

Submission to Ofcom's the Future of
Public Service Media

pact.

March 2021

Introduction

1. Pact is the UK trade association representing and promoting the commercial interests of independent feature film, television, digital, children's and animation media companies.
2. Pact is a strong supporter of the UK Public Service Broadcasting (PSB) system, which in the UK is a key intervention in the UK broadcasting ecology and plays a significant role for creatives, producers and audiences alike. It underpins a wider creative economy and plays a strong part in providing high quality UK content which is beneficial to audiences across the UK
3. The delicate balance of legislative and regulatory interventions has led to the creation of a broadcasting ecology here in the UK which is internationally recognised as one of the most dynamic, innovative, creative and diverse in the world. In 2019, UK independent television sector revenues were over £3 billion.¹ The PSBs still accounted for over 77% of the total UK commissioning spend. This growth has meant the UK independent television sector has transformed from a cottage industry in 2003 to one of the most successful in the world.²
4. The UK is the second largest exporter of TV content in the world (after the USA)³ and the biggest international exporter of programme formats (the templates for ideas which make a TV programme).
5. The 'Film, TV, video, radio and photography' sector had a GVA of £9 billion in 2001. In 2019, the 'Film, TV and Music' sector had a GVA of £21.7 billion.⁴
6. That said, these figures reflect a world before the COVID-19 pandemic had taken hold of the UK and given the current situation we expect a markedly different outlook in the coming years. Given the precarious outlook, Pact considers that any significant changes to the interventions that underpin the PSB ecosystem must be avoided.

¹ Pact Census 2020

² IBID

³ Mediametrie Television Year in the World report (2013)

⁴ DCMS Sectors Economic Estimates. The methodology was changed in 2014

Overview

- 1.1 Pact is a strong supporter of the public service broadcasting system. It delivers significant benefits to audiences, public service broadcasters, and independent producers in the UK.
- 1.2 As Ofcom identifies, satisfaction with PSBs remain relatively high with 73% of all audiences in 2019 being satisfied with PSB services.⁵ PSBs also continue to account for 77% of original UK commissions and therefore continue to hold buyer power within the UK domestic commissioning market.⁶
- 1.3 Pact considers that the current public service broadcasting compact – whereby the BBC, ITV (and the other Channel 3 licensees), Channel 4, S4C and Channel 5 (the PSBs) receive certain benefits, such as EPG prominence, and in the BBC's case a licence funding in return for obligations, such as the Terms of Trade and a requirement to commission more content from independent producers works well in practice. Furthermore, in a time of extreme uncertainty within the sector we argue that any fundamental changes to the structure will exacerbate further the precarious situation the sector is facing and damage any shoots of recovery.
- 1.4 Total independent production revenue has grown steadily over the years and in 2019 UK and international primary commissioning revenue stood at £3.3 billion and was growing year-on-year by 9.3 per cent.⁷ A large part of this success is down to the PSB compact which includes the flexibility of the legislation in Section 285 of the 2003 Communications Act. This has enabled independent producers to retain their Intellectual Property (IP) rights by introducing Codes of Practice which govern the way the PSBs do business with independent production companies. It has been a catalyst for the sector to use their asset value to grow their businesses.
- 1.5 Parliament's rationale for introducing this legislation was to address a market failure in the UK television industry. At the time when these were introduced, the four PSB channels (BBC, ITV1, Channel 4 and Five) controlled 92%⁸ of investment in new UK programmes. Consequently, they could demand all intellectual property rights to programmes shown on their channels. This led to a lack of efficient competition, limited exploitation of international and secondary IP rights for television content in the UK and an under-capitalised and dependent UK production sector.
- 1.6 As highlighted in Ofcom's consultation document, the PSBs continue to play a vital role in the success of the UK independent sector, accounting for the majority of production investment in the UK. In 2019 total PSB spend on new UK TV content was £2.8bn⁹ which is 77% of the investment in original UK programming each year.
- 1.7 For this reason, we strongly believe that the market failure due to buyer power which the legislation was introduced to address remains relevant.

⁵ Ofcom PSB Tracker. For 2014-2019 data, see Ofcom, 2020. Small Screen: Big Debate – a five-year review of Public Service Broadcasting (2014-18) interactive data report.

⁶ Pact Census, Oliver&Ohlbaum, 2020

⁷ Strengthening UK Culture and Creativity – impact of COVID-19, Oliver and Ohlbaum Associates Ltd, 2020

⁸ Ofcom's Second Public Service Broadcasting Review, Phase One: The Digital Opportunity, April 2008, page 56, states that the PSBs accounted for 92% of spending on network originations in 2004.

⁹ Ofcom analysis of broadcaster data. The main PSB channels invested £2.5bn in first-run UK originations in 2019. In addition, the BBC, ITV and STV spent £316m on first-run UK content in the nations and regions.

- 1.8 Ofcom has included, in the Future of PSM consultation document, the wider international market including SVoD commissions for the purpose of assessing the UK commissioning market. And Ofcom has assumed that increased international commissions are evidence of a change in the relationship between PSBs and the UK production sector. The wider international market does not change the UK market dynamics and the PSBs' hold on this. What it does signify, however, is how international co-production of programmes with the PSBs by SVODs and other non-UK broadcasters creates a symbiotic relationship, enabling original programme commissions, which the PSBs may not otherwise be able to wholly finance. PSBs can access the global TV sector to fund an increasing share of their schedule/content via producers.
- 1.9 Pact recognises that Ofcom has a duty to report on wider market developments and in the past commented on the need to keep the UK production sector under review. But before carrying out a call for evidence we expected an extensive analysis of the UK production sector and its market dynamics before deciding on whether a full review was necessary. Pact is disappointed that the focus on the UK production sector's international success is apparently being called into question and used as a basis for the Call for Evidence on PSBs and the UK production sector which we will also be responding to separately.
- 1.10 Any changes to the Indie quota and guidance to the Terms of Trade will have a chilling effect on the market and could reduce or freeze investment. Furthermore, this will impact the PSBs or PSM providers and audiences in the future. Through control of their IP rights and consequential investment in development, the market is offered a wide range of ideas (IP) from a large number of participants. Having many organisations pitching ideas to the commissioners makes for a very competitive marketplace and ensures that only the best IP is made available to the audience. Take these incentives away and much of the content that audiences enjoy would be depleted and PSB commissioners would have less choice. The large number of participants has been made possible by the low barriers to entry. Creative talents from either the larger companies or other sectors are able, under this system, to launch their own production companies. The dynamism of the independent production sector as a consequence of the large number of SMEs acts as a platform to find and develop new talent both off and on-screen to the benefit of the PSBs and UK audiences
- 1.11 Control of IP rights benefits all sizes of companies and across all genres . Again, removing the incentives would see a number of companies move their investment activities out of the UK and significant talent would move to global streamers, where they can see better income opportunities. One of the determining factors in attracting and engaging creative talent is the incentive for them to invest in and nurture their own ideas and businesses, with the potential earn-outs that enables in the long-term. If these incentives are removed or diminished this could accelerate lock in deals with the global streaming platforms to the detriment of the UK PSB system who would be unable to compete with the large sums offered.
- 1.12 Under this regulatory regime, which rewards innovation and creativity, independent producers are incentivised to invest in IP as any production or series of productions might prove to be a success and thus ensure a valuable ROI to the production company for a number of years. In addition, the need to sell the content's secondary rights both in the UK and internationally means that the producer must deliver content of the highest quality possible. The quality of this content then benefits both the commissioning broadcaster and the UK audience.

