age

Whereas the principle of the licence fee remains right, the current mechanism needs to be updated to reflect changing technologies and audience behaviour. The licence fee has always adapted flexibly to changing technology—for example in 1946 to cover TV (previously it was for radio only), in 1968 to accommodate colour TV, and in 2004 to include simulcast consumption of TV content on the internet—and it should now do so again.

The BBC therefore welcomes the Government's recent commitment to bring forward legislation by July 2016 to modernise the licence fee to cover public service broadcast catch-up TV. This will help ensure the licence fee remains sustainable and fair (by closing the loophole where audiences can watch on-demand TV without a licence, free-riding on those who watch TV live and need a licence), and will safeguard the funding available for BBC content and services (by ensuring that many who move from linear to on-demand-only TV consumption still need to pay for that content). The change will capture the video-on-

demand distribution of content and services that are already covered by the licence fee when made available live. As such, it provides an opportunity to tackle the perverse incentive for audiences to move from live to on-demand TV usage to avoid the licence fee. The change can be enforced through existing licence fee collection methods, without any requirement on the commercial public service broadcasters to 'gate' or otherwise reorganise their services.

We can see merit in the Government's option in the consultation paper for medium-term reform of the licence fee by universally levying it on all households, as happens in Germany. This further modernisation would reflect the universal usage of the BBC and the value its services deliver to society as a whole, as well as address the fact that currently people can use the BBC's radio and text services for free. It could also reduce collection costs and increase the BBC's investment in UK originated content for the long-term.

3.11.4 Other funding mechanisms would change the nature of the BBC, mean less choice and more expense for audiences, and de-stabilise the broadcasting ecology

The consultation paper identifies two potential alternative funding models to a reformed licence fee:

- full subscription model (in the longer-term) and
- a hybrid licence fee and subscription model.

Subscription funding, either alone or as a partial substitute for the licence fee, is the wrong model for the BBC in principle and in practice. It would harm UK content investment and quality, restrict access for audiences, and increase the cost they pay—ultimately damaging the UK's media ecology. Public support for a subscription-funded BBC has been falling over the past 10 years and is now the least popular option.

There are also significant practical barriers to the introduction of subscription funding for the BBC, as acknowledged in the consultation paper:

While pay-TV users have set top boxes or other equipment with 'conditional access modules' (CAM) that enable subscription, pay TV equipment is only in just over 50% of UK households. Around 11 million households have free-to-air TV alone while there are upwards of 35m active TV sets overall which do not have conditional access capability. This equipment would need to be fitted with CAMs or a new set top box, at an estimated cost of c£500 million¹⁵⁹. It is also not technically feasible to encrypt the BBC's broadcast radio services.

We consider the impact of a full subscription and hybrid model in turn.

¹⁵⁹ House of Commons, Culture Media and Sport Committee, 'Future of the BBC', 2015, available at <http://www.publications.parliament.uk/pa/cm201415/cmselect/cmcmucom/315/315.pdf>

Full subscription

Loss of universality: Under a subscription model, the BBC's incentives could change. Normally, subscription prices are set at a revenue or profit maximising level. Previous analysis suggests this would be around two thirds higher than the current licence fee for the same number of services¹⁶⁰. At a higher price the BBC's reach among the public would reduce, denying people access to services they value and detracting from the social, democratic and cultural benefits of widespread consumption of BBC content. The BBC would lose its ability to bring the country together; to turn things as diverse as ballroom dancing, home baking, business, classical and pop music, as well as charitable causes and sport, into national, shared events. Whilst subscription channels tend to be good at serving specific audiences they do not provide universality. In the US, for example, which is focused more strongly on pay TV than the UK, outside sport the biggest audiences are not much bigger than those in the UK, though their population is five times larger.

Reduction in media choice and investment: The BBC's programming choices would optimise to attract subscribers and maximise revenues, for example by focusing on exclusive content that has low price sensitivity. For example, over 80% of non-PSB channel spend on first run UK originations was on sport¹⁶¹, and leading pay channels tend to focus on a relatively small number of 'peak' brands that attract and keep customers. The UK's pay-TV sector accounts for c.45% of TV revenues but only around one fifth of total UK original investment¹⁶². The BBC's overall level of investment in UK content would also suffer given the significantly higher costs of operating a subscription service than collecting the licence fee¹⁶³. In addition, as the BBC would be in direct competition with existing pay-TV providers for revenues, the overall pot for investment in content would also fall.

Loss of welfare and value for money: Because of increased costs and a smaller subscriber base, those paying it would likely have to spend more. This would reduce affordability, resulting in many more losers than winners. In particular, it would likely exclude many who value BBC services but could not afford to pay the higher subscription price—this would be both unfair and inefficient given the low marginal cost of making our content available to additional viewers once it has been produced. Those who remain would pay a higher price than at present for a less distinctive BBC, reducing value for money—as detailed above, for example, programmes on BBC TV cost about five times less per household for each hour consumed than those on pay TV. Those who lose out in these ways would outnumber the smaller set of households who value the BBC at less than the cost of the licence fee and so might opt-out, and so audience welfare overall would reduce¹⁶⁵.

Overall, subscription funding would change the nature of the BBC, as BSKyB noted in its evidence to the Select Committee: *“operating in a commercial environment for subscribers... means that you have to think commercially all the time. If you wanted to retain the universality of the BBC to some extent, if you wanted to retain its public purposes, you would either have to carve that out or you would have to constrain what the BBC could do within its subscription model. It seems to me that that would make it quite difficult to prosper in that environment.”*¹⁶⁶

¹⁶⁰ Preliminary BBC analysis (Revenue maximising price point based on likely demand response to an increase in price)

¹⁶¹ Ofcom, 'Public Service Content in a Connected Society', 2014, Figure 42.

¹⁶² BBC analysis of Ofcom data for 2013: 'The Communications Report', 2014, and 'Public Service Content in a Connected Society', December 2014.

¹⁶³ BSKyB noted this at its evidence session before the House of Commons, Culture, Media and Sport Committee inquiry into the future of the BBC "... 100 million [current licence fee collection costs] is nothing compared to what they [the BBC] would likely have to spend on marketing in order to retain their subscribers."

¹⁶⁴ Mediatique for the BBC 'Index of Cultural Inflation', August 2015

¹⁶⁵ BBC analysis

¹⁶⁶ Sky's oral evidence to the House of Commons, Culture, Media and Sport Committee inquiry into the future of the BBC, given in July 2014, question 375, available at <http://data.parliament.uk/writtenevidence/committeeevidence.svc/evidencedocument/culture-media-and-sport-committee/future-of-the-bbc/oral/10684.html>

Mixed licence fee and subscription funding

The consultation paper also raises mixed licence fee and subscription funding as an option for the BBC. It states that the subscription element could be applied to certain elements of the BBC portfolio, for example, by funding a 'core service' through the licence fee with other services funded via subscription.

We have conducted preliminary analysis of one hypothetical scenario for a 'core' licence fee funded BBC with remaining services available on a subscription basis. Illustrative results suggest this would not be a viable alternative to the current model and they reveal the significant drawbacks with disaggregating the BBC's bundle of services.

The first problem is one of selection. Licence fee payers have many different concepts of what the 'core' BBC services are, suggesting that any attempt to divide BBC services into a licence fee funded 'core' and subscriber-funded 'non-core' would leave most feeling under-served by the core. In particular, from a sample of 1038 households research agency, Kantar Media, counted 825 different combinations of BBC services used in a week; 791 households used their own unique combination that no other household in the sample used; and no more than 3% of households used the same combination of services.¹⁶⁷

Setting this selection problem aside, and taking into account technology feasibility, potential commercial viability and the need to still reach large audiences with public service content, we assessed a hypothetical scenario where BBC Three (the current broadcast service), BBC Four, BBC iPlayer, and BBC Online were made available on a subscription basis. This highlighted two further significant problems with the hybrid model. First, the services are very unlikely to be commercially viable. For the TV services and BBC iPlayer there could be different routes to market:

- 1 **Subscription as stand-alone BBC services.** As argued above, conditional access technology would first need to be widely available, at significant cost, to enable subscriptions to be collected from viewers. Furthermore, market practice suggests availability on a standalone basis is an unusual route for mixed genre channels and we are not aware of other channels of this kind being sold successfully on a stand-alone basis in the UK. Channels tend to be bundled, allowing fixed customer and service costs to be distributed across a range of services and because consumers are more willing to buy a bundle with a wide range of programmes than single channels.
- 2 **Include the BBC services in a third party pay-TV package where the pay-TV provider retails the services and pays the broadcaster on a per subscriber basis having covered platform costs and retained a margin.** This would restrict coverage of the BBC subscription services to the c.50% of UK households with pay-TV, with those using Freeview and Freesat excluded.
- 3 **Online distribution, such as subscription VOD.** International experience suggest that SVOD services tend to focus on a subset of the most popular genres and content, including movies, high-end drama and children's content. Putting these genres and services—which are pre-existing and currently available free to air through the licence fee behind a pay-wall—would involve a significant narrowing of the BBC's universal offer, as these are genres which, if removed from the licence fee, would significantly impair the BBC's ability to provide something of value to everyone, deliver public service benefits and bring the nation together.

We have examined willingness to pay for the subscription services to understand the optimal price point¹⁶⁸, likely uptake and the resulting revenues. The headline conclusion is that the channels would likely be loss-making given content costs, the new costs associated with customer acquisition and retention, and platform charges for carriage.

¹⁶⁷ Kantar Media for the BBC, 1,038 UK adults, July-August 2015

¹⁶⁸ Revenue maximising price point based on likely demand response to an increase in price

The third problem is the loss of consumer welfare, as audiences would have to pay significantly more to access the BBC under a hybrid model. Audiences that wanted to subscribe to the same BBC services as before would have to pay around twice the level of the current licence fee. Indeed, the cost of taking just one of the above services on a subscription basis would likely exceed the licence fee saving. Although households who chose not to subscribe to any of the services would save through a lower 'core' licence fee, the saving would be small. It would be a maximum of c.£1.40 per month, assuming that all the subscription services covered their costs, which the analysis suggests they would not. We estimate that the total loss of consumer surplus would be over £150 million per year from putting the services in question behind a pay-wall.

Rather than delivering the best of both worlds, our initial analysis suggests that under a hybrid model some people would pay significantly more for the same number of services and others would pay a bit less for a lot fewer services. Moreover, higher prices overall would exclude many people who value the services, thereby reducing the society-wide benefits that flow from universal access to the BBC.

3.12

Should the level of funding for certain services or programmes be protected? Should some funding be made available to other providers to deliver public service content?

3.12.1 Protecting levels of funding for certain activities undermines the BBC's independence

The consultation paper raises the prospect of protecting or ring-fencing the level of funding for certain BBC activities or services in the next Charter period. Ring-fencing the level of funding for certain services or programmes would be inappropriate and fall short of the longstanding, Charter-enshrined guarantees of the BBC's operational and strategic independence.¹⁶⁹

As part of Charter Review, it is legitimate to seek views on the priorities for the BBC among different public purposes and genres. It is also right that the BBC is transparent about what it spends, and that significant changes to scope are subject to appropriate scrutiny. However, it would not be right for specific areas of the BBC's spending to be ring-fenced.

