

Response of Channel 5 Broadcasting Ltd (Five) to *Preparing for the Digital Future*, Phase Two of Ofcom's Second Public Service Broadcasting Review

INTRODUCTION

Five welcomes the opportunity to respond to this second document in Ofcom's review of public service broadcasting (PSB). The paper refines and develops the analysis and options set out in Ofcom's first document, and we have been impressed by the breadth of research in it. However, it has not led us to change the basic approach and analysis set out in our response¹ to Ofcom's opening report.

We continue to believe the current PSB system is capable of delivering considerable public service outcomes for some time to come, including through on-line and on-demand platforms, and that a managed evolution of that system is preferable to radical restructuring. To that end, Five strongly supports Ofcom's proposals to relax Five's origination quotas; this will help us deliver our public service obligations, while not having any detrimental effects for viewers.

Five continues to see our PSB status as an important and defining part of our identity. We believe Five contributes significantly to the overall strengths of the PSB system, providing additional breadth and range in a number of areas. As we argued in our previous response, we see Five's core PSB offering centring on distinctive news, an extensive portfolio of children's programmes and the provision of factual programming in peak time.

We also believe the purposes of public service broadcasting are served better by rolling forward as much of the present system as possible than by replacing it with a series of untried initiatives. We believe Ofcom should concentrate on examining how the current system can evolve, for example by looking at more targeted roles for the commercial PSBs, by exploring proposals for partnerships with the BBC and by ensuring a more congenial regulatory environment. We remain sceptical of the case for additional public funding, and are not persuaded by Ofcom's arguments that it is necessary in all three of its putative models. The regulatory assets that Ofcom has identified in the current system have considerable value, and can help underpin the system for some years to come – especially if combined with help in kind from the BBC.

¹ Response of Channel 5 Broadcasting Ltd (Five) to *The Digital Opportunity*, Phase One of Ofcom's Second Public Service Broadcasting Review, June 2008

The current major downturn in advertising revenues is putting severe pressures on the finances of Five and the other commercial PSBs. Like ITV and Channel 4, we are examining our cost base forensically and reviewing all current spending plans and future investments. However, we believe Ofcom must be careful not to conflate the current cyclical phenomena with the structural factors that restrict the future value of the PSB licences.

FIVE'S PUBLIC SERVICE CONTRIBUTION

Five has already set out at length how we see our contribution to public service broadcasting, both now and in the future². We believe it is important for Ofcom to remember that Five is proud to be a public service broadcaster and wants to continue playing a significant role in public service broadcasting well into the future.

Five was created as a public service broadcaster for the digital age, our public service obligations suited to the competitive multi-channel environment in which we launched. Over the last eleven years, even though market conditions have got tougher, we have realised a significant range of public service outcomes.

We have invested heavily in original UK production - **spending over one billion pounds commissioning over a thousand independent production companies**. We have delivered a fresh and distinctive news service, garnered reputations in a range of factual genres, established ourselves as a major provider of programmes for younger children, and developed a distinct voice and outlook that provides a point of difference to the other PSBs. We have also given both on-screen and off-screen talent their first breaks, thereby adding to the talent pool available to all the PSBs.

Five delivers real additional value to the PSB system by providing a range of accessible programmes and a different style and approach. This may not be reflected fully in Ofcom's audience research: precisely because Five is younger and smaller than the other PSBs, audiences will not have as rounded a view of our schedule as of the other PSBs'. (It is telling that Ofcom research found "for Five, agreement that it achieves its [PSB] targets was higher ... most notably, among those who said they watched Five most often"³).

Five remains committed to being a PSB both currently and in the future. We accept Ofcom's analysis that "For Five, the benefits of PSB status are likely to outweigh the cost of its obligations up to and beyond digital switchover"⁴. There is therefore a real incentive for Five to make a success out of being a PSB. We remain committed to providing a quality news service, extensive factual programming in peak and an enhanced commitment to children's programmes, even though the economic downturn is going to temper our commercial prospects over the next few years.