- 1.13 Pact supports Ofcom's analysis that PSB still matters to UK audiences and the wider broadcasting ecology but we would also like to highlight that it is the broader PSB system and its regulatory regime that has brought much of the success that we see today. Therefore if a new framework is to be created in the future the regulatory regime must replicate those interventions that allow for:
- High originations
 - Quotas and Terms of Trade for the independent production sector
 - Nations and Regions quotas
 - Low barriers to entry
- 1.14 Ensuring these are maintained in any new system is vital for the continued success of the independent sector and wider PSM ecology that Ofcom is trying to bolster and maintain into the future.

1. The Context for Ofcom's consultation

The Role of PSB within the wider media sector

- 2.1 Public service broadcasting in the UK is a hugely valuable public asset which delivers economic, social, cultural and citizen benefits to viewers.
- 2.2 The delicate balance of legislative and regulatory interventions has led to the creation of a broadcasting ecology in the UK which is internationally recognised as one of the most dynamic, innovative, creative and diverse in the world. The public service broadcasters are central to this.
- 2.3 The current PSB institutions – the BBC, Channel 4, ITV plc, STV group plc, UTV Media plc, S4C and Channel 5 – remain by far the biggest investors in original non-sport UK content, with the PSB channels¹⁰ accounting for 77% of UK revenues.
- 2.4 Given the important role which they play in this market, independent producers work closely with the PSBs in order to support them whenever possible in developing and retaining British audiences, thereby enabling them to continue investing in original content.
- 2.5 We agree that in recent years there have been increased opportunities from multichannel and international commissioners who have begun to commission more from UK producers. That said, Ofcom needs to be careful about what market they are intending to define and assess. Pact reminds Ofcom that under their General Duties they have powers '*to further the interest of consumers in 'relevant markets', where appropriate by encouraging competition.*' The definition of relevant markets remains '*markets for any of the services, facilities, apparatus or directories in relation to which OFCOM have functions.*'¹¹ Ofcom currently has no functions over international channels or platforms.
- 2.6 The increase in originated content being commissioned from UK producers by platforms and international channels has benefited audiences, PSBs and indies of all sizes.
- **Audiences:** have enjoyed higher quality content as platforms operating on scale are spending for global purposes. As a result, UK audiences get to

¹⁰ The PSB channels are: BBC One, BBC Two, BBC Four, BBC News, CBBC, CBeebies, BBC Parliament, BBC HD services, BBC Alba, ITV, STV, UTV, Channel 4, Five, S4C.

¹¹ [Communications Act 2003, general duties of Ofcom part 3 1 \(b\)](#)

benefit from any scale enterprises either as a subscriber or as a licence fee payer. Licence fee payers also benefit from these scale enterprises as often productions commissioned by PSBs rely on third party investment (which could involve platforms and international channels).

- **PSBs:** PSB spend has been boosted by third party investment which includes co-production agreements and deficit funding from independent producers both of which involve working with platforms or international channels either via secondary sales or through co-funding productions.
- **Independent producers:** through secondary sales and exploiting their own IP have been able to build businesses of scale and the system continues to allow growth. The ability to exploit IP allows producers to ensure they maintain profit margins which in turn builds their businesses. This allows all companies to benefit from the system. For example smaller indies tend to invest 4.5% of their revenues (which includes secondary exploitation revenues) into research and development.¹²

2.7 Although the impact of international platforms and channels have brought much needed finance into the sector this is far from the significant amounts of investment the PSBs bring. In our last Pact Census, we found that revenue from SVoDs and international channel commissioning amounted to just under £1bn versus PSBs commissioning revenue of £1.6bn. Independent producers in recent years have relied on international sales to help with margins and recoup their investment after deficit financing productions commissioned by PSBs. With this investment it has helped their R&D funding. We disagree with Ofcom that international platforms like Netflix are part of the domestic UK commissioning market.

2.8 SVoDs commission for a global audience. As identified above they commission at scale to cater to global audiences which UK audiences also benefit from. We commissioned Oliver & Ohlbaum(O&O) Associates to look at the impact of SVoDs within the UK commissioning market and they found that SVoD commissioners operate in a 'distinct market separate from commissioning of PSB original content and therefore do not impose a sufficient competitive constraint on the market power of PSBs when commissioning UK originated content.'¹³SVoD commissions are based on high-quality stand out premium content which aims to drive higher rates of subscription whilst PSBs cater to UK audiences with a range, breadth and depth of distinctive content. There are also differences in tone which O&O identified whereby PSB commissions are expected to be distinctive in representing UK culture, 'some PSB commissions may be successful in international markets, this comes in addition to the primary purpose of serving all UK audiences. SVODs generally take global rights precisely because the content is destined to serve both a local and a global audience, where 'rest of world' success is more important than the UK.'¹⁴

2.9 A final important point that O&O has identified is the fact that 'competition authorities generally delineate audio-visual markets on the basis of their funding as this is a major determinant of who are regarded as direct competitors, and the content produced and shown'.¹⁵ Because PSB programming is funded predominately by the licence fee and advertising revenues this makes it distinct from SVoD funding which is via subscriptions. Furthermore, SVODs operate in a wider ecosystem of multisided markets in competition with other online platforms such as Amazon and Apple all affected by