First, there is no evidence of any areas in need of 'protection'. The BBC allocates resources according to its Charter and Agreement obligations, public service mission and audience priorities. Far from needing to be protected from creative decisions, the BBC's activities need to be insulated from political direction.

Second, ring-fencing is a zero-sum game. By elevating some causes, it would downgrade others and make them subject to a level of cuts which may not reflect audience interests. The BBC already faces tough financial challenges in the next Charter. The decisions about how best to respond to these and to the changing requirements of audiences and new technologies should be audience-led and creative. The BBC should have the flexibility to make choices within its public service remit.

Third, by establishing the principle that some areas must receive a 'minimum level of funding', Government opens the door to BBC spend being prioritised by the loudest lobby, not by decisions in the interest of licence fee payers. It risks shifting the argument from one about mission to one about how much money each vested interest can secure.

The consultation document points to precedents of ring-fenced funding for S4C, local television and the World Service. These are misleading. In each of these cases, the decision was not that the recipients required safeguarding because of their importance in contrast to 'unprotected' areas such as drama, children's TV content, or national news. Nor were funding guarantees required to protect the recipients from unwarranted cuts by the BBC. (The BBC voluntarily increased World Service funding upon its transfer from grant-in-aid to the licence fee). Rather, the decision to ring-fence these budgets was a direct result of the transfer of Government spending and policy priorities to the licence fee. In short, what was being protected was not the audience interest from BBC re-prioritisations; it was the delivery of commitments which the Government no longer wanted to fund directly.

¹⁶⁹ BBC Royal Charter (October 2006). Clause 6 of the Charter states: "the BBC shall be independent in all matters concerning the content of its output, the times and manner in which this is supplied, and in the management of its affairs." Clause 7 states that the BBC "Executive Board has responsibility... for all aspects of operational management." Available at: http://downloads.bbc.co.uk/bbctrust/assets/files/pdf/about/how_we_govern/charter.pdf

3.12.2 Contestable funding is a solution to a problem that does not exist

The consultation paper also considers whether alternative providers should be able to access the licence fee and/or whether elements of the licence fee should be allocated to support new public policy projects. Just as it is not clear what ring-fencing BBC funding would be intended to protect, and from whom, so it is not clear what problem top-slicing or contestable licence fee funding would solve.

We welcome the Government's commitment to phase-out the broadband ring-fence and we expect the time-bound contribution to local TV to end with this Charter. Contestable funding, in our view, would be bad public policy, both in principle and in practice. This is because it would substitute public money for private, and be allocated by committees rather than commissioners. It would be subject to lobbying rather than audiences, and it would weaken accountability for public money and erode the BBC's independence.

We would regard any new proposal to top-slice the licence fee or introduce contestable funding as re-opening the Budget agreement on the BBC's future funding.

The consultation document suggests three possible advantages of contestability.

First, it is suggested contestable licence fee funding 'introduces an element of competition' which would promote efficiency.

The BBC is not a monopoly supplier of public service broadcasting. It operates in a market with growing levels of competition. On the output side, this includes 'competition for quality', which ITV described as "*a unique feature of the UK television market, sustaining genres such as high-end drama and free-to-air sport.*"¹⁷⁰ Policy often seeks to introduce a right of exit for consumers of public services—but there is already a right of exit for the BBC's audiences via the remote control. 46 million people use the BBC everyday. Commissioners know which programmes are being consumed—getting audience sizes overnight and, within two days, detailed audience appreciation ratings, demographics and qualitative feedback such as

verbatim. That has a powerful role in driving up standards, giving commissioners a good mix of incentives to universality and quality. As far as we know, no public service has a greater element of competition for its outputs than the BBC.

On the input side, two-thirds of what the BBC spends is contested already, with a plan to increase this to 80% and open up our TV, radio and online schedules to greater competition. Again, we do not know of any other public service that comes near to that level. To take one of the main areas of BBC spending, in 2014/15 just over half of network TV commissioning spend (aside from news and sport) went to the external production sector, whereas only 6% of the NHS England's commissioning budget was spent directly on private healthcare providers.¹⁷¹

The BBC has embraced contestability but through a model that works to increase quality and value—precisely because spending decisions are made creatively, by commissioners and channels that are close to the audience and held accountable for performance. Introducing a third type of competition, this time for funding, would blur a set of incentives that are currently working well.

The argument also neglects the BBC's strong efficiency track record based on its current model of competition, as set out in section 3.13. There is little evidence of a lack of efficiency or efficiency incentives which contestable funding would solve. Indeed, as the consultation document rightly points out, making the licence fee contestable could be costly and complex to administer. By requiring a layer of bureaucracy and transaction costs, contestable funding would likely diminish, rather than increase, efficiency and reduce the actual funding available for content.

Further, public funding would simply substitute for commercial investment. There were previously calls for licence fee funds to be used to sustain ITV regional news and/or Channel 4's content budget, early in the current Charter¹⁷². Yet, despite no such contestable funding, ITV agreed a new 10 year licence with its

¹⁷⁰ ITV plc, written evidence to the CMS Select Committee inquiry into the Future of the BBC, December 2013, paragraph 7, available at <http://data.parliament.uk/writtenevidence/committeeevidence.svc/evidencedocument/culture-media-and-sport-committee/future-of-the-bbc/written/4165.pdf>

¹⁷¹ Department of Health, 'Annual Report and Accounts 2014/15', July 2015

¹⁷² In 2009, Ofcom proposed the establishment of IFNC (independently funded news consortia) to provide regional news for ITV using up to £50m of licence fee funds. It was dropped in 2010. ITV has subsequently agreed new 10 year PSB licences with its national and regional news commitments intact. Channel 4 and Ofcom predicted a "funding gap" of up to £150m pa. in Channel 4's means to sustain investment in PSB content from around 2005 to 2009; in 2007 Channel 4's then CEO, Andy Duncan, declared "debate over" Ofcom having proven the need for licence fee funding for the channel. Channel 4's investment in UK originations has since returned to high levels.

national and regional news obligations intact, and Channel 4's content investment has remained strong. Similarly, the BDUK contestable fund for super-fast rural broadband roll-out provides a cautionary lesson. £600m from licence fee funds was earmarked to fund the tenders for superfast broadband rollout. But £129 million of public funding is now being clawed-back, given the higher than predicated take-up of broadband in the relevant areas. While the returned funds will support further tenders for broadband rollout, the process demonstrates the risk of public investment subsidising commercial activity that could have happened anyway.

Second, it is suggested that contestable funding could improve plurality of supply of key genres.

Overall, there is no evidence of a major supply problem: across all genres, audiences have more content and providers to choose from than ever before. For example, in children's TV, the BBC's "near monopoly"¹⁷³ is hard to recognise when the BBC's children's channels sit below twelve other children's channels on Sky's Electronic Programming Guide. Ofcom's PSB review has identified pressure on the delivery of certain genres. The starting-point should be to analyse why this provision is at risk in order to ensure that any policy proposals work with the grain of market dynamics, rather than against them. The preference should be for policy levers that can stimulate additional investment. Examples include the Government's tax breaks for animation and live-action children's productions, introduced in 2013 and 2015 respectively. By contrast, contestable funding is a zero-sum game that would divide the existing funding

pie and create extra accountability requirements which DCMS states "may reduce demand from other broadcasters". In evidence to the CMS Select Committee and to Ofcom's PSB Review, Sky, ITV, Channel 4, PACT and COBA have all flagged their reservations about contestable funding.¹⁷⁴

Third, it is argued that contestable funding could help sustain the broader public service broadcasting ecology.

This was not the conclusion of Ofcom in its recent statutory review of how the PSB system might be maintained or strengthened. They found that:

*"There remains a strong clarity of purpose which is achieved through institutional funding. Although contestable funding remains an option, it would require detailed consideration, in particular addressing the dangers of uncertainty of funding, undue bureaucracy in implementation, reducing the actual funding of PSB content and the introduction of conflicting incentives into the commercial business models and focus of the broadcasters which compete with, and complement, directly funded services."*¹⁷⁵

Instead, Ofcom suggested that if policy makers want to maintain or strengthen PSB, they should consider a range of other interventions before turning to the licence fee for funds, including its recommendation to future-proof the prominence of PSB services on platforms.

In summary, there is little evidence to suggest that any of the three claimed advantages of contestable licence fee funding would, in practice, be delivered.

173 DCMS, Charter Review Public Consultation, page 57, "For example, children's programming is an area in which the BBC has a near monopoly

174 ITV oral evidence to the CMS Committee on the future of the BBC: "we have no ambition, as ITV, to access licence fee funding"; BskyB oral evidence: "there is a bid danger to the top slicing... that is you lose that accountability, you lose that transparency and you lose the ability to understand what the impact on the market is. It potentially leads to much worse public outcomes, because you are increasing the distortions right across the market place. It is much better to keep the funding in one place of the organisation to use that is governed in a transparent way and is accountable to its licence fee payers or whoever is funding it." Q378; in response to Ofcom's PSB Review: PACT stated it "does not consider that contestable funding is the most appropriate solution" (and when asked if they opposed top-slicing by the CMS Select Committee stated 'yes' Q403); Channel 4 stated: "the introduction of a system of contestable funding could risk upsetting the delicate balance of funding that exists in the PSB ecology... the independence of our commercially-funded model is a better way to deliver our unique remit than by receiving public money, and therefore it is not seeking the introduction of contestable funding"; COBA said: 'we are not convinced of the merits of making the licence fee contestable. 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.'

175 Ofcom, Public Service Broadcasting in the Internet Age, 2 July 2015, paragraph 6.15.4

3.12.3 Contestable funding would put at risk the level of BBC investment and reduce the accountability and impact of public spending

There is, however, strong evidence to suggest contestable funding would come with significant disadvantages: primarily the negative impacts on BBC services, and the accountability and impact of public spending. A contestable licence fee fund would come at the expense of the BBC's own investment in valued services and investment certainty. This investment, in turn, supports a competitive broadcast ecology, as described in section 3.5.

The risk to the accountability and impact of public spending is equally important. Funding policy priorities from the licence fee can avoid the usual strong spending disciplines of both Government and the BBC. Such an accountability 'double-bypass' can bring into question the effectiveness of public spending.

Take the example of local TV. Licence fee funding for Local TV, allocated as part of the 2010 funding settlement, was designed to kick-start a new sector. Some stations have shown signs of success. However, evidence of audience impact to date is limited and it would be hard to argue that the £40 million of licence fee funding has, so far, delivered value for money. As the CMS Select Committee recently found: *"So far these services do not appear to have had any significant impact among audiences nor have they made a meaningful contribution to the provision of local news and content and as such their viability remains in doubt."*¹⁷⁶

As part of the BBC Strategy Paper, we set out a range of partnership proposals—open to all local news providers—which should offer a more sustainable and impactful contribution towards a pluralistic local media and deliver value for money for licence fee payers. Under this model of local partnership, the BBC would make decisions about how licence fee funds are spent and be held accountable for those decisions.