² See: Initial Submission by Channel 5 Broadcasting Ltd (Five) to Ofcom's Second Review of Public Service Television Broadcasting, November 2007; Further Submission by Channel 5 Broadcasting Ltd (Five) to Ofcom's Second Review of Public Service Television Broadcasting, February 2008; and our Response to *The Digital Opportunity*, June 2008

³ *Preparing for the Digital Future, Annex 6: Assessing the value of public service programming on ITV1, Channel 4 and Five*

⁴ *Preparing for the Digital Future*, Page 116

We stated in our previous submission that we were “interested in discussing with Ofcom a more explicit commitment to Five’s provision of children’s programmes as part of a long-term PSB settlement that would entrench our commitment within the PSB system”⁵. We are now prepared to commit to a minimum number of hours of original children’s programmes a year for the foreseeable future.

So long as there is an appropriate regulatory environment (which includes a reduction in our origination quotas and congenial advertising rules), Five will continue to deliver considerable public value without additional public support.

CONSULTATION QUESTIONS

Section 4: Models

1) Do you agree that public service provision and funding beyond the BBC is an important part of any future system?

Five continues to believe there should be public service provision beyond the BBC. We also believe the existing commercial PSBs – ITV1, Channel 4 and Five - can continue to deliver public value for many years, even if overall levels of such provision are not as great in future as they have been in the past.

We believe that genuine plurality requires a multiplicity of providers, which together can offer real creative competition and alternative contributions to the BBC. On its own, no single commercial broadcaster has the range or depth to match the BBC – but together the three commercial PSBs, with their different styles and strengths, can provide a range of outcomes that are complementary to its offering.

Ofcom should also recognise how resilient the PSB system has proved in adapting to new business opportunities while continuing to deliver public service outcomes – whether through launching digital channels or pioneering video on demand services. We believe the BBC and the commercial public service broadcasters are well placed to help the development of the next phase of digital services, as is becoming clear with the development of the iPlayer, Demand Five and the ITV and Channel 4 equivalents.

Five is not convinced by Ofcom’s arguments in favour of additional public funding, whichever of its three models might be adopted. Instead, we favour an approach based on:

- defining more closely the roles to be played by each of the commercial PSBs, and seeing what they and the market together can deliver
- sweating PSB assets through partnerships between the BBC and the commercial broadcasters, for example through exploring production efficiencies, exploiting content in international markets and cross-promotion of selected “at risk” programmes on BBC airtime
- advertising rules that are congenial to all the commercial PSBs, which requires a suitable conclusion of the RADA and CRR reviews

⁵ Response of Channel 5 Broadcasting Ltd (Five) to *The Digital Opportunity*, page 18

- some relaxation of regulatory burdens, such as the proposed amendment to Five's origination quotas, the rationalisation of regional news requirements on ITV and a reduction in planned spectrum charges
- a full review of the regulation of public service broadcasters' terms of trade with independent producers, designed to better reflect the changing balance of risk and reward in broadcaster-funded content

We accept that in the longer term there might be a case for some discrete public funding of specific services such as news in the nations and regions, but we do not believe it is necessary to commit to such expenditure at the present time. We would also be opposed to top-slicing the BBC licence fee in order to provide funds for such a purpose.

2) Which of the three refined models do you think is most appropriate?

The Evolution Model

As Five is fully committed to continuing as a PSB, the only model acceptable to us is the "Evolution" model. We see no point in dismantling the present PSB system while it is still capable of delivering a range of public service outcomes, in favour of untried alternatives.

We also believe the evolution model will allow many of the values of PSB to be transferred into the broader digital world, with the development of on-demand and on-line content and applications by all the PSBs. We think the prospect of major strategic partnerships between the BBC and the commercial PSBs, which allow some of the BBC's technological expertise and brand strength to be used for the benefit of all the PSBs, will greatly help this objective.

The Five Licence

In this context, it is completely unacceptable for the Five licence to be opened up to competition from other providers, as Ofcom suggests⁶. This would run counter to the process established by Parliament for the renewal of the Channel 3 and Channel 5 licenses, which allows licensees to apply for renewal of their licences without any such open competition⁷.

We find it hard to see how such a move could be presented as part of an "evolution" strategy designed to preserve the PSB system, as it could cripple a business that had proved its ability to deliver PSB outcomes over the life of its licence. Five's shareholder RTL has invested millions of pounds in our business, with limited return, on the basis of a legislative and regulatory regime that provided an opportunity to apply for renewal of Five's licence after 2014. We do not see the justification for such investment decisions to be undermined retrospectively.