¹² Oliver & Ohlbaum, Call for Evidence PSBs and UK production sector, 2020

¹³ IBID

¹⁴ IBID

¹⁵ IBID

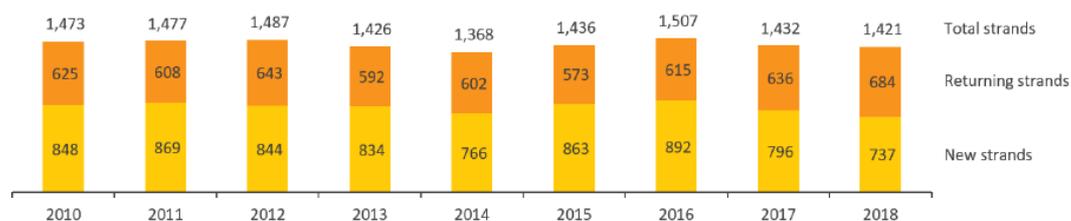
more complex competitive factors that have little to do with those relevant to the production of UK originated content.¹⁶

Why PSB still matters

2.10 Pact considers that the cultural and societal impacts of the PSBs on the whole are valued by the UK public. In a recent Ofcom survey it found that Public Service Broadcasting remains very highly valued by viewers, with three quarters of those who ever watch any PSB channel (BBC One, BBC Two, ITV, Channel 4 and Channel 5) reporting that they are satisfied with PSB broadcasting.¹⁷ This is particularly true when it comes to the provision of news, for example in the most recent Media Nations report by Ofcom it found that audiences find ‘news programmes which are trustworthy’ (73% of viewers gave it a 7-10 rating) and ‘helping me understand what is going on in the world’ (69%) continue to be the most important PSB purposes to the public.¹⁸

2.11 Economically the PSBs continue to be a significant part of the broadcasting ecology within the UK. The PSBs continue to play a vital role in the success of the UK independent sector. The UK market remains key to most indie production companies: 77% of UK revenues are reliant on the four main PSB network groups.¹⁹ PSB spent 2.5 billion in 2019 which is nine times more than the SVoDs’ £0.4 billion spend on UK originations in 2019.²⁰ The PSBs delivered over 32,000 hours of UK original content in 2018, compared to 221 hours of SVOD original productions made in the UK.²¹ In a O&O commissioned report it can also be seen that despite a ‘fall in commissioning spend, the five PSB networks still manage to commission over 1,500 titles a year between them (excluding one-offs), of which roughly 40 per cent are new titles (see **Figure 1**). This level of innovation – 600 new experiments per year – is unique to the UK PSB system and is the lifeblood of the UK content sector.’²²

Figure 1 Number of new and returning titles broadcast on the five main network PSB channels, 2010-2018



Source: Oliver & Ohlbaum programme database, Oliver & Ohlbaum analysis

2.12 The independent production sector has also contributed to the success of the UK PSB system through bringing in top-quality popular IP across every programme genre. In

¹⁶ IBID

¹⁷ Ofcom, Media Nations Report 2019

¹⁸ IBID

¹⁹ Pact Census Independent Production Sector Financial Census and Survey 2019, by Oliver and Ohlbaum Associates Limited

²⁰ Oliver & Ohlbaum, Call for Evidence PSBs and UK production sector, 2020

²¹ Oliver & Ohlbaum, Call for Evidence PSBs and UK production sector, 2020

²² Oliver & Ohlbaum: Strengthening UK Culture and Creativity in a globalising TV marketplace, 2020

both 2016 and 2018, the PSB channels allocated an average of 48% of spend across all genres of first-run UK-originated content to external commissions, which is approximately £1.2 billion and 52% to in-house commissioned productions, approximately £1.3 billion.²³ This has meant that it has considerably helped boost the creative sector's increasing importance to the UK's GDP is shown by the fact that the sector's rate of Gross Value Added (GVA) growth was twice that of the rest of the economy between 2010-17.²⁴ Socially and culturally the PSBs also do much to develop the UK domestic production through training and talent nurturing to become the world acclaimed sector it has now become.

Examples of PSB programming made by indies

Independent production companies produce a range of high-quality programming for the PSBs that helps them not only meet their PSB obligations, but also draw in big audiences.

First Dates produced by TwentyTwenty for Channel 4 remains of the channels most popular factual entertainment series. The programme is now in its thirteenth series and production has now moved to Manchester.

It's a Sin a drama mini-series for Channel 4 set in the 1980s and depicts the lives of a group of gay men and their friends during the HIV/AIDS crisis in the UK. The programme, produced by Red Production Company, was filmed in various locations across the North West of England and has so far amassed over 6 million viewers in the UK.

People Just Do Nothing a BAFTA and RTS award winning mockumentary series for the BBC and produced by Roughcut follows the lives of a group of friends who run a pirate radio station in West London.

Murder Case, a documentary series on BBC, follows Scottish police as they investigate some of the country's most complex crimes. The second series of the BAFTA and RTS Scotland winning programme was filmed across a number of years by Firecrest Films, a small but fast-growing indie based in Glasgow.

A&E After Dark is a documentary series which follows the A&E team on the nightshift in Hull. The programme was produced for Channel 5 by Crackit Productions, who have offices in Manchester and London.

Waffle the Wonderdog is a live action Children's series produced by Darrall Macqueen for CBeebies. Each episode is based around everyday issues that affect young children. The series is hugely popular and has been viewed on iPlayer 24 million times.

Keeping Faith/ Un Bore mercher, produced by small Welsh indie Vox Pictures for S4C, is a thriller series filmed in both Welsh and English across a variety of locations in Wales. The programme was not only extremely popular in Wales but was also a hit after airing on the BBC in England.

Only Connect a quiz show for the BBC produced by Parasol Media, a small indie based in Cardiff, has been dubbed Britain's hardest quiz show and remained a key part of the BBC's schedule since 2008.