Unitary receipt of the licence fee allows the public to make a simple, direct link between the benefits they receive from the BBC, and the outlays they make. Licence fee payers know they fund the BBC. The model is transparent. A recent survey showed that more than 9 in 10 people knew the licence fee funded BBC services, while only a fraction of audiences were aware that it currently funds local TV and broadband rollout¹⁷⁷. The link audiences make between the licence fees they pay for and the BBC services they receive is a fundamental part of the audience 'ownership' of the BBC.

¹⁷⁶ Future of the BBC, February 2015, paragraph 165

¹⁷⁷ 91% for all BBC, 5% for local TV and 5% for broadband; Ipsos MORI for the BBC, 27 Feb-11 March 2015, 1,038 adults 15+, Face to face sample

3.12.4 Investment in children's content

The consultation paper identifies children's programming as a genre that could benefit from contestable funding. Top-slicing the licence fee to fund children's content would, in our view, be unnecessary and counter-productive.

Ofcom and Government have been right to scrutinise children's content given its importance and the decline in overall UK investment in the genre. The BBC will remain committed to informing, educating and entertaining all UK children. We will maintain our role as the provider of UK-produced, advertising-free content for children, and supporting this vital part of the UK's creative economy, including independent producers.

At present, CBBC and CBeebies are among the nation's most popular children's TV channels, able to reach 28% and 45% of their target audience respectively (compared to 19% for CiTV).¹⁷⁸ CBeebies is the favourite brand of children under 6 years old¹⁷⁹, and parents agree that it has learning at the heart of all its programmes; twice as much as the next nearest competitor¹⁸⁰. 7 in 10 children agreed they 'found out lots of new things on CBBC' and close to 8 in 10 agreed it was fun.¹⁸¹

As recognised by Ofcom's PSB review¹⁸², the BBC has not been the cause of the decline in market investment in UK children's originations—being neither dominant in viewing nor competing for commercial revenues. Rather the decline started because of the removal of quotas for children's programming on the commercial PSBs in the 2003 Communications Act and the ban on HFSS advertising in 2008.

Notwithstanding the decline, it would be wrong to assume a crisis in children's TV. Overall choice for children has grown. Multichannel providers continue to invest in programmes, being responsible for one-seventh of UK originations¹⁸³, while Netflix and Amazon have also announced investment plans.¹⁸⁴ Audience satisfaction with the range of high quality and UK made programmes for children is still high.¹⁸⁵ This Government's tax breaks for animations and for live-action children's productions should further stimulate the market. These were created with the stated aim of "counteracting a decline in investment in children's TV in the last decade"¹⁸⁶. It is too early to come to a conclusion on their level of success, due to the long lead times in developing animation and realising its full revenue potential. However, a recent Nordicity/Olsberg SPI report considers there to be 'green shoots emerging as a result', with an 11% boost in UK animation revenues in 2013/14¹⁸⁷.

178 BARB data for year 2014/15.

179 28% of 0–6 year olds chose CBeebies as their 'most loved brand', well ahead of Lego, Disney Jr and YouTube, each at circa 15%, Ipsos Mori Brand Tracker, January 2015

180 GfK for the BBC, 251 adults with children aged 15 or under: 63% feel that CBeebies has learning at the heart of all its programmes and content, 34% for Disney and 23% for Nickelodeon.

181 BBC Trust, Service Review of the BBC's Children's Services, Public Knowledge, 2013, 8140 children replying to a public consultation, available at: http://downloads.bbc.co.uk/bbctrust/assets/files/pdf/our_work/childrens_services/public_consultation.pdf

182 Ofcom identify four causes: the two regulatory ones mentioned and two market-led: the internationalisation and digitalisation of the market

183 Ofcom, Public Service Broadcasting in the Internet Age, Data Annex, July 2015, 2003 data from figures 18 and 19

184 Netflix has signed a 100-hour deal with Dreamworks Animation with a further four original animations. Amazon has recently announced six children's pilots.

185 Ofcom, PSB Annual Report 2015: PSB Audience Opinion Annex, July 2015. Available at: http://stakeholders.ofcom.org.uk/binaries/broadcast/reviews-investigations/psb-review/psb2015/PSB_2015_audience_impact.pdf

186 HM Treasury, 'Twelve things you should know', Autumn Statement 2014

187 Nordicity/Olsberg SPI, Economic Contribution of the UK's Film, High-End TV, Video Game, and Animation Programming Sectors, February 2015, available at <http://www.nordicity.com/media/2015225acmcjdvvn.pdf>

It would be equally wrong to assume the decline in market investment in TV originations is the only—or even primary—issue the sector is facing. A radical change is occurring in the migration of children from TV to online. YouTube is used by 78% of 6–12 year olds¹⁸⁸ while almost a quarter of all viewing to CBBC is now via iPlayer.¹⁸⁹ At the same time, the TV screen remains the favourite screen to watch programmes on for 86% of kids¹⁹⁰, according to a recent survey, and 63% of children still watch programmes when they are scheduled on TV.¹⁹¹

To respond to these changes, the BBC has proposed a new investment in an internet-first service for children. iPlay would be an open platform, and would showcase the best content from the BBC and others, as well as commissioning from the independent sector. Further details are set out in the BBC Strategy Paper.

50% of BBC Children's online spend in 2013/14 was on independent external suppliers¹⁹²—higher than any other part of the BBC—and we would expect iPlay to have similar ambitions. Overall, BBC Children's is now responsible for 88% of first-run originations. It sustains what PACT describes as 'effective competition'¹⁹³ though a WOCC in which indies win c.60% of commissions, and the independent quota.

It is very difficult to see how these benefits could be replicated through the use of contestable licence fee funding. The proposal would be subject to many significant disadvantages, including a negative impact on BBC's children's services as finite resources are fragmented, with consequent risks to universality and the BBC's ability to build a relationship with the next generation of viewers.

188 Ipsos Connect for the BBC, Children's brand tracker, July 2015, 151 6–12 year olds

189 BBC analysis of BARB / iStats AV / TRP, Quarter 2 2015.

190 Ipsos Connect, BBC Children's Digital Tracker, Wave 8, 845 0–12 year olds, June 2015

191 Children's TV Viewing Behaviour, Illuminas / BBC 2014,

192 BBC Trust review on supply arrangements, June 2015

193 PACT response to BBC Trust children's service review, 2013

Has the BBC been doing enough to deliver value for money? How could it go further?

We first set out our efficiency record and describe our future plans for further efficiency through a 'compete or compare' framework. Section 8 of the BBC Strategy Paper sets out how we propose to fund the new investments and the challenges this will create.

3.13.1 The BBC has transformed its efficiency

Any assessment of BBC efficiency must look at delivery over a sustained period of time. Over the past 20 years, the BBC has transformed its efficiency and productivity, delivering more services for less, and is now at least as efficient as comparable organisations. In the 1990s the BBC embarked on the most radical marketisation programme in the public sector: 'Producer Choice' introduced competition for everything from studios to security. The 1990 Broadcasting Act ensured at least 25% of TV content was made by independent producers, and the BBC introduced a pure purchaser-provider split to implement that. The combined impact was an immediate and significant efficiency dividend of over 6% a year from 1993 to 2000. Having harvested the main savings from these structural reforms, the BBC then turned to continuous improvement programmes, resulting in an average improvement of c.4% a year.

Since 2006 there have been two licence fee settlements. The 2006 licence fee settlement provided a degree of protection against inflation which allowed the BBC to reinvest the vast majority of its savings from its efficiency programmes in content and services such as iPlayer. But after the financial crisis we voluntarily froze the level of the licence fee in 2011/12 and, at the next licence fee settlement in October 2010, the Government extended this to 2016/17. As a result, the licence fee has fallen in real terms while other household costs have risen.

Under the 2010 deal the BBC also had to pay for c.£500m a year of obligations. That licence fee settlement led to a new drive to make savings, the Delivering Quality First (DQF) programme, to pay for the obligations and offset inflationary pressures in the cost base.

Our savings are externally audited on an annual basis. The NAO also regularly reviews the BBC's progress in delivering major savings programmes (reporting in 2011 and 2015) as well as carrying out regular value for money reviews. By the end of this Charter, we will have saved £1.6 billion in cumulative annual savings (including £700 million pa of savings by 2016/17 under DQF), over 40% of the BBC's addressable cost base.

The majority of the savings so far have resulted from productivity improvements including, for example: procurement savings, which exceeded £90m in 2013/14; property savings of £75m a year; and technology savings of over £90m in two years from 2015 to 2017.

At the Culture, Media and Sport Select Committee in July 2014, Sir Amyas Morse, Controller and Auditor General, National Audit Office said:

"I have to testify that the BBC have done, in my view, a good job of addressing their cost structure. They have been successful with their cost reduction work over a period of time; they have set targets and they have achieved them. I am impressed with that and we have reported on it on various occasions and always given positive comment about it. The criticism I have always made of it is that it does not tend to have what I call a destination model."

The BBC is implementing a strategy of 'compete or compare' to ensure that there are clear 'destination models' for our activities.

The Government's consultation highlights the challenge of ensuring value for money is embedded throughout the BBC and it mentions a number of areas where the BBC has been criticised over this Charter period, including the cost of New Broadcasting House and staff pay. However, contrary to those criticisms, the BBC has reduced its pay and property costs, often at a faster pace than the rest of the public sector. For example:

BBC Property: An NAO review of BBC property this year found that the BBC has made good progress in rationalising and upgrading its estate. We have already reduced the size of the BBC estate by 35%, and set ambitious targets for the better use of space. Major disposals have included Television Centre and the recent deal to sublet much of the Media Village site in West London. These property moves mean the BBC is on course to save in excess of £75 million a year on property costs by 2017—an increase of £19 million from the original target.