⁶ *Preparing for the Digital Future*, Paragraph 4.52

⁷ Communications Act, s216

We believe a proposal to open up competition for both Channel 3 and Channel 5 licences would discriminate in practice against Five. It is hard to see how ITV plc would face any meaningful competition for its licenses, because of its entrenched position as the broadcaster of the most popular commercial channel. The channel 3 licences would be of extremely limited value without ITV's programming strengths; and ITV plc would have no incentive to sell its programming to new Channel 3 licensees as it could always broadcast its programmes on non-PSB DTT capacity that it already owns.

Conversely, it would be far easier for a rival company to replicate Five's business, because of our publisher/broadcaster model and our substantial investment in acquisitions. A successful counter-bidder could acquire our programme contracts, while we would have no viable alternative access to market for our family of channels.

If Ofcom pursues this idea any further, Five and RTL demand the opportunity to discuss in detail the purpose, rationale and implications of such a move before any final decision is taken.

Rejecting the Other Models

Our views on Ofcom's other two models were set out in our response⁸ to the phase one document. We said then that a BBC/Channel 4 model would "dispense with the PSB contributions of ITV1 and Five, thereby reducing plurality, reach and impact - and put the overwhelming burden of providing competition to the BBC on Channel 4's shoulders". And we argued that a system of competitive funding "would be less trusted, flexible, innovative and cost-effective than the current model. In place of a system of PSB, based on established institutions valued by viewers, there would be an untried and unstable patchwork of providers, with varying levels of access to market".

3) Do you agree that in any future model Channel 4 should have an extended remit to innovate and provide distinctive UK content across platforms? If so, should it receive additional funding directly, or should it have to compete for funding?

Five remains unpersuaded of the case for public funding of Channel 4. We also believe any public funding of Channel 4 raises serious issues of accountability, governance, state aid and market impact, which have been addressed only partly by Ofcom⁹. Because we believe such issues are of crucial importance to the debate about Channel 4 and public funding generally, we commissioned Perspective Associates to provide advice on them. Their report is attached as an Annex to this submission, and is discussed as part of our response to section 6.

⁸ Response of Channel 5 Broadcasting Ltd (Five) to *The Digital Opportunity*, pages 13-4

⁹ *Preparing for the Digital Future*, paragraphs 6.90-6.98

Public funding for Channel 4 is proposed for two separate reasons: to make up the so-called "funding gap" between the PSB outcomes that Channel 4 would like to deliver and those it believes it will be able to afford; and to fund "an extended remit to innovate and provide distinctive UK content across platforms".

Funding the Channel 4 Remit

The model used by Channel 4 and Ofcom is based on preserving the shape of Channel 4's 2006 schedule. But no-one has carried out an exercise based on assessing the extent to which Channel 4 could fulfil its PSB remit within its existing and foreseeable resources (and discounting the harsh but temporary difficulties being suffered by all advertiser-funded businesses as a result of the current economic downturn). Five is a smaller company than Channel 4, but can still deliver considerable public service outcomes while seeking to make a return to our shareholder. Channel 4 has a much stronger market position, considerable brand recognition and more valuable regulatory assets and does not have to pay any dividend. That suggests it should be able to generate extensive public value without external intervention.

We also believe that Ofcom's £80m estimate for the medium term value of Channel 4's regulatory assets (including its not-for-profit status and its ownership of half a PSB multiplex) seriously undervalues these resources. Our own summary analysis suggests that in 2012 the annual value of Channel 4's public status and regulatory assets will be well in excess of £100m, and could be nearer £150m - which would allow it still to deliver considerable public value.

Extending the Channel 4 Remit

It obviously makes sound commercial sense for Channel 4, like Five and other major broadcasters, to make its programmes available on an on-demand basis and to provide on-line content that complements its main service. In the process, many of the values of the PSB system will be transferred to the digital world. However, we do not believe the argument for Channel 4 to have a public remit to provide non-commercial and (by implication) loss-making content on-line has been tested sufficiently robustly.

Five believes that, before agreeing to such an extended remit for Channel 4, government needs to consider:

- exactly what it requires Channel 4 to do outside television
- what commercial business models might be available to fund it
- what impact such funding might have on commercial on-line enterprises
- how it can ensure any money provided for Channel 4's on-line provision is not used to subsidise the broadcast part of its business and hence allow it to compete unfairly in the television advertising market

Five does not believe the case has yet been made for a second broadcast-based provider of on-line content in addition to the BBC. There are many other ways of

publicly funding on-line content, as reports¹⁰ for Ofcom have demonstrated. We are also concerned that extending Channel 4's remit would be like unravelling a ball of string – there would be no clear limits to what it was expected or required to do, so over time its demands on public funds would be inclined to expand.