- 2.13 Pact also notes that Digital Terrestrial Television (DTT) will continue to have an impact (as identified by Ofcom) over the next 10 years and 20 million UK households continue to use it.²⁵ Consequently, it has not got to the stage where linear PSB content has become obsolete. If PSB content continues to be found where it is expected by the audience, Pact considers that PSBs are no less disadvantaged than any other broadcaster or streaming service. High quality content continues to be the key factor in

²³ Ofcom Media Nations Report, 2019

²⁴ Creatives Industries, UK Creative Industries Value, November 2018, <http://www.thecreativeindustries.co.uk/resources/infographics>

²⁵ The Future of DTT, http://www.digitaluk.co.uk/about_digital_uk/the_future_of_dtt - Accessed 24/4/2019

driving people towards the TV channels. If the PSBs are creating engaging and relevant content, then they will continue to amass the viewing figures and reach that their channels already secure amongst the UK audience. In a recent Freeview survey it found that in times of crisis, free TV (without subscription or contract) is very/quite important for society – for 91% of the respondents surveyed across all age groups.²⁶ In June 2020, the PSBs' combined viewing share was 54.6%²⁷. In 2018, this share was 52% and in 2017 the PSBs' share was 51%.²⁸ In 2014, the combined share of the five main PSB channels accounted for over half (51.2%) of all viewing in 2014. From these Ofcom stats, the PSBs' share of viewing has remained largely stable. This shows that audience migration - although considerable with the younger age groups - may be less straight forward as a trend for all age groups.

Public service broadcasting underpins the UK's creative economy

2.14 Although the PSBs have brought a considerable level of stable investment over the years it is the wider PSB system which allows independent producers to exploit IP that has brought the key benefits. PACT questions Ofcom's analysis of the UK production sector's revenues. The current analysis of the UK broadcasters does not include the international revenues of broadcaster productions. A more accurate reflection of the market would be that the indie sector's domestic revenues (based on primary commissions) are close to £1.7bn which is only £500m more than UK broadcasters' domestic production revenues.²⁹ If we were to look at the broadcasters' total productions revenues which includes both international and domestic revenues, both ITV and BBC Studios would have revenues of around £3.1bn which is only £200m less than the independent production sector's revenues.

2.15 A significant omission from Ofcom's analysis within the main future PSM consultation document are the changes that have happened within broadcaster entities themselves and how they impact the UK commissioning market. Since 2017 BBC Studios has been created as a broadcaster-owned production arm of the BBC and subsequently in 2018 BBC Studios merged with BBC Worldwide, the distribution subsidiary and then in 2019, BBC Studios took full ownership of seven of ten UKTV channels. Ofcom will be well aware that these developments must be carefully handled as there are clear regulatory responsibilities for Ofcom to make sure that the relationship between BBC Public Service and the BBC's commercial arms do not distort the market or create an unfair competitive advantage.

2.16 The production arms of the BBC and ITV still capture a significantly larger share of the UK production market than any individual independent. In fact, as shown in **Figure 2**, ITV Studios' reported UK production income is around the same level as *the eight largest indies combined*, and BBC Studios is not far behind (despite it excluding the BBC's production activities relating to sport, children's, and news content – which remained in-house when the rest of production was spun out in 2016). Although this is likely to increase as the BBC has recently announced further changes within its BBC

²⁶ Freeview survey based on online survey with a nationally representative UK sample, involving more than 1,000 interviews. <https://www.freeview.co.uk/corporate/news/freeview-research-value-of-pbs-during-lockdown>

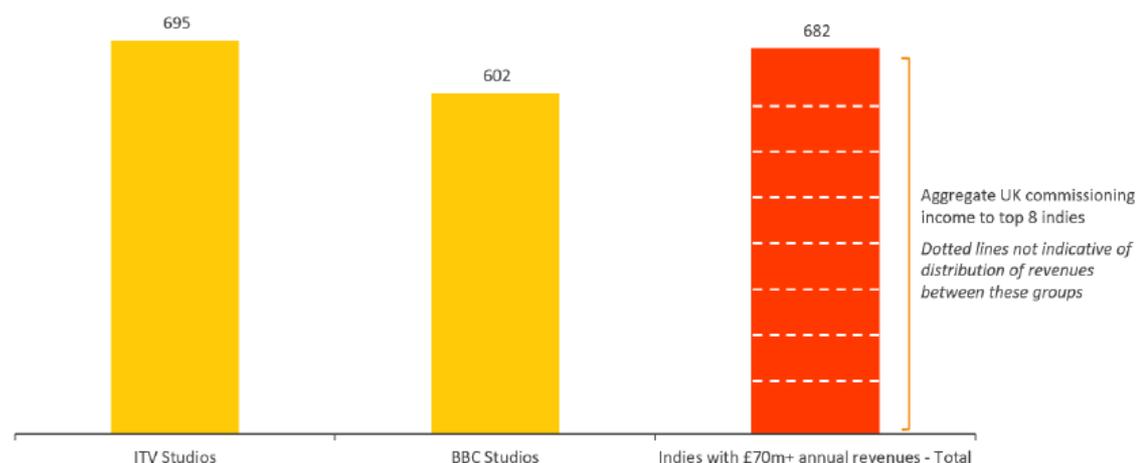
²⁷ Ofcom Media Nations 2020

²⁸ Ofcom Media Nations 2019

²⁹ PACT Census, O&O 2020

Studios structure as BBC Children's and BBC Three's in-house production teams will now become part of BBC Studios. This undoubtedly calls for a continuation in safeguards against vertical integration of PSBs impacting the market.

Figure 2: UK production revenues of BBC Studios, ITV Studios, and top 8 independent producers