BBC Staff: We have significantly reformed remuneration for BBC staff and actively controlled our paybill and average salaries. Our pay restraint, combined with headcount reductions, had delivered over £150m a year in reduced costs by the end of 2013/14. Since 2009 we have reduced the number of senior managers and the bill for them by more than a third, saving over £20m a year. We implemented pension reform that led the public sector and at the time reduced the pension scheme's funding deficit by around £0.5bn. This year BBC Trust commissioned a second review of the BBC's management of talent. The report, completed by independent consultants Oliver & Ohlbaum (O&O), found that the BBC attracts talent at competitive rates. O&O concluded that BBC spending on talent fell by 15% from £221m in 2008/09 to £188m in 2013/14. In 2014, we committed to keep spend on talent to no more than 16% of overall internal spend on content. In 2014/15, total talent spend represents 12.2% of the BBC's spend on internal content.¹⁹⁴

SM PAY REDUCED	SM HEADCOUNT REDUCED	BONUSES REMOVED	PENSIONS REFORMED	SEVERANCE REFORMED
We operate a salary discount policy for Senior Managers (20% to 80%) versus market levels	Senior manager headcount has reduced from 640 to under 400 (c35% reduction) in the last 4.5 years Further savings planned to end of Charter	The BBC removed discretionary bonuses indefinitely from Executive Board and Senior Managers in 2009	BBC started significant pension reform earlier than other parts of public sector It has now closed its scheme to new joiners and replaced it with a defined contribution scheme	In Sept 2013 we implemented a cap of £150k on severance and redundancy pay

¹⁹⁴ Total talent spend in 2014/15 was £208m. The difference between this figure and £188m in 2013/14 is mainly accounted for by the inclusion of the World Service for the first time and a different classification of talent to include organisations such as external orchestras. Further detail on Talent spend is set out on page 85 of the BBC Annual Report and Accounts 2014/15.

3.13.2 There is still work to do to achieve further savings in this Charter period

In March 2015, the NAO published a review of DQF which concluded that it has so far delivered value for money, that the savings have exceeded implementation costs and have had a limited impact on audience perceptions¹⁹⁵. However, the NAO's report said that it would be increasingly hard for the BBC to find repeatable savings that did not have an impact on audiences and that the last few years of DQF would therefore be more challenging. So far most of the DQF savings have come from productivity. There are c.£320m p.a. of DQF savings to deliver in the final two years. Detailed plans are in place and the remaining savings split roughly equally

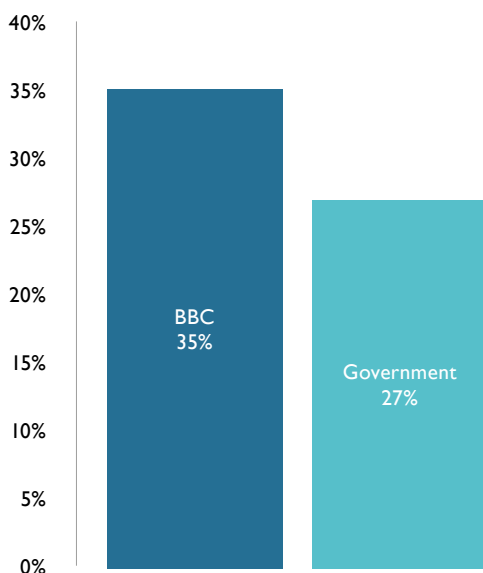
between productivity and scope changes, including the closure of BBC Three as a TV channel (up from about 30% scope in the first three years of DQF).

In addition to these savings under DQF, the BBC needs to find additional savings in excess of £150m a year by 2017/18 to address the decline in TV penetration to the end of this licence fee settlement. We have announced plans to find at least £50m of these savings through further productive efficiencies by merging divisions, cutting management layers and improving processes.

3.13.3 The BBC compares well on efficiency benchmarks

Any assessment of BBC efficiency should also look at performance against comparable organisations. In the decade since the last Charter Review we have gone further than Government in delivering efficiency.

Cumulative annual net efficiencies from 2005/06 to 2014/15



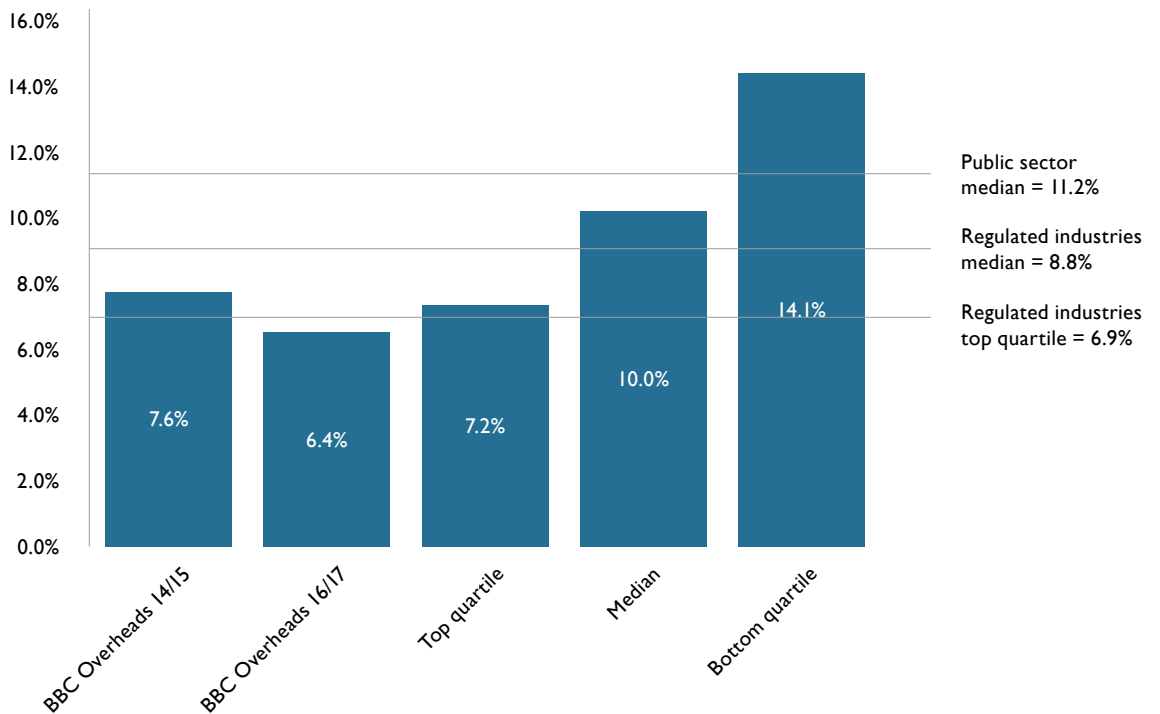
¹⁹⁵ NAO, 'Reducing Costs Through Delivering Quality First', March 2015 available at <http://www.nao.org.uk/wp-content/uploads/2015/03/Reducing-costs-through-delivering-quality-first.pdf>

PwC have compared the BBC's overheads to industry benchmarks. PwC found that the BBC compares well—we are close to the top 25% of regulated industries for expenditure on general overheads, and well above average compared to media companies.

The completion of DQF and plans for £50m of further annual savings, as mentioned above, means we will be in the top 25% when compared to benchmarks of companies that operate in regulated industries, by the end of the current Charter.

Overhead ratio, BBC compared to public sector and regulated bodies¹⁹⁶

Overhead ratio (Overhead costs / total costs)



¹⁹⁶ PwC, 'BBC Efficiency Review - An update on the BBC's overheads', July 2015

3.13.4 The BBC offers good value for money

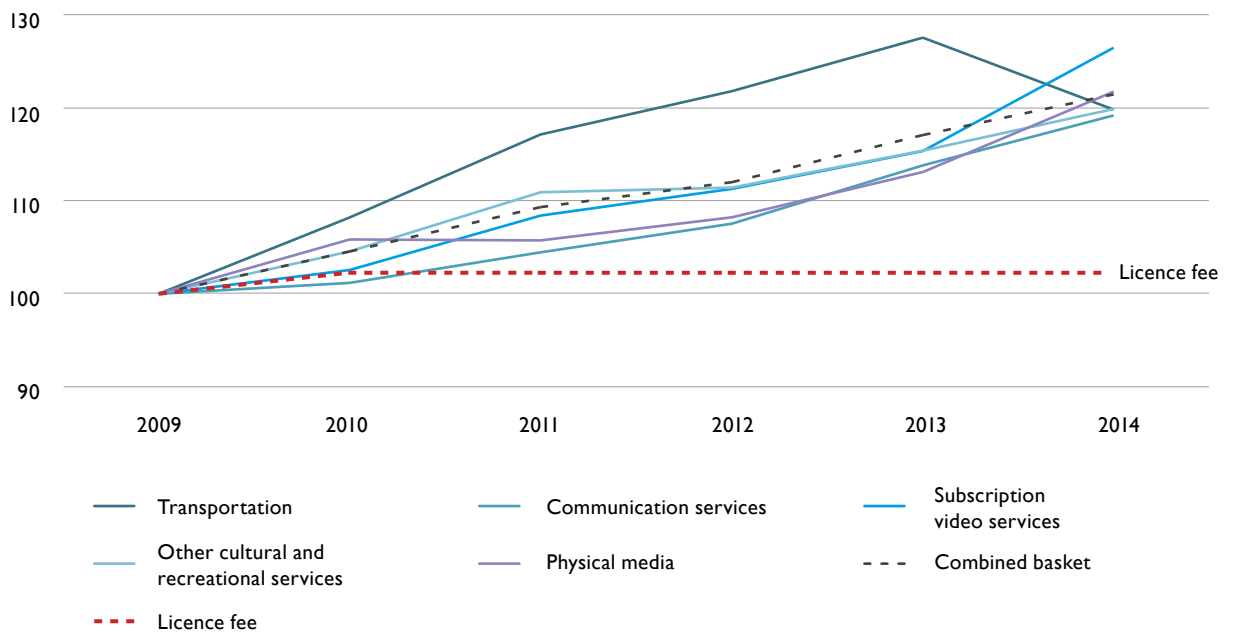
Cost efficiency is only one part of the equation. We also need to look at the value the BBC provides audiences, to assess value for money. As explained in section 3.4, the BBC now provides a wider range of services compared to 20 years ago, for the same price in real terms.

The licence fee has stayed flat while other goods and services have become more expensive¹⁹⁷. While the level of the licence fee has stayed more or less flat in

nominal terms, the cost of most other communications, recreational and media services has increased. The prices of comparable products increased in the range of 10–40% between 2009–2014 while the licence fee increased by only 2% over the same period.

Index of prices rises of selected goods and services within categories

(2009–2014), nominal prices



Further analysis of the BBC's value for money is contained in an annex to this submission.

¹⁹⁷ Mediatique for the BBC 'Index of Cultural Inflation', August 2015

3.13.5 The BBC will continue to improve efficiency and make savings over the next Charter period

We expect the Budget agreement to result in a c.10% real terms cut in the BBC's funding over the next five years. The BBC will have to make significant further savings to live within this envelope and also to modernise its services, as set out in its Strategy document. Within the funding envelope that has been agreed, we face a strong incentive to maximise efficiencies so we can re-invest as much as possible into front-line services for audiences.

We will need to make a total saving of £700m a year by 2021/22. This £700m represents close to 20% of our expected 2016/17 spend. This is a challenge of the magnitude of our current DQF savings programme, but without the same scope for one-off savings or productive efficiencies. We believe that we can deliver this within the Budget funding agreement, although it will require painful choices.

The BBC Trust and the BBC asked PwC, as part of their work on the BBC's efficiency, to look at the potential rate that the BBC could achieve from purely productive efficiency. PwC evaluated what other organisations are doing, market trends, external benchmarks and what opportunities can be identified from a detailed review of areas of the cost base. The BBC will have to achieve an average savings target of around 3.5% a year over the next five years.