4) Do you think ITV1, Five and Teletext should continue to have public service obligations after 2014? Where ITV1 has an ongoing role, do you agree that the Channel 3 licensing structure should be simplified, if so what form of licensing would be most appropriate?

Five remains committed to being a public service broadcaster, as we set out above in the introductory section "Five's public service contribution".

We have also made clear our belief that the public interest is best served if both Five and ITV continue as PSBs. The PSB system is greatly valued by viewers (as Ofcom's research demonstrates), and has served the UK well. We believe it would be perverse to wind up the system when it still has demonstrable strengths.

Five's PSB offering centres on a distinctive and accessible news service, an extensive range of factual programmes in peak time, being the main provider outside the BBC of UK programming for younger children and funding a significant quantity of UK production. Five has volunteered that this commitment to children's programmes be formalised in the form of a quota similar to those for news and current affairs. We are also committed to making our children's content available on-line and on-demand.

Further Provision of Children's Programmes

We recognise the importance of UK-originated programmes for older children being provided by broadcasters other than the BBC. But we are not sure to what extent Five can make a major contribution to the provision of such programmes.

Our well-established and highly regarded *Milkshake!* brand for children up to the age of seven comprises 22 hours of predominately UK-produced programmes every week, is widely watched by its target audience, and has a strong reputation among parents. Therefore, we are able to bring real weight and substance to our role of providing a PSB alternative to CBeebies.

The programmes we used to make for older children, although well-regarded and of high quality, did not attract audiences equivalent in size to *Milkshake!* That was a major factor in our decision to withdraw from such programmes in 2007. Five is currently looking at providing a modest number of programmes for older children in future. However, the size of commitment we are likely to be able to make will have only limited reach and impact, so may not make a great difference to the plurality of provision for older children.

¹⁰ *The Digital Opportunity*, Annexes 8 and 9 - reports by MTM London

An alternative approach might be the launch of a stand-alone children's channel committed to predominately UK content. The financial barriers to providing such a channel on all major platforms are considerable, but we would be interested in discussing this further with Ofcom.

Channel 3 Licences

We recognise the sense in simplifying the Channel 3 licensing structure if that can help ITV provide regional news in the future. We note that Parliament has already given Ofcom power to vary the Channel 3 licences by area and time¹¹.

5) What role should competition for funding play in future? In which areas of content? What comments do you have on our description of how this might work in practice?

Five continues to believe it is preferable to fund public service broadcasting through the provision of long-term licences that reflect both regulatory assets and public service obligations than a series of piecemeal commercial contracts. We believe a broad range of public service outcomes is far more likely to be delivered by the three largest commercial broadcasters, each with a history and commitment to PSB, than by a series of unconnected contracts from providers who might well not be able to deliver the reach and impact necessary to justify the public investment. This is most keenly acknowledged by Ofcom's discussion of news provision in the nations and regions, where it says, "The weakness of all competitive funding models is the cost involved in achieving anything like the reach and impact currently achieved by the ITV nations/regions network"¹².

Five acknowledges that there may be some isolated and specific instances where competitive funding is the best way to achieve a particular aim. For example, it made better sense for the Teachers TV contract to be awarded on such a basis than for a requirement to carry such a service, with its limited target audience, to have been shoe-horned into an existing broadcaster's licence.

Five believes public service broadcasting can best be maintained beyond 2014 by agreeing new licence terms with the existing networks that set out the PSB obligations of each. These terms should recognise a greater differentiation of roles for each of the commercial PSBs, with each one playing to our strengths. That would ensure a sustainable future for PSB, even if at a more modest level than at present.

¹¹ Communications Act, s216 (7)

¹² *Preparing for the Digital Future*, paragraph 5.43

Section 5: Long-term: nations and regions

1) Do you agree with our findings that nations and regions news continues to have an important role and that additional funding should be provided to sustain it?

Five has always been a pan-UK broadcaster, but we recognise the importance viewers attach to news in the nations and regions. We believe the proposed reorganisation of ITV's regional news provision will help make this affordable for some years to come. We also believe this may be sustainable for longer than ITV and Ofcom currently suggest, not least when all the advantages of the BBC's partnership proposals (which we understand include the sharing of resources and newsgathering at regional level) are factored in.