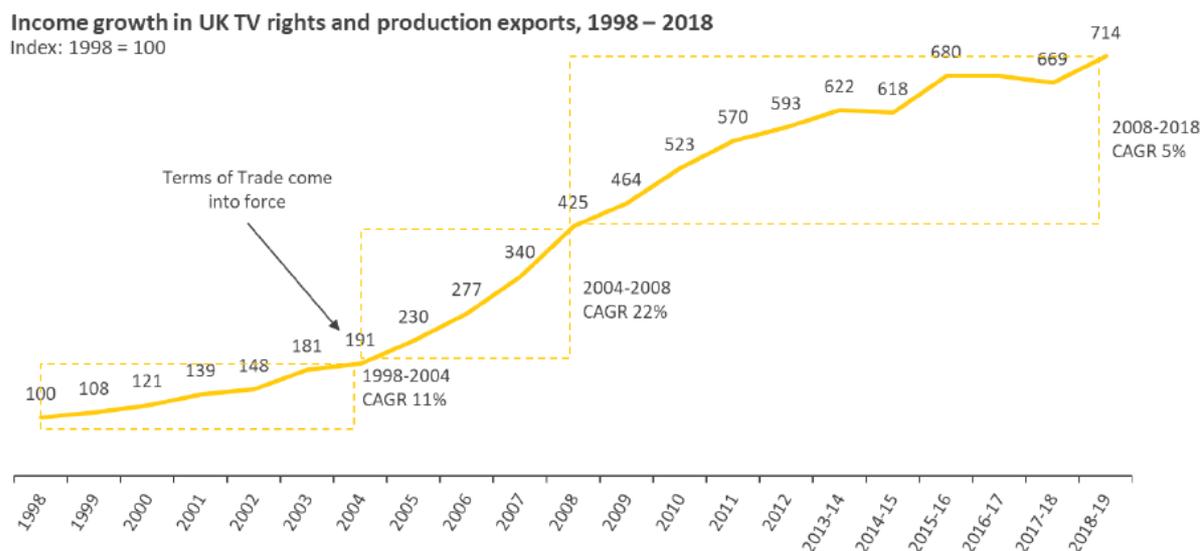


*Note: Excludes spending on news, as well as BBC spending on children's and sports production and inward investment
For this reason, totals here do not sum to the total shown in Figure 15*

Source: ITV Annual Report, BBC Studios Annual Report, PACT annual census, Oliver & Ohlbaum analysis

2.17 Ofcom must recognise the role independent producers have played as part of the PSB ecosystem to bring deficit financing to help cover the costs of programming. As found in O&O research commissioned by Pact, **Figure 3** below shows that since the introduction of Terms of Trade UK, independent producers have become asset-owning creative businesses rather than 'work-for-hire' service companies. This allows them to raise the funds necessary to participate in a liberalised global market for programme IP and formats and enables more producers to enter the indie market and ensures a thriving competitive production industry in the UK. The O&O research also found that with the control of rights now with the producers not the broadcasters, distributors – including the distribution operations of the BBC and ITV – had to offer competitive terms to producers to secure the mandate to sell the rights, and independent producers pushed the distributors hard to make the most of the catalogues they had been allocated. This in turn compelled the distributors to increase their sales efforts – to win mandates and make a return on the competitive terms they had to offer to obtain the mandates. We can see below that the seven to ten years immediately following the introduction of Terms of Trade there was a 22 per cent a year annual growth in ready-made programmes and format right sales to the rest of the world. Whereas if you look at the period just before this where broadcasters had full control of the rights the annual growth rate was half at 11 per cent.

Figure 3: Income growth in UK TV programme rights and production exports, 1998 to 2018



Note: The reported periods in the source data changed from calendar to financial years after 2012 – the growth rate between 2012 and 2013-14 is therefore based on the restated 2012-13 equivalent

A change in methodology in 2016-17 used by Pact led to anomalous data

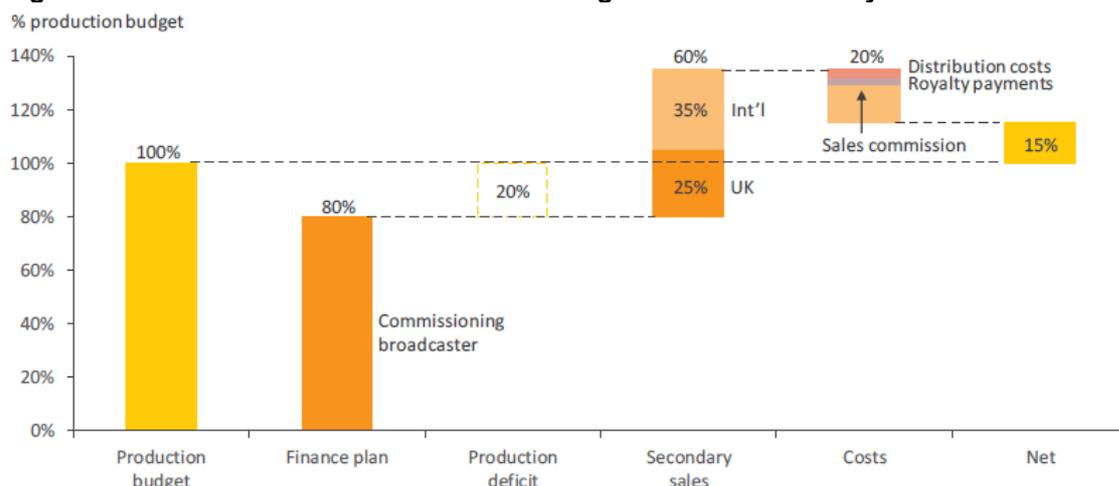
Source: BTDA, Pact, Oliver & Ohlbaum analysis

2.18 Through deficit financing independent producers have played an important role in protecting UK PSBs from the full impact of increased programming costs. They have invested their own profits into programme development and production. This was further shown most recently when Pact commissioned O&O in 2019 to carry out research on the impact of the iPlayer changes on the TV production market. In that report it showed the gap between the tariff provided by the UK commissioner (BBC) and the actual cost of the series. Excerpts from the market impact assessment are shown below.

2.19 Figure 4 reviews the financing model for scripted content and comedy. This shows the gap finance that producers need to make up via their international sales in order to make the production budget and that in turn impacts their profit margin. It underlines the importance of secondary rights sales to the independent production sector's ability to complete the necessary finance for their productions. Research by O&O for Pact found that the UK's five main UK PSB networks (BBC1, BBC2, ITV, Channel 4 and Channel 5) have faced increased competition for audiences over the last 20 years, resulting in broadly flat revenues, and reduced real terms spending on original UK commissioning (a 13 per cent reduction in real terms between 2000 and 2018).³⁰ Despite this audiences have benefited as UK PSBs have been able to commission more high-quality original UK content at a lower cost because indies have bridged the gap in finance. During this period, there has been no lessening of the quality of UK content evidenced by its ability to win prizes, both at home and overseas.