The PwC work recognises the BBC's long history of delivering efficiency means that the future opportunities are inevitably more limited than in the past. They advise that we should aim to achieve around a 1% annual productive efficiency saving, although even this will require major restructuring and significant changes to working practices.¹⁹⁸ This alone will not be enough to fund our existing inflationary

pressures and our on-going capital expenditure. Changes in the scheduling mix, where we will aim to have limited audience impact, alongside careful management of inflation in our long-term contracts, will deliver further required efficiencies of around 1% a year over the period, in addition to those identified by PwC.

We are experiencing significant additional cost pressures in a number of areas including sports rights, drama, natural history and digital skills, given the intense global competition for the best ideas and talent. We may need to extract further efficiency savings to cope with these pressures.

The BBC is implementing a strategy of 'compete or compare' to ensure we deliver the best output for the lowest cost. Currently around two-thirds of the BBC's costs are open to some form of market testing and we will increase that towards 80%. Where we cannot use competition, we will use comparison. Where the private sector has relevant benchmarks, we will use them. We expect to be able to cover nearly 90% of our cost base through either direct competition or rigorous comparison and benchmarking. The remaining 10% of our cost base is activities that are difficult to benchmark due to their unique nature. We will continue to drive efficiency in these areas through activities like lean process reviews.

This programme will be a systematic approach to every major item of BBC spending over a period of five years. It will provide the 'destination model' of efficiency for which the NAO has called. It would represent best practice in the public sector, and compare well to leaders in the regulated private sector.

¹⁹⁸ PwC, 'BBC Efficiency Review Identifying Efficiency Savings for the Next Charter Period Summary Report', September 2015, available here http://downloads.bbc.co.uk/aboutthebbc/insidethebbc/reports/pdf/bbcreport_pwc_efficiencyreport.pdf

3.14

How should the BBC's commercial operations, including BBC Worldwide, be reformed?

Every public service is being asked to deliver more for less, so the BBC needs to have a commercial strategy that supplements the licence fee and delivers as much as possible back into its UK public services. The BBC has built a world-class and growing media business in BBC Worldwide.

The current ownership structure works. BBC Worldwide is materially important to the BBC's overall financial model and its ability to fund content. It is the main vehicle through which the BBC commercially exploits intellectual property (IP) in the UK and globally to generate a cash return to licence fee payers. It serves both as an important source of investment in British original content and is instrumental in showcasing UK content across the globe. The consultation paper suggests that Charter Review should: "consider the full range of options for reform of the BBC's commercial operations including full or part privatisation of Worldwide."

As set out in the BBC Strategy Paper, we have a strategy in place to increase the returns from BBC Worldwide within the current ownership model, by taking advantage of the demand for British programming and new digital opportunities.

Any option to carve out BBC Worldwide from the BBC would not be in the interests of licence fee payers. While every major global player is creating a more integrated system, it would make no sense to go the other way and break up a model that is delivering returns that are essential to support public service programmes. It would make it harder for the BBC to diversify its revenues still further. It would diminish one of the best shop windows to the world for British talent and programme-makers.

3.14.1 BBC Worldwide is a well-run commercial venture and there is no case for a carve-out on the basis of current performance

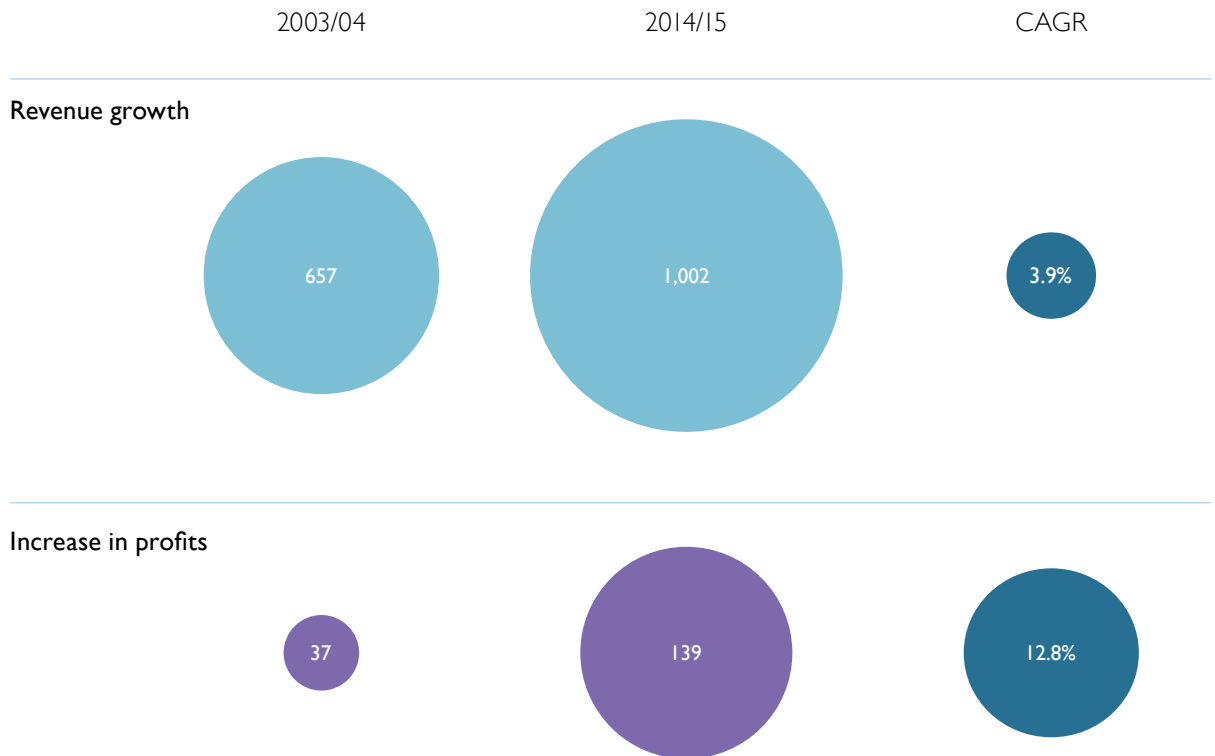
BBC Worldwide has successfully transformed its portfolio over the last ten years, enabling it to deliver sustained and growing cash returns to the BBC, whilst also driving significant benefits to the wider UK creative economy. It has increased returns to the BBC by 6.2% a year, from £168m in 2009/10 to £226m in 2014/15. It has achieved this growth despite facing headwinds from the structural decline in the market for physical sales, notably DVDs. These returns are in line with market peers¹⁹⁹.

As set out in the Strategy document²⁰⁰, BBC Worldwide has a clear funded plan to grow its commercial returns, as a core part of the BBC's mixed funding model. It is expected to deliver £1.2bn in cumulative returns to the BBC over the next five years—a more than 15% increase on returns over the previous five years. As part of its strategy, BBCW will consider further partnership and capital opportunities.

¹⁹⁹ For example, average EBITDA growth between 2011 and 2014 for peer group (Disney, Fox, Viacom, ITV, AMC Networks, Discovery, CBS, RTL) is 7.5% p.a. (range of -3.1% to +15.3%)

²⁰⁰ BBC, 'British, Bold, Creative, The BBC's programmes and services in the next Charter', September 2015, Section 8.2

BBC Worldwide Revenue and profits have grown significantly over the last 10 years, £m



- Key Drivers**
- **Re-focussed on long-term strategy** from short-term cash flow
 - **Diversification of portfolio** into sales, channels and other content
 - **Diversification of content**—50% BBC in-house production and 50% other indie content
 - **Future-looking** with reduced exposure to legacy markets and growth in the digital business

3.14.2 The current ownership model for BBC Worldwide, and the strategic alignment it enables, supports the delivery of the BBC's public service remit

The BBC public service and BBC Worldwide are integral parts of the same enterprise. BBC Worldwide's core business is investing in and exploiting BBC content around the world, whether made in-house or by independent producers.

The strategic vertical integration ensures that BBC Worldwide's activity is consistent with and supports the BBC's public purpose to bring "The UK to the World and the World to the UK", and builds the BBC's brand globally.

This model puts more money on-screen for the British public and takes the best British creativity to global audiences. Over the last couple of years, BBC Worldwide has been investing even more in content. The licence fee paid for less than half the budget of some of the BBC's biggest dramas last year. Our big upcoming dramas like *War and Peace* and *Dickensian* are dependent on co-production deals and investment involving BBC Worldwide.

It is because of BBC Worldwide's special relationship with the BBC that it has scale and access to a strong pipeline of content on a long-term basis. 80% of BBC Worldwide's profits and just under 60% of its

revenues are generated from the exploitation of BBC in-house content. It is because of this special relationship that BBC Worldwide can take British creativity to the world and has been able to attract strong partners for joint ventures, including AMC Networks (BBC America) and Scripps (UKTV). Without the control of distribution and large scale branded destinations under BBC Worldwide, the BBC would have reduced access to the investment, talent and ideas necessary to deliver the breadth and quality of content for its public services. The licence fee would be £10 higher without the sustainable returns generated by BBC Worldwide.

The global market trends in content supply and exploitation suggest that the Worldwide model will become increasingly important in future. The BBC's largest UK and international private sector peers are vertically integrated, enabling them to access, control and monetise content through their own production and distribution assets.

3.14.3 The current regulatory model for BBC Worldwide is well-established and effective

BBC Worldwide is established as a wholly-owned commercial subsidiary of the BBC. To satisfy regulatory obligations that BBC Worldwide must not receive a selective advantage from using licence fee funds, the following arrangements are in place:

- Financial and operational separation, as required in the Charter and Agreement and under EU state aid rules;
- BBC Worldwide must comply with the four commercial criteria set out in the Charter and Agreement: fit with the BBC's public purposes;
- exhibit commercial efficiency; not jeopardise the reputation of the BBC or the value of the BBC brand; and comply with the BBC's Fair Trading guidelines and in particular avoid distorting the market;
- Regulated transfer pricing exists between the BBC and BBC Worldwide for goods and services provided by the BBC, including BBC Worldwide paying fair market rates for BBC content.

How should the current model of governance and regulation for the BBC be reformed?

The BBC welcomes the Government's decision to establish the review into how the BBC is governed and regulated. The BBC will input to this process. We set out below our initial thinking on reform of the BBC's current governance and regulation model, and the principles that should guide it.

3.15.1 BBC governance and regulation should adhere to best practice principles and ensure the BBC operates in the public interest

The BBC's model of governance and regulation should be clear, flexible, proportionate, transparent, easy to understand and enable effective decision-making in response to a fast-moving environment. The new arrangements should fulfil the following core principles:

- Protect the BBC's independence;
- Uphold the interests of licence fee payers ;
- Enable the BBC to remain distinctive and relevant in a fast-moving world;
- Take market impact considerations properly into account;
- Ensure the BBC operates in the public interest, with effective routes for redress when it does not; and
- Ensure a clear separation between corporate governance and regulation.