We believe any proposal to provide public money to fund regional news will require appropriate governance arrangements and close examination of the potential market impact on the rest of the television industry. We would also favour examination of market-based options – such as collaboration between local/regional newspapers and radio stations – before agreeing to public funding.

2) Which of the three refined models do you think is most appropriate in the devolved nations?

Five believes the evolution model forms the most sensible basis for the continued provision of discrete programming in the devolved nations, as only ITV has the infrastructure and scale needed to deliver a comprehensive service.

3) Do you agree with our analysis of the future potential for local content services?

Five has no comments on this.

Section 6: Funding

1) Do you agree with our assessment of each possible funding source, in terms of its scale, advantages and disadvantages?

Five believes the PSBs' existing regulatory assets, in particular DTT spectrum, are of real and continuing benefit. We have already shared with Ofcom our estimate of their value to Five. We believe Ofcom may have underestimated their value to ITV and Channel 4. We have already indicated the reasons why we believe Ofcom has underestimated the value to Channel 4 of being a PSB; we believe similar analysis could be applied to ITV. In particular, we question whether Ofcom's counterfactual analysis looked at the extent to which both ITV and Channel 4 benefit from making their services available on a wholly-owned multiplex with near-universal reach and the ability to sell advertising regionally (all flowing from PSB status).

Spectrum Pricing

We are pleased Ofcom is continuing to consider carefully the potential impact on the provision of PSB of introducing spectrum pricing. Without mitigation, spectrum pricing will lead to a direct reduction in the levels of PSB that the system can provide. We would welcome an early decision that spectrum pricing be set at zero for PSB channels.

Advertising Minutage

We are glad Ofcom is minded not to sanction any increase in advertising minutage in light of the widespread opposition to it. This will go a substantial way to meeting Five's requirement for congenial advertising regulation to support PSB, although we continue to believe that a reduction in average advertising minutes allowed on non-PSB channels to PSB levels would deliver real benefits to the PSB system, especially at the present time.

CRR

We hope Ofcom and the OFT recommend the maintenance or strengthening of the CRR Undertakings, as the other part of the requirement for advertising regulation appropriate to all PSBs. ITV Sales has 46% of the spot advertising market, which clearly requires continuing regulatory restrictions.

Terms of Trade

Another issue that we believe Ofcom needs to address is the regulation of the public service broadcasters' terms of trade with independent producers. In order to retain a viable model for original UK production, broadcasters need to develop value in increasingly important on-line platforms. The current terms of trade regime limits the ability, particularly of publisher/broadcasters like Five, to invest as significantly as they might in original UK production. We believe the terms of trade need to be revised to better reflect the changing balance of risk and reward in broadcaster-funded content.

BBC Partnerships

Five believes the most interesting and potentially productive ideas for increasing resources available to PSB lie in partnerships with the BBC. The BBC has considerable technological expertise, huge scale and a major brand position. If such resources, which already exist within the PSB system, could be utilised for the benefit of all PSBs, it would represent a major step in underpinning the PSB system for years ahead and in assisting all PSBs to transition to the all-digital world. In many ways, the biggest challenge for the PSB system is to make itself as relevant in the new media as it has traditionally been in the old.

We welcome the BBC's proposals to share its expertise and resources and have had a series of fruitful bilateral discussions with them.

In addition, we continue to find considerable merit in the idea of some of the BBC's promotional airtime being used to cross-promote PSB programmes on commercial channels. This has the clear advantage of targeting resource on defined PSB programmes, rather than providing a subvention that might not all be spent on PSB. It is not clear how Ofcom has arrived at its estimate for the value of this help; we would welcome further analysis.

One further advantage of proposals for BBC partnership, which appears not to have been explored by Ofcom, is that they would be more cost effective than any direct transfer of resources to commercial PSBs. Direct transfer arrangements would not only have to meet the costs of funding PSB programmes but also cover the opportunity costs to commercial broadcasters of providing appropriate slots in their schedules.

Help in kind would reinforce the PSB system because it would be provided on the basis of co-operation and collaboration. In contrast, topslicing the Licence Fee would be combative, as it would pitch the BBC in direct competition with other actual or potential Licence Fee recipients.