³⁰ Oliver & Ohlbaum: Strengthening UK Culture and Creativity in a globalising TV marketplace, 2020

Figure 4: Illustrative finance model for mid-range drama and comedy



Note: To protect commercially sensitive information, the programme titles used in the text are not necessary those provided to us by producers and may not be accurately represented by these finance model illustrations
 Source: O&O analysis and estimates

2.20 Without the guarantees to control and exploit their IP rights, as set out in the Terms of Trade, independent producers would not be able to continue to invest in the content which they create. Should this happen, UK commercial PSBs in particular would be much more vulnerable to cyclical changes in the TV advertising market than they currently are, with a lack of additional investment coming from UK independent producers. Pact is anecdotally aware of members having to cash flow whole productions and pay any costs linked to borrowing from banks when being commissioned by one of the commercial PSBs. Furthermore, this will have a critical impact on the very high-quality productions that Ofcom has identified as being most valuable to audiences. Ofcom noted in their PSB quantitative research in September 2020 that 32% of respondents included “high-quality productions” in their top three most personally valuable PSB benefits, and 21% included in their top three most societally valued benefits.³¹

Technology and global competition are driving the need for change

Audience Migration and wider market changes

2.21 We acknowledge that the world is changing from a consumer perspective. Audiences want to be able to access content whenever they like, wherever they are. But share of PSB viewership continues to be over 50% of all hours watched by all adults in the UK whilst SVoDs represent 12% of viewing based on the last Ofcom Media Nations Report. Although this has dropped again during the pandemic to 46% share of viewing for PSBs and an increase to 26% for SVoDs.³² However this is coming from a very high base for example 91% of the UK adult population still uses BBC services at least once a week.³³

2.22 Pact recognises the need for providing audiences with enhanced utility of content and this is one aspect of attracting and retaining audiences. The current PSB framework including the Terms of Trade, has shown to be flexible and adaptive enough to cater to these new preferences by agreeing to new Terms of Trade that will allow PSBs to utilise content in longer windows. That said, distribution is not the sole challenge to be

³¹ [Annex 6: Why public service broadcasting still matters \(smallscreenbigdebate.co.uk\)](#),p12

³² Media Nations 2020 Ofcom

³³ BBC Annual Report and Accounts, 2018/19

faced by PSBs. Pact considers that the issues that face PSBs are focused on editorial and content in a more competitive market for audiences - especially younger viewers - which has accelerated due to the COVID-19 crisis.

Terms of Trade are flexible enough to adapt to the market changes

2.23 PSBs are also benefiting from these changes. The Terms of Trade enable them to accommodate changes within the current rights or enables opportunities for further negotiation. Indies and broadcasters renegotiate Terms as required in order to gain longer windows and exclusivity online during the broadcast licence. Most recently new Terms of Trade have been concluded with the BBC which saw an increase in the initial window period to 12 months on all content it commissions with initial payment, and Channel 4 which now applies to all productions commissioned for both the main channel and the secondary channel E4 for the first time ever. Since 2004 the BBC and Channel 4 have negotiated the Terms of Trade six and five times respectively. The legislation is sufficiently flexible so as to allow these negotiations to take place as regularly as required. The industry has a proven track record of reaching regulated settlements without any regulatory intervention to enable the PSBs to meet their business strategies and consumer demands by launching new products and services

2.24 Indies have more incentives to ensure that their content meets consumer expectation of high-quality output being shown on as many platforms as possible. Indies are incentivised to generate as high a return as possible on their content, to generate revenues to invest back in content development and production. The majority of broadcasters are incentivised primarily to protect their core services, on which advertising revenues are based.

2.25 Competition is important and Pact welcomes the investment in content production by non-PSB channels and SvoD platforms as an important means of increasing the number and range of buyers in the TV content market, thus offering more opportunities for independent producers to pitch ideas and generate a benefit to audiences as a broader range of programmes make it on screen.

2.26 Pact recognises that technological change and global competition has driven a need to re-assess the current regulatory framework and in relation to prominence; PSBs or PSMs will likely need to ensure they have the tools to ensure the greatest accessibility for their services going into the future. But these changes do not merit looking at other elements of the regulatory regime that are proving so successful.

2. Proposals for a strong public media system

Question 1: Do you agree that a new regulatory framework for PSM delivery should support a more flexible 'service neutral' delivery approach that is more outcomes focused? p 39

Service neutral approach

3.1 Pact conditionally supports Ofcom's rationale for setting a service neutral delivery of public service media in addition to the extension of PSB to include digital offers and portfolio channels which Ofcom has already recommended to Government. For

commercial PSBs these could then be included more fully in their biannual deals with media agencies. This could have a positive effect on the ability of the commercial PSBs to generate revenues, which would be welcome. That said, Pact considers there are implications which would result from this which need to be carefully looked at:

- 3.2 If any public service media platform received a PSB benefit, they would also have to accept the PSB responsibilities – for example a higher indie quota than the 10% currently required for example on portfolio channels, Nations and Regions quotas and the application of the Terms of Trade.
- 3.3 What does that mean for content investment? Presuming that there is no additional money, this could risk a reduction on content budgets across the board, if spending is flat it may mean that tariffs and content budgets would be at a reduced level than they currently are. For example, currently portfolio channels and online only commissions operate at lower budgets and tariffs compared to the main PSB channels. Pact has a particular interest in how the new framework would impact the level of new commissions on any future services and channels and how this would work with the current market.
- 3.4 Ofcom must be careful about how it intends to set this new framework. Pact is concerned that any changes will damage the successful supply side of the market. It is important for Ofcom to consider – and publish evidence on – the full impact of allowing the PSBs greater flexibility in a new PSB compact on the UK production market and on the overall ecology for audiences and PSBs.
- 3.5 With limited resources available, our concern is that PSM providers might campaign for a 'levelling down' of the independent production quota, making the argument that it would be impossible for them to commission enough original UK content from independent producers so as to meet a 25% quota across the board.
- 3.6 Pact would strongly contest this claim, should it be made. The supply side of the production sector is thriving and has demonstrated time and again its capacity to make high-quality original content which meets the PSB values and helps the PSBs meet their obligations.
- 3.7 We seek assurances that the 25% independent production quota would be extended to include any additional services or channels which would seek to receive PSB benefits.
- 3.8 Furthermore, the extension of PSB/PSM status to any linear channel or digital service beyond the existing PSBs must also extend the scope of Section 285 of the Communications Act and that any future legislation would make the PSBs' services subject to the Terms of Trade.

Clear accountability framework

- 3.9 While we conditionally support Ofcom's rationale, a full impact assessment of the new framework is needed for Pact's full support for Ofcom's proposal for a more qualitative approach to PSM delivery. Pact seeks assurances that a qualitative approach to PSM delivery will not make it harder for independent producers to hold PSM providers to account and that ultimately the interventions that currently produce the success we have across the PSB ecology will not be lost – i.e. the 25% quota for qualifying independent producers and the Terms of Trade.