The three core functions that the BBC's governance and regulatory system must perform as a whole are: corporate governance (the mechanisms by which the BBC is directed and controlled)²⁰¹, regulation (holding the BBC to account for the delivery of its remit and for upholding editorial standards), and public accountability (to licence fee payers and, as appropriate, to political institutions).

Despite having some strengths, the current model does not meet all these tests. We agree with the BBC Trust Chair that there are blurred responsibilities and accountabilities between the Executive Board and the BBC Trust, including in areas of strategy and financial oversight²⁰². The overlapping roles and complicated structures have, in our view, compromised the effectiveness of decision-making. At critical points this has resulted in reduced confidence in the governance and regulation of the BBC. It has also hampered the BBC's agility and flexibility to respond to fast-changing audience needs and market changes. Charter Review presents the opportunity to develop a reformed model that enables the BBC to be better run in line with the above principles, with more effective decision-making and greater clarity between those who run the BBC and those who regulate it.

²⁰¹ Corporate governance is about making sure the BBC is well-run in the interests of licence fee payers, encompassing the following key functions: approving strategy; allocating resources and approving budgets; monitoring performance; audit and risk management; remuneration policy; and overseeing compliance with regulatory codes/frameworks (e.g. Fair Trading).

²⁰² http://www.bbc.co.uk/bbctrust/news/speeches/2015/oxford_media_convention

3.15.2 Implications for any future model of governance and regulation of the BBC

In line with the above principles we believe that the future model for the governance and regulation of the BBC should include:

- A single, unitary, BBC Board independent of Government;
- Ex-post regulation by a single body outside of the Corporation;
- Accountability to licence fee payers to be a core part of corporate governance;
- BBC governance to be responsive to the diversity of the UK.

A single, unitary, BBC Board independent of Government

The new Charter and Agreement should clarify that the BBC is run by a single Board. BBC corporate governance, including the development and approval of strategy, should not be shared between two bodies as currently.

This would ensure that the BBC is more agile in responding to a rapidly changing environment; that there is clarity of roles; and as a result, that the BBC Board is clearly accountable for its decisions and for the BBC's performance and services; and that the external regulator is seen as credible and independent in evaluating BBC decisions, rather than complicit in them. This reflects the view reached by the Culture, Media and Sport Committee's Future of the BBC Report, namely that the introduction of "such a structure for the BBC should enable the Corporation to be more agile and dynamic in undertaking corporate governance and taking strategic decisions on priorities in line with its public purposes".²⁰³

The existing Executive Board should be transformed into a stronger unitary BBC Board composed of a non-executive Chairman and majority of non-executive directors, the Chief Executive in the form of the Director-General and a small number of executives. In line with the UK Code on corporate governance, this would result in a BBC where

responsibilities are distributed across an appropriate balance of executives and non-executives; where the roles of Chairman and Chief Executive are held by different people; and where non-executives—who will be in the majority—play a critical role, providing constructive challenge to executive thinking and ensuring that the BBC operates in the public interest. The independence of the new unitary BBC Board must be safeguarded, including in relation to the appointments process for its members.

Ex-post regulation by a single body outside of the Corporation

The corollary of a shift to a unitary BBC Board with its own Chairman is a move to external regulation by a single body.

Any model built on the principles set out above will need to move, as far as possible, to give primacy to ex-post regulation of the BBC's delivery of its public purposes and remit.

Responsibility for compliance with editorial standards and complaints must also be considered. Under the current model, responsibility for approving the BBC's editorial standards falls to the BBC Trust as does the adjudication of appeals on matters of due impartiality and accuracy. Adjudication on the remaining areas of editorial standards is shared between the BBC Trust and Ofcom where both the BBC's own editorial standards and Ofcom's Broadcasting Code apply. Under a new model, the unitary Board should play an important role in ensuring that the Corporation continues to uphold the public's high expectations of editorial standards at the BBC. However, the question of which body should adjudicate on appeals needs to be considered. The key principles that should guide reform are: to ensure that the BBC's independence is secured, that the processes for complaints and appeals are clear, transparent and proportionate, that there is no overlap in regulatory responsibilities, and that the high expectations of the public continue to be met.

²⁰³ House of Commons Culture, Media and Sport Committee, 'Future of the BBC', Paragraph 296, February 2015

Accountability to audiences to be a core part of governance

The Government raises a question about who the unitary Board should be accountable to. Proper accountability to those who pay for the BBC—licence fee payers—must be a core function of a reformed governance system. We set our initial ideas for how public engagement and accountability could be enhanced in the next Charter in section 3.17 and will develop these in consultation with licence fee payers.

Governance to be responsive to the diversity of the UK

Under a new model, the new unitary BBC Board must be able to take decisions in the best interests of licence fee payers across the UK and to appropriately reflect the increasing diversity of the UK.

3.16

How should Public Value Tests and service licences be reformed and who should have the responsibility for making these decisions?

The constitutional model of the BBC should meet a number of conditions:

- A clear definition of the BBC's public purposes and public service remit and the activities covered by it, that is set by the Charter Review process;
- Entrustment of that remit to the BBC in the Charter & Agreement;
- Effective supervision of fulfilment of the BBC's public purposes and remit;
- Evaluation of the BBC's strategic decisions to make significant changes to the scope of the BBC's services in line with the public purposes, to ensure that the public value outweighs the adverse competitive impact.

3.16.1 Clarifying the Charter and Agreement could make the BBC's remit more accessible, transparent and predictable

Underpinning the BBC's model of governance and regulation are its public purposes and remit. These summarise why the BBC exists and the role it should play. They provide a summary of the high level objectives and characteristics of the services that the BBC should deliver, making it not only possible for licence fee payers and market players to know what to expect from the BBC, but also for there to be requirements against which the BBC's delivery can be assessed.

Under the current model, the BBC's remit is set out in two core documents, the Royal Charter and the Agreement with the Secretary of State. Service-level

aspects of the remit are further elaborated across 26 separate service licence documents, issued by the BBC Trust. We believe that improvements to this model, in line with the above conditions, should be considered. The BBC's public remit and key obligations could be expressed in one place, in the core constitutional documents for the BBC: the Charter and Agreement. This would make the BBC's remit more accessible, efficient and less diffuse, and it would give greater transparency and predictability to licence fee payers, market participants as well as the BBC's future regulator about what the BBC is for and what it should be expected to deliver.

3.16.2 A clearer remit for the BBC in the Charter and Agreement could mean that service licences could be simplified

There are in principle advantages to having a service licence regime which establishes how each service contributes to the BBC's public purposes. It provides a clear signal to audiences and stakeholders about what the BBC is seeking to achieve, sets out boundaries for BBC activity and is expressed in terms of the unit of activity (e.g. TV channel brands) that the public can most easily recognise. It would, therefore, be sensible to retain licences in some form under any new model.

However, the current service licence system presents two issues. First, they are, in our view, unnecessarily detailed and prescriptive, based more on inputs than outcomes, and insufficiently flexible and dynamic to fit with the evolution of service provision for licence fee payers. They need to have the flexibility to evolve with audience expectations and technology, for example, to move from a focus on linear service brands (like BBC

One) to genre based licences (e.g. for news, sport and children's) if these become a more meaningful way of delivering the BBC's output in future. It is also not clear how service licences would fit in a world where the BBC is increasingly working in partnership with others to deliver the public purposes.

Secondly, under a new regulatory model built around ex-post review, the continuation of service licences as a regulatory tool risks maintaining the confusion and overlap of the current system. Service licences are, in reality, a highly specified, ex ante tool of governance and this would bring them into conflict with the overall shift towards establishing a clearer set of roles and split of functions between the BBC Board and its external regulator.

3.16.3 Building on the current system of PVTs

PVTs have introduced greater transparency into BBC decisions about significant changes to the Corporation's scope, and have provided more accountability through a public process of evaluation and review. The introduction of market impact tests have ensured that the BBC's impact on the market is taken into account. However, the current approach is not without its issues. As the Government's consultation sets out: "The PVT can be too blunt an instrument, it is a single, relatively costly and time consuming process."²⁰⁴ The time from the BBC's decision to make a PVT application to approval or rejection has been at least a year for the five PVTs to date. This has two disadvantages. It introduces uncertainty into the market, an issue that the CMS Select Committee highlighted in their report. It also delays changes to the BBC's scope, whether the

launch of new services or reductions in activity to meet funding constraints, to the detriment of licence fee payers.

There are, in addition, two particular areas that merit consideration: first, the 'triggers' for PVTs whose mechanics under the current model would appear to depart from the primary purpose which the PVT system is intended to serve; and second, structures and processes for deciding 'who' makes the PVT decisions, which will need to be considered as part of reforms to BBC governance and regulation.

204 DCMS, 'BBC Charter Review Public Consultation', 16 July 2015, page 70

3.16.4 Triggers for PVTs should focus on market impact risks and the decision-making body should balance the need for accountability and agility

The objectives of the PVT system are to allow the BBC to change its scope and services during the lifetime of the Charter—for example, to respond to changes in public expectations, technology, and market conditions; and to ensure that when the BBC has a significant change of scope proposal, there is a mechanism in place to ensure that the public value of the proposed change outweighs any adverse market impact.

The key principle for how PVTs are triggered, therefore, should be whether a specific proposal poses a significant risk of adverse market impact. This follows a straightforward logic: the public value of any change will, by definition, outweigh the risk of adverse market impact if the change does not present a market impact risk; and so, under this scenario, the new unitary Board should be able to implement strategic decisions, in line with the BBC's public purposes, without the need for a PVT. This would mean, for example, that a year-long PVT was not required before the BBC could close a service in response to financial pressures. The unitary Board would, of course, need to act in accordance with the BBC's public purposes and remit, with due accountability to the public and with ex-post review by the external regulator.

Under the current model, PVTs can be initiated by seven different and broad-ranging triggers. Our view is that these triggers should be streamlined and replaced with a test focused on adverse market impact risks with clearer thresholds. This is not to say that a significant service change would not trigger a PVT, only that it should do so where a specific proposal trips the threshold of a market impact-based test. This would represent a more rational, proportionate and transparent system for initiating PVTs that would bring the triggers in line with the objectives of the system as a whole.

In addition to the triggers for PVTs, the structure of the PVT process will need to be considered in light of wider changes to the BBC's governance and regulatory system. Under any model, our view is that the market impact assessment should remain with Ofcom drawing on its expertise of the sector and its experience undertaking market impact assessments.

There is also a decision about which body should make PVT decisions, balancing public value with the market impact advice provided by Ofcom. We would suggest that the following principles should guide the model: to ensure that it is capable of achieving agility of process, minimising unnecessary delays that create market uncertainty and deprive audiences of services which are valuable to them; to secure a clear split of functions between strategic decision-making and ex post regulation; and to give confidence that judgements take account of market impact while recognising that they are ultimately decisions about the BBC's public service strategy and how it best delivers the public purposes and remit, as set out in the Charter and Agreement.