The Licence Fee

The most striking aspect of Ofcom's research into the potential use of the Licence Fee to fund broadcasters other than the BBC is the lack of enthusiasm for it among licence fee payers. Ofcom found that the most popular option for using the so-called "switchover surplus" was to reduce the cost of the licence fee. More than twice as many people (63%) favoured this option to giving the money to provide PSB programming on Channel 4 (31%)¹³. We also note that the latter option was considered no more favourably than other public policy options such as extending broadband availability (41%) or DAB access (33%) or funding new BBC digital services (31%).

Other Revenue Sources

We see no new reason to alter our opposition to a new industry levy to support PSB. We also believe any further consideration of this option needs to factor in the lengthy amount of time that would be needed to gain broad political acceptability for it and to arrive at a practical and even-handed way of generating revenue.

Ofcom's analysis shows government is prepared to fund directly some discrete public services. We seriously doubt whether the public would find it acceptable for national lottery funds to be used for the provision of programmes on commercial PSBs.

¹³ *Preparing for the Digital Future*, Annex 8, pages 5 and 10

2) What source or sources of funding do you think are most appropriate for the future provision of public service content beyond the BBC?

Five believes the options that should be pursued are a combination of retaining regulatory assets with the existing broadcasters, appropriate policy decisions on advertising regulation, spectrum pricing and terms of trade, and exploring the considerable potential that exists for partnerships with the BBC. This will be the best way to preserve the major features of the current system, to help it transition to the all-digital age and to ensure it continues to deliver public value beyond digital switchover.

If government believes there is a need for some discrete service to be funded publicly, then it should be provided out of general taxation, in the way that S4C, Teachers TV and MG Alba are funded.

Five remains completely opposed to using any part of the license fee or industry levy to fund PSB outside the BBC, for the reasons we set out in our previous response¹⁴. Top-slicing would remove the clear and transparent link between the licence fee and the BBC, create new forms of conflict between the BBC and commercial broadcasters, prove burdensome to administer and not lead to any overall increase in the volume of PSB programming.

3) Which of the potential approaches to funding for Channel 4 do you favour?

We have already made clear above that we are unpersuaded of the case for public funding of Channel 4, and believe Channel 4 can continue to deliver considerable public benefit on the basis of its existing regulatory assets (including its not-for-profit status), plus availing itself of the opportunities for partnership with the BBC. We also believe it would be wrong to conflate the structural issue of how Channel 4 delivers its public service remit in future with the cyclical problems flowing from the current economic downturn, from which all advertiser-funded broadcasters are suffering.

Of the funding options considered by Ofcom, three involve a direct injection of public funds; we have already made clear our opposition to top-slicing the licence fee and to new industry levies; direct public funding would be the least worst of these three.

Five's Regulatory Assets

The fourth option would destroy public value in ITV1 and Five by taking away our regulatory assets, while not guaranteeing an equivalent increase in public value delivered by Channel 4. Plans for a second PSB channel run by Channel 4 would need to be subject to considerable scrutiny: it is not clear how such a channel could be commercially viable while delivering sizeable public value additional to that on Channel 4.

¹⁴ Response of Channel 5 Broadcasting Ltd (Five) to *The Digital Opportunity*, page 10

We are alarmed, amazed and angry at the parenthetical suggestion that ITV1 be guaranteed a slot on the Digital3and4 multiplex while no equivalent slots were reserved for Five or indeed for S4C, in spite of the recent Parliamentary Order¹⁵ guaranteeing our positions on the multiplex. Five expects to have the opportunity to discuss in detail the purpose, rationale and implications of such a discriminatory approach before it was pursued further. We would find it totally unacceptable if both ITV and Five were deprived of our PSB licences but ITV1 was nonetheless guaranteed a position on a PSB multiplex while Five was not. Such a move would be blatantly discriminatory.

The BBC and Channel 4

We do not believe the proposal to give Channel 4 entire or partial control of BBC Worldwide has been thought through in sufficient detail. At one level, it is simply an alternative way of top-spicing the licence fee – diverting commercial revenues destined for the BBC to Channel 4, thereby leading to increases in the licence fee or cutbacks in services. But in addition, a BBC Worldwide not wholly owned by the BBC would be subject to different commercial and strategic imperatives, as a new shareholder would not have the same interests in promoting the BBC and furthering its corporate commercial interests.

As we have indicated above, we support proposals for the BBC to cross-promote PSB content on other channels, but see no reason why such an arrangement should be limited to Channel 4 when it could be applied to “at risk” programming on all PSB channels.