- 3.10 We want Ofcom to clearly outline how the new framework will intend to uphold the PSB purposes and objectives. How will this framework ensure there is the continued breadth and depth of original programming across a range of genres? As Ofcom's own five-year review of PSBs show the 'purposes and objectives of PSB have remained important to audiences. Viewers and listeners value programmes that inform our understanding of the world and that show different aspects of UK life and culture. The PSB channels are still distinctive in the amount and range of first-run, original UK programmes'.³⁴
- 3.11 We urge Ofcom to set out how exactly PSBs would set out their remits and to what extent this would come under public scrutiny and/or industry engagement. As Ofcom will understand Pact has found engagement with the BBC in recent years, which has followed an ex-post framework of regulation, less than transparent and would want to make sure that any new framework allows for industry engagement ahead of any remits being agreed.

Question 3: What do you think should be included in the PSM 'offer'? p 43

Question 4: What options do you think we should consider on the terms of PSM availability? p 43

- 4.1 Universality is a key principle which allows PSB programmes to be available to everyone, free at the point of use. Based on the current statistics on DTT usage it appears that a measured approach to changing the PSB model would be required. As noted in the Lords Communication Committee's report into the PSB system in 2019 - broadband is still not universal: 13 per cent of adults do not have it.³⁵ It also found that 'broadband is associated with a monthly subscription contract which undermines the notion of 'free TV'. It is also not as reliable or secure, and the internet TV industry is still developing.'³⁶ Ofcom has also noted in its support documents that 'around one in eight adults (13%) do not use the internet at home, a figure that has remained broadly constant since 2017 and which includes some 15% of working age adults in the lowest (DE) socio-economic groups'.³⁷
- 4.2 Pact has conditionally supported increasing the prominence of PSBs pending market impact analysis which continues to be lacking. If PSB benefits were to be extended to new services and new providers of PSM the current Terms of Trade and associated quotas will need to be extended. If, as Ofcom outlines, a net zero fee principle impacts content investment, Pact considers that this will have an implication on whether we support the new PSM offer and framework.

Question 5: what are the options for future funding of PSM and are there lessons we can learn from other countries' approaches?

- 5.1 The current mixed model for PSB funding works well in practice. The combination of licence fee (BBC) and commercially funded PSBs (ITV, Channel 4, Channel 5) helps to

³⁴ [Small Screen: Big Debate – a five-year review of Public Service Broadcasting \(2014-18\) \(ofcom.org.uk\)](#), p5

³⁵ Lords Communications Committee Report PSB: Vital as Ever, 2019

³⁶ IBID

³⁷ [Online Nation – 2020 report \(ofcom.org.uk\)](#)

ensure that UK audiences get not only value for money, but also a diverse range of high-quality content. While dips in revenue streams such as advertising are inevitable, this is why many PSBs now have multiple revenue streams. For example, ITV expanded into production with ITV Studios, and in 2019 revenues were £758m.³⁸ The BBC's commercial subsidiaries delivered dividends of £189m in 2019/20.³⁹ These commercial investments work well for the PSBs and allow them to invest more in their owned and controlled businesses and content.

- 5.2 Ofcom should be wary of completely changing the current model, particularly whilst the sector is in the midst of recovery from the ongoing COVID-19 pandemic. There may be some lessons to learn from other countries' funding of PSBs, however it seems that Ofcom fails to take into account how successful the UK PSB system, and wider sector actually is. In June 2020, the PSBs' combined viewing share was 54.6%⁴⁰. This share of viewing has remained relatively stable over the years. In 2014, the combined share of the five main PSB channels accounted for over half 51.2% of all viewing. If we compare this to Ireland, whose PSBs share is around 26.6%⁴¹, our sector is much larger, has a greater share of viewing and is also internationally renowned.
- 5.3 Given the success of the UK sector, the UK is highly attractive for inward investment. In 2019, inward investment across film and high television topped £3 billion for the first time.⁴² Radically overhauling the PSB system also risks disincentivising inward investment which benefits the whole sector, including PSBs. Inward investment into the UK ultimately leads to an increase in studio facilities, jobs and inward investment in the form of co-productions means the PSBs can commission high quality content with financial backing from the SVoDs or international channels. A decrease in inward investment would also damage the UK production sector, who are key contributors to the UK economy, wider creative economy and a strong source of job growth. In 2018, the creative industries contributed £111.7bn to the UK economy, an increase of over 40% since 2010.⁴³

Third-Party funding

- 5.4 Third party funding is increasingly being used to finance PSB programmes, which the PSBs may not usually be able to afford alone. Third party funding could include: deficit financing (secondary sales both UK and International and merchandise), co-production financing, and tax reliefs. For example, *His Dark Materials*, a BBC and HBO co-production, which drew in a substantial UK audience⁴⁴ and has also been an international success. *The End of the F***ing World*, a Channel 4 and Netflix co-production, remains the best performing original All 4 exclusive ever⁴⁵ as well as being

³⁸ <https://www.itvplc.com/investors/results-centre>

³⁹ BBC Annual Report 2019/20

⁴⁰ Ofcom Media Nations 2020

⁴¹ RTÉ Annual Report 2019.

⁴² BFI stats 2019, <https://www2.bfi.org.uk/news-opinion/news-bfi/announcements/bfi-statistics-2019>

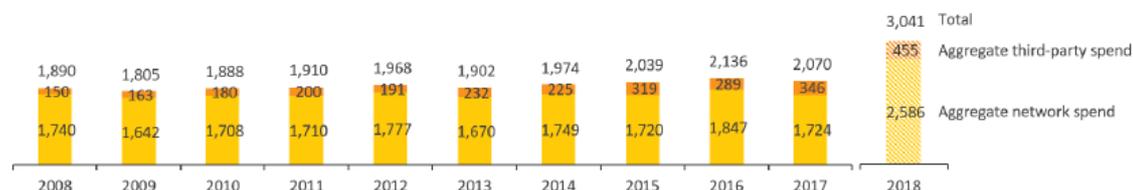
⁴³ DCMS Sectors Economic Estimates 2018: GVA, Department for Digital, Culture, Media and Sport, February 2020

⁴⁴ The first episode of the second series was watched by an average 4.4 million viewers according to press reports. See here: <https://www.bbc.co.uk/news/entertainment-arts-54871354>

⁴⁵ <https://www.channel4.com/press/news/end-fing-world-fking-back-channel-4-november>

nominated for a variety of awards. It is highly unlikely that Channel 4 or the BBC would have been able to finance these productions without third party financing.