3.17

How could the BBC improve engagement with licence fee payers and industry, including through research, transparency and complaints handling?

3.17.1 The BBC will do more to engage with licence fee payers and be accountable to them in the next Charter

Every day, the BBC engages with licence fee payers in countless ways. Whether it is taking part in a local radio phone in, joining the Facebook group of a favourite programme, touring Broadcasting House, Mediacity or Pacific Quay, attending one of the BBC's live events like Radio 1's Big Weekend, following a BBC Twitter feed or being one of around 1,500 people a day who contact the BBC Audience Services team with a comment, compliment or complaint, audiences are close to the BBC.

We want to build on this and create an open BBC that has a new, two-way relationship with audiences. We want to engage with audiences as citizens as well as consumers. Our relationship with the British public must be accountable, interactive and creative. We will now engage with licence fee payers and stakeholders about what a full programme of public engagement could be, but we have some initial proposals:

- **Taking part in the design of content and services**—This will take many forms, from asking audiences to share, curate and test new content and products to using MyBBC data to improve audience experiences and the personalisation of services. We will make sure we are entirely transparent with audiences about how we use their data, and in so doing help them understand how their digital data can be used.
- **Corporate decision making**—we will ask audiences to advise us on how we run the BBC. The kind of activities we will explore to do this include:
 - **A BBC Online Forum**—a mass online engagement, research and networking tool developed as an extension of myBBC. We will aim to have 10% of signed-in users actively advising the BBC through an online platform within the next three years;
 - **Deliberative Juries**—purposefully recruited groups so audiences can debate what they want and need from the BBC;
 - **Open data**—As we said in the BBC Strategy Paper, we expect data to become critical to all we do, enabling personalisation and informing choices about commissioning and programme making (although never replacing the judgment of our creative experts)²⁰⁵. We can go further than this—sharing audience data/research with the audience and engaging them and industry stakeholders in data analysis in order to improve content and decision-making.

205 BBC, 'British Bold Creative, The BBC's programmes and services in the next Charter', September 2015, Section 4.3

3.17.2 We can simplify and streamline the way we handle editorial complaints without reducing accountability to audiences

The BBC is accountable to the public and needs to make sure that it deals with their complaints quickly and effectively. The processes we have in place are easily accessible and work well—in 2014/15 we received 260,000 editorial complaints and answered 96% on time. Fewer than 1% of complaints went to appeal by the BBC Trust.

As part of the independent review into how the BBC is governed and regulated, we would like to consider what the options are for reforming the complaints process to ensure that we can continue to provide a good service while focusing resources on the most serious editorial complaints. The options will depend on the nature of any changes made to the BBC's governance and regulatory structures which we cover above.

We believe a reformed complaints system should meet the following principles:

- Ensure the BBC retains high editorial standards;
- Be 'broadcaster first', requiring the complainant to deal with the BBC initially so that the BBC can respond quickly to issues raised. The BBC's regulatory body should not take action without evidence that the BBC had first had the opportunity to investigate and address the issue within the BBC. Its role in editorial complaints handling should be focused on investigating on appeal serious breaches of editorial standards (i.e. substantive issues);
- Continue to be simple and accessible for the public, but reduce the cost to licence fee payers by initially adopting more proportionate approaches to the handling of those complaints which do not raise substantive matters;
- The BBC should only be expected to deal with those complaints in areas over which it has direct control;
- Avoid duplication by having a single regulator body for complaints. At the moment it is possible for both Ofcom and the BBC to be considering the same complaint simultaneously but to come to different conclusions. It is difficult to see how this is helpful to the complainant or a proportionate use of resources.

3.17.3 The BBC has a strong track record in transparency that also takes account of editorial freedoms and effective decision-making

As the Government's consultation paper notes, the BBC takes a proactive approach to transparency. The BBC regularly reports on expenses, gifts and hospitality, audience performance and on senior management pay and talent costs. This is in addition to the BBC's comprehensive annual report and accounts. We continue to keep this under review, but have not seen any evidence that there are significant omissions in the information we publish.

The BBC, like other public sector bodies such as the Bank of England, is subject to the Freedom of Information Act 2000 for certain specified purposes. In 2014 the BBC received more than 2,000 requests under the Act and more than 1,000 of those were considered to be in scope. In relation to more than two thirds of those requests where information was held, the BBC either provided the requested information in full or in part or the information was already publicly available. The BBC also voluntarily disclosed information in relation to hundreds of requests deemed out of scope. The BBC's decisions in this area are subject to review by the independent regulator and the courts.

The BBC's commitment to transparency must be balanced against the need for editorial independence and must take account of the fact that we operate in competitive markets for many of our inputs, including programmes and major rights contracts. It is critical that the BBC, like other public service broadcasters, continues to be subject to the derogation in the Act which excludes material held for the purposes of 'journalism, art or literature' to give our programme-makers and journalists creative freedom to deliver high quality, impartial content. Like other public sector bodies, we must also continue to be able to apply the current exemptions, including to protect commercial interests so that we can preserve the BBC's ability to secure best value for money for licence fee payers and to avoid market distortion. It would not be desirable, for example, if the BBC were required to put information into the public domain about its relationship with external commercial partners which harmed its ability to negotiate to secure best value for licence fee payers. We welcome opportunities to contribute further on this issue and to the work of the Independent Commission on Freedom of Information.

3.17.4 The BBC will maintain high standards in fair trading, ensuring it is accountable to commercial stakeholders without risking market distortion

The BBC does business through engaging with the broadcasting, media and wider creative industries every day. From commissioning independent productions to working with other broadcasters on new distribution technologies, we understand the value of working closely with industry partners.

The BBC has a range of regulatory tools which invite industry engagement such as service licence reviews, the fair trading complaints process and Public Value Tests. We also actively engage both the public and industry before taking a view about the BBC's strategic priorities, for example the BBC Trust is currently consulting on the proposals we published in September²⁰⁶.

The BBC complies with its corporate governance obligations; information about all group companies is held and published by Companies House, including audited group accounts, which are also made available on the BBC's website. The BBC Trust is currently consulting on its Fair Trading Framework and has signalled that it will clarify in its revised documents what information it expects to be published by the BBC about its relationship with its commercial service subsidiaries and about the relationship that exists between them and the public service side of the BBC. In addition, the Trust has this year published a new

framework for commercial services which sets out the arrangements covering the requirements, boundaries and expectations of the operation of the BBC's commercial services. A further study is also planned for later this year looking at issues around transfer pricing and separation in relation to the BBC and its commercial subsidiaries.

It is right that the BBC's fair trading responsibilities, in so far as they apply the principles of state aid and competition law to the BBC, should be made explicit in the Charter and Agreement. There are also currently provisions to ensure financial and organisational separation of the BBC's public and commercial services in line with state aid law and best practice. In addition, there are requirements for the BBC to have regard to the competitive impact of its activities on the wider market, to comply with a fair trading policy and to provide for complaints-handling. These should be retained (or adapted to any new governance and regulatory model) to offer assurance and clarity to others in the market about our continued compliance with state aid and competition law. However, the requirement in the Agreement for there to be a statement of policy on competitive impact goes beyond the application of state aid and competition law to the BBC and is unnecessary as it adds no additional, meaningful 'check' beyond other provisions in the Charter and Agreement.

3.17.5 Partnerships are at the heart of the future BBC and it must become easier to engage with partners for mutual benefit

In section 3.1 of this document we explain that partnership should be an important means of delivering the BBC's public purposes. We want to give people working in the BBC and for partner organisations clarity about the terms under which they can work together and confidence that both sides are acting to achieve maximum impact. To realise the full benefits of partnership, it will be necessary to consider the rules in the Charter and Agreement which restrict how resources other than the licence fee can be used²⁰⁷.

The original intention of the 'alternative finance' rules remains—to ensure compliance with state aid regulation by avoiding over-compensation and maintaining the BBC's editorial independence. But these objectives can be achieved by setting out principles which aid partnerships rather than limiting permitted alternative sources of finance to specific exceptions. The BBC's comprehensive editorial guidelines can be relied upon to safeguard the BBC's reputation and editorial integrity and to guard against any perception of sponsorship.

²⁰⁶ <https://consultations.external.bbc.co.uk/bbc/future-ideas/>

²⁰⁷ Clause 75 of the BBC Agreement (Alternative Finance)

3.18

How should the relationship between Parliament, Government, Ofcom, the National Audit Office and the BBC work? What accountability structure and expectations, including financial transparency and spending controls, should apply?

3.18.1 The BBC's relationship with Government and Parliament may need to be reformed to protect the BBC's operational and strategic independence

One of the core functions that the BBC's governance and regulation must perform is exercising the BBC's accountability to licence fee payers and—as appropriate—to the political institutions of the UK. It is appropriate that Government and Parliament ultimately determine the overall purposes and remit of the BBC. The Charter Review and funding review processes provide a periodic opportunity to assess these issues. It is also right that the BBC is open to proper scrutiny by Parliament, including by Select Committees.

Beyond this, the BBC's editorial, operational and strategic independence is paramount. It is not clear that the BBC's current constitutional model is protecting this independence. The licence fee settlements of October 2010 and July 2015 show that the BBC is vulnerable to being drawn into policy decisions linked to the Budget and Spending Reviews, rather than its funding being determined on its merits after consultation with those who pay for the BBC, licence fee payers, and those who are most affected, the industry. The Charter model itself has strengths (see below) but allows for the Government of the day to make more or less unilateral decisions about the future of the BBC.

It is worth considering what options there are for introducing a more public and open process. We propose three possible reforms for debate (see the next section for further details):

- A move to a Charter term length that provides sufficient long-term security and decouples decisions about the BBC's future from the electoral cycle;
and
- A legal obligation could be introduced in the next Charter for Government to consult licence fee payers and the BBC's regulatory body on future decisions about the funding and scope of the BBC. We discuss the issue of check and balances further in the next section.

In addition, the BBC's wider relationship with Government has become more complicated over the last decade or so. Top-slicing has meant that the licence fee funds departmental spending, potentially bringing the BBC into annual Budget rounds. The fact that the licence fee is now classified as a 'tax' and the BBC is termed an 'arm's length body' of DCMS has brought the BBC into the 'National Accounts'. This has had consequences such as limiting the BBC's and BBC Worldwide's ability to borrow (because any borrowing adds to the public sector net debt). The concern is that the cumulative impact is a BBC that is now less independent than it used to be and than it needs to be.

As a minimum, the BBC's classification as a 'Public Service Broadcasting Authority' should be reconfirmed in the course of Charter Review to ensure that there is no risk of these successive adjustments gradually turning the BBC into a *de facto* Government body. But we also want to debate how else the BBC's independence can be protected. There are a wide range of options and the BBC is not the expert in these areas. But there should be a simple test—the BBC's independence should be assured, with guarantees of how licence fee settlements and Charter Reviews happen in future, and checks and balances to prevent unilateral, fundamental changes to the BBC.