Tax Relief

We would be interested in exploring ideas for tax relief on certain programmes, as we have indicated already in respect of UK-produced children's programmes. But as we pointed out in our previous response¹⁶, assistance to producers is of little value if broadcasters are not committed to commissioning their programmes in the first place.

Accountability and Channel 4

Any direct public support for Channel 4 would require substantial changes to Channel 4's accountability arrangements, as Ofcom recognises. Not only would government need to be satisfied that public money was being spent on the public purposes for which it was intended – other commercially funded broadcasters would want to be reassured that the money was not being used to unfairly subsidise Channel 4's commercial activities.

¹⁵ The Television Multiplex Services (Reservation of Digital Capacity) Order 2008

¹⁶ Response of Channel 5 Broadcasting Ltd (Five) to *The Digital Opportunity*, page 18

Because we believe such issues are of crucial importance to the debate about Channel 4 and public funding generally, we commissioned Perspective Associates to provide advice on this issues. Their report is attached as an Annex to this submission.

Perspective believes that providing public money to Channel 4 would have implications not only for Channel 4 itself, but for the PSB system as a whole, for the BBC, for Channel 4's commercial competitors and for Ofcom. The report looks at the impact of such a policy on a range of issues, including:

- The continuing independence of Channel 4, including the role of its Board
- Channel 4's flexibility over its budget, commissioning and output
- The role of an external body in allocating public funds to Channel 4 and accounting for them
- Channel 4's public service remit
- The dangers of two publicly funded bodies duplicating each other
- Ensuring Channel 4 does not use public money to bolster its position in the advertising market
- How Ofcom's role in conducting Market Impact Assessments will change its relationship to Channel 4
- The incentives on other public service broadcasters to produce public service content without public funding
- The long-term sustainability of the licence fee

Section 7 and annex 1: Matters for short-term regulatory decision

1) Do you agree that our proposals for 'tier 2' quotas affecting ITV plc, stv, UTV, Channel TV, Channel 4, Five and Teletext are appropriate, in the light of our analysis of the growing pressure on funding and audiences' priorities? If not, how should we amend them, and what evidence can you provide to support your alternative?

Five is pleased Ofcom has listened to the representations we made about our origination quotas and has brought forward proposals for modest reductions in them.

We said in our previous response¹⁷ that Ofcom "should consider carefully all applications for regulatory relief that will enable the commercial broadcasters to deliver PSB more effectively". And we identified our main priority as "sustainable origination quotas, to allow us to invest in quality programming without having to make perverse commissioning or scheduling decisions, including allowing greater flexibility over origination in peak".

Five has made clear to Ofcom that, on the whole, our acquired programming is more profitable than our commissioned programming. Therefore, our business only functions successfully if our schedule contains a sufficient proportion of popular acquired programmes to help pay for the original programming, including our PSB contributions.

¹⁷ Response of Channel 5 Broadcasting Ltd (Five) to *The Digital Opportunity*, page 8

Our ambition is to develop a larger proportion of commercially successful originated programmes, which will obviate our reliance on acquired titles. But in the short and medium terms Five's business will still depend on acquisitions. Therefore, we are seeking a sustainable basis to our origination commitments, so that we do not need to divert attention and resources to meeting quotas that could be better spent on delivering both the public service and the more commercial programmes to which we are committed.

The proposed reductions in our quotas are modest. Reducing the peak time quota from 42% to 40% is the equivalent of just over half an hour a week, while reducing the all hours quota to 50% represents less than 45 minutes in a day. But we believe these changes would give us the flexibility to vary our schedule in light of changing economic and programming circumstances.

Five believes a substantial commitment to UK origination is the central part of any PSB role. But the minimum level of that commitment needs to be set at a realistic level in order for Five to be confident of delivering on it every year.

ITV and Channel 4 Regional Requirements

Five supports the relaxation of ITV's regional programming commitments proposed by Ofcom. However, we are not convinced of the merits of a radical decrease in ITV's regional production quota and the corresponding, albeit modest, increases in Channel 4's obligations. ITV has traditionally been a regional-based broadcaster and is also by far the largest commercial broadcaster: a reduction from 50% to 35% in its out-of-London quota is a massive reduction. And given that Ofcom accepts that production quotas represent an additional business cost, we are surprised that Channel 4 is to be saddled with such increased obligations ahead of any decision about its future funding.

Channel 5 Broadcasting Ltd

December 2008