3.18.2 The terms of the relationship between the NAO and BBC should be clarified

The current relationship between the BBC and NAO works well overall. The NAO has been able since 2010 to gain greater access to the BBC to carry out value for money studies on any aspect of the BBC's finance or operations but critically, excluding editorial matters.²⁰⁸ This has resulted in thorough reviews of, for example, the BBC's efficiency programme and property estates. These serve a number of important roles: they give confidence to the general public that the licence fee is being well spent; they help the BBC identify ways it can do even more to improve value; and they provide evidence for Parliament's scrutiny of the BBC through the Public Accounts Committee.

However, there is a case for further revising the terms of this relationship to ensure that:

- The NAO has no doubt about its ability to carry out appropriate value for money reviews, even at relatively short notice; and
- The BBC's independence with regard to the content, choice and scheduling of programming and services is absolutely safeguarded. This editorial carve-out is critical because the NAO's role is to scrutinise public spending for Parliament and if it strays into editorial areas that could effectively invite Parliament (the Public Accounts Committee specifically) to make judgements about editorial matters. The public would not be comfortable with this kind of political interference

in the BBC—a clear majority believe that the BBC should be independent of both Government and MPs in how it spends the licence fee on BBC programmes and services. Further, on weighing up potential greater transparency in how the licence fee is spent compared with potential greater political influence over the BBC, close to 8 in 10 people say that, on balance, committees of MPs should not be able to review in detail how the licence fee is used on BBC programmes and services. The majority of people say that they could be concerned that political influence in the BBC would increase if MPs could review in this way how the licence fee is used.²⁰⁹ It is, in any case, in line with the NAO's and PAC's stated approach towards other Government departments and public bodies: 'we do not question Government policies but examine objectively and independently... value for money'²¹⁰. However, in the case of the BBC—where freedom to make editorial decisions without fear of political consequences is paramount—this boundary needs to be absolutely explicit.

These changes to the relationship can be achieved by revisions to the BBC Agreement that:

- The NAO should continue to determine its value for money reviews and share the annual programme with the BBC each year. The restrictions on the NAO which stop it from changing its annual BBC programme with less than 3 months' notice or carrying out a study on an

208 The 2011 Amendment to the Agreement sets out the NAO's access arrangements, confirming that "(16) Nothing in this clause entitles the CAG to question the merits of any editorial or creative judgment which is made by or on behalf of the BBC, or of any policy objective of the BBC relating to the manner in which BBC services are made or distributed."

209 Ipsos MORI for the BBC, 1,032 UK adults 18+, October 2015

210 NAO website, <http://www.nao.org.uk/about-us/>

area already under review by the Trust (if it has a public interest justification) should be removed. The BBC Trust has already agreed in 2013 not to delay the NAO from pursuing a review and to disregard the 3 month requirement. This should now be reflected formally via changes to the Agreement;

and

- Strengthen the current protection against the NAO questioning the BBC's editorial or creative judgements or policy on its services by codifying the BBC's right to refuse access if the NAO seeks to conduct a study that veers into editorial or creative decision-making, and to remove any NAO conclusion or recommendation that questioned an editorial judgement.

These changes would allow the NAO greater flexibility and agility in its scrutiny of the BBC without risking the BBC's editorial independence. A solution that gives the NAO greater access but with protections for the BBC's editorial independence is the public's preferred option²¹¹. There would be no further benefit to putting the BBC and NAO relationship on a statutory basis as this would not, in practice, increase the NAO's access to the BBC but could weaken the BBC's editorial protections. The BBC welcomes thorough scrutiny of its Annual Report and Accounts which is why it opens up the role of external auditor to competition on a regular basis and makes the appointment on the basis of relevant experience and expertise.

211 Populus for the BBC, 2,101 UK adults 18+. When the issue is explained to the public, 41% say that the NAO should have more access than today to information about BBC finances but with protections for BBC editorial and programme decisions; 16% say that the NAO should have more access than today but without protections for BBC editorial and programme decisions; 19% say that there should be no change and that the NAO should have no more access than they already do today; 24% don't know

Should the existing approach of a 10-year Royal Charter and Framework Agreement continue?

3.19.1 A long-term Charter underpins the BBC's independence but the debate about the BBC's scale and funding should be taken out of the political cycle in the future

The Charter model underpins the BBC's governance structure and funding model, and explicitly commits the Government of the day to respect the editorial and operational independence of the BBC.²¹² The continuity that a ten year Charter provides enables the BBC to take a long-term, strategic approach to its investments and to the delivery of its remit. It provides the stability and confidence to adapt to changing audience needs and to modernise PSB. The Charter also has a symbolic value emphasising to the UK public and stakeholders the special role and responsibilities which the BBC has as an independent broadcaster and trusted national institution. In contrast, a shift to a five year Charter would lead to permanent review of the BBC which would create instability and risk its independence.

Charters of ten plus years have been the norm for all but one agreed since 1927²¹³. At the last Charter Review, it was concluded that the best way of giving the BBC the independence and stability it needs would be to renew its Royal Charter for ten more years. The case for a long-term, ten year Charter still stands.

The vast majority of the public believe it to be of real importance for the BBC to be independent from the Government of the day²¹⁴. Though it contains provision in itself for the BBC's independence, once agreed and set, the Charter provides some insulation from political interference and builds in protection from ad-hoc challenges to the BBC's founding basis from statutory amendments.

The Government's consultation paper suggests that there is a trade-off between flexibility and certainty with a long-term Charter. This has not been evident over the past decade—a period of significant change for the BBC and the sector—at either a technological or constitutional level.

In fact, a tradition of long-term Charters is one of the conditions that have enabled the BBC to develop new technologies and keep up with changing audiences. Alongside the licence fee, it gives the BBC the certainty it needs to take a long-term, strategic approach to innovation and investments. A shorter Charter period would compromise these benefits. Indeed, this has been recognised by the wider industry, who also argued to maintain a long-term Charter in evidence to the select committee's inquiry.²¹⁵

The ten year Charter allows the BBC to invest efficiently in long-term strategic assets which are essential to delivering its services. It allowed the BBC to manage a seven-year digital television switchover process and establish a new base in Mediacity for example. The BBC can make deals and partnerships—such as in sports rights deals and joint ventures—but these may be more challenging and complex to negotiate if the Charter is renewed on a five-year basis.

The BBC's constitution has also allowed flexibility to change over the past ten years—though crucially as an important safeguard to independence—by mutual consent between the BBC and the Government. Whilst the Charter provides a guiding framework, the detail is set out in the Agreement which can and has been revised.

212 The Charter includes a clause on 'the independence of the BBC', stating that 'the BBC shall be independent in all matters concerning the content of its output, the times and manner in which this supplied, and in the management of its affairs'

213 The exception was following the Second World War in 1947

214 ICM Unlimited for the BBC Trust, 'Future Priorities for the BBC, An Audience View', 2111, November- December 2014: 'When it comes to things that you think the BBC should focus on in the future, how important would you say each of the following are?' 83% of the public believe it is either very or fairly important to ensure that the BBC is independent from government and MPs.

215 See Channel 4 and PACT submissions to the Commons Culture, Media and Sport Select Committee Inquiry into the Future of the BBC, December 2013

The introduction of fixed term parliaments has provided greater certainty on the electoral cycle. The Charter term can now be set with greater certainty of keeping it out of step with elections. A shift to 'a new normal' of Charters of five years would lock into five year fixed electoral terms, and therefore risk the BBC itself becoming a routine fixture of political debate during every election at the very point where its independence is paramount.

The Charter Review process should include thorough and detailed public consultation, research and debate. It takes considerable time and resource in both the BBC and Government. Doubling up this process to every five years would reduce its value—taking on a shorter term perspective—but increase its cost for all parties involved.

We propose instead that an 11 year Charter is introduced in order to take the BBC out of the political cycle and so strengthen its independence.

3.19.2 A wider range of inputs is required into the BBC Charter and funding processes including the right of the public to be consulted

An 11 year Charter will not alone be sufficient to safeguard the BBC's independence. To do that, we need to consider new constitutional safeguards and a wider range of inputs to major decisions about the future of the BBC.

The public is not convinced that decisions about the BBC should lie in the hands of politicians. Across all governance and accountability functions tested by ICM Research recently, two thirds or more felt that responsibility should lie with an independent body or the BBC.²¹⁶

Charter Review is an opportunity to look again at *how* decisions about the BBC's funding and role are taken and consider changes.

Firstly, it is critical that the voices of licence fee payers, who fund the BBC, are formally heard in the debates about the role as well as the funding of the BBC. The last two licence fee settlements were not good processes and did not meet the public's expectations. To ensure that the public and stakeholders are properly consulted about the role and funding of the BBC, we propose that this is made a legal requirement in the new Charter.

Secondly, the Charter model itself has many strengths but the process effectively allows for the Government of the day to make significant decisions unilaterally. The last two funding settlements show that the BBC is vulnerable to being drawn into wider Government spending and policy decisions, rather than our funding being determined on its merits after consultation with audiences and the industry.

The last Charter Review included measures that made the BBC more independent, flexible and accountable. One important example was the transfer of powers of approval for launching new services away from the Secretary of State.

The Royal Charter on press regulation, approved in 2013, includes independence safeguards that may be relevant to the circumstances of the BBC. A change to the Press Charter explicitly requires the consent of the supervisory body: *"a proposed change must be ratified by a resolution that has been passed unanimously by all of the Members of the Board, who shall determine the matter at a meeting duly convened for the purpose"*²¹⁷. In practice, this has been the case with changes to the BBC's Agreement, but the codification requiring the BBC's regulator to be formally consulted on role and funding would potentially provide greater security when the Charter itself is reviewed. As with the Charter for the Press, this sort of provision could be specifically provided for in the BBC Charter itself.

We note that in the case of the Press Charter, a further protection from a unanimous action by the Privy Council was added by the requirement of a parliamentary vote in both Houses in order to ratify a significant change to the Charter. We also note that legislation was passed to protect the Charter, with the provision that: *'for generations to come Ministers cannot interfere with this new system without explicit and extensive support from both Houses. That is an important step forward'*. We note that legislation was passed to protect the Charter, with the provision that: *"where a body is established by Royal Charter after 1 March 2013 with functions relating to the carrying on of an industry, no recommendation may be made to Her Majesty in Council to amend the body's Charter or dissolve the body unless any requirements included in the Charter on the date it is granted for Parliament to approve the amendment or dissolution have been met"*.²¹⁸

The application of these sorts of safeguards to widen the inputs to important decisions about the BBC's role and funding should be debated in the Charter Review process.

216 ICM Unlimited for the BBC Trust, 'Future Priorities for the BBC, An Audience View', 2111, November- December 2014

217 Royal Charter on Self-Regulation of the Press, Section 9, available here https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/254116/Final_Royal_Charter_25_October_2013_clean_Final_pdf

218 Section 96 of the Enterprise and Regulatory Reform Act 2013 (Royal Charters: requirements for parliamentary approval)