Figure 5: PSB third party spend, 2008-2018 (£millions, nominal terms)



Note: ITV spend is not included pre-2018
Source: Ofcom Media Nations, Oliver & Ohlbaum analysis

- 5.5 Indies play a role in bridging the gap in finance needed for productions. By providing finance and taking on a greater share of the risk from broadcasters it reduces the cost of the primary licences to UK broadcasters. Industry estimates suggest that today only 55 per cent of BBC commissions are fully funded, with the remaining 45 per cent depending on co-production or deficit finance. This willingness of independent producers to take more of the financial burden is not restricted to the large indies. Analysis of smaller indies in the UK suggests that on average they, as we have already identified, spend 4.5 per cent of their revenue on R&D, and only earn margins on UK production activity of around 2 per cent.⁴⁶ Furthermore, the BBC itself enters into co-productions for many of their wholly owned shows.
- 5.6 The increased share of viewing and the contribution of the system towards a vibrant and diverse sector usually associated with third party funding compensates for any loss of rights in the secondary windows and markets. Ofcom agrees with this point regarding viewing and state that ‘popular programmes help audiences to value the PSB sector and feel invested in its continuity’.⁴⁷ For the commercial broadcasters, popular programmes can also cross-subsidise other programmes. Channel 4 states that they ‘do this through a cross-funding model that funds genres such as News, Current Affairs, British Film and Education (which are typically loss-making), with revenues from commercially valuable programming’.⁴⁸ The UK PSBs are able to commission a wider range of high-quality content that both domestic and international audiences love because of co-production partners and deficit financing. In research we commissioned O&O to carry out they found that SMEs made up a sizeable share of first-run originated hours on the PSB channels for Arts & Classical, Children’s, Comedy and Drama, i.e. genres with both greater and lesser demand in the market as a whole.⁴⁹

Figure 6: Share of 1st run originated hourstaken by Qis and NQIs producers split by producer revenue band (to include SMEs)

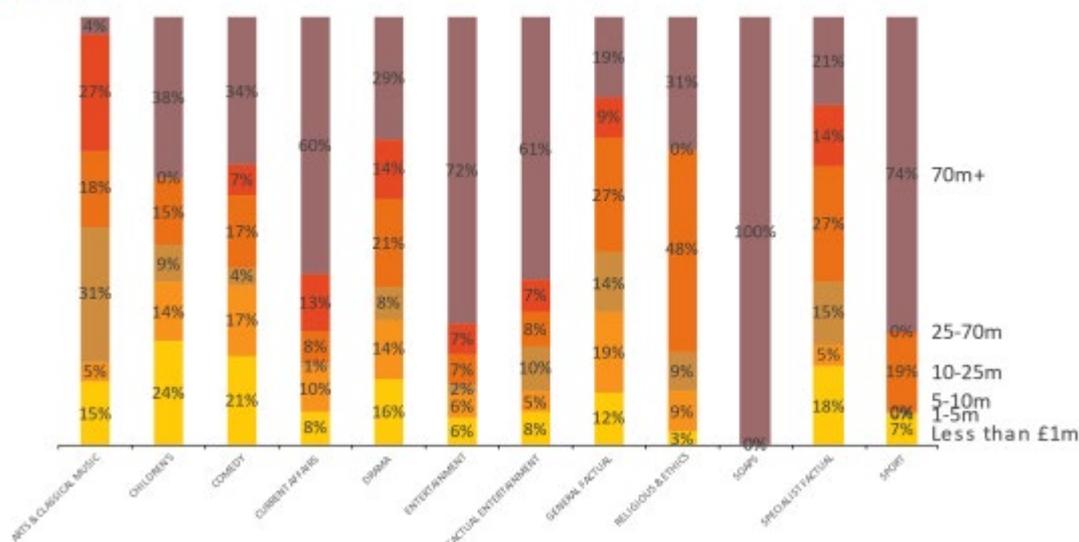
⁴⁶ Oliver & Ohlbaum, Call for Evidence PSBs and UK production sector, 2020

⁴⁷ Annex 6: why public service broadcasting still matters, Ofcom, December 2020, p11

⁴⁸ <https://www.channel4.com/corporate/about-4/who-we-are/our-model>

⁴⁹ Oliver & Ohlbaum, Call for Evidence PSBs and UK production sector, 2020

SME producers are responsible for a greater number of first run originated hours made by QIs and NQIs across the majority of genres— larger budget genres such as entertainment and sport are however mostly made up by larger producers



Source: Oliver & Ohlbaum analysis

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5.7 Fewer programmes made with co-producers and deficit finance, or a complete stop, would likely lead to a less vibrant and dynamic market and some genres, particularly high-end natural history which is incredibly popular, may be lost from the PSBs' schedule entirely.

Contestable Funding

5.8 Contestable funding is used in other countries and has been suggested in the past as a potential funding model for PSB content, particularly for underserved genres that may be less commercially viable than others. However, using contestable funding can be inefficient and Pact would not support a contestable funding model being used as a replacement for the current system or to fund multiple PSB genres. For example, there are substantial administrative costs associated with running a contestable fund and this funding would be better spent on investing in PSB content rather than running an administrative body. Contestable funding is inefficient in a number of ways:

- **Associated costs:** Any form of contestable fund incurs significant transaction costs associated with the establishment and running of an administrative body. This money would be better spent on additional content investment rather.
- **Risk of 'deadweight':** there is also a risk that commissioners would use the fund to invest in ideas that they would have done regardless. This could mean that content investment would actually diminish as the fund would create a reliance on Government funding and take money away from actual spend on content. This would be difficult to prevent and an independent body administering the fund would likely be unable to establish whether the investments were truly additional or substitutional. This problem is apparent in the animation and children's tax credits, neither of which have stimulated a significant demand for children's programming from the broadcasters.
- **Safe programming:** a contestable fund could also lead to the commissioning of safer programming and diminish risk taking by the broadcasters. Spreading public funding to others who have a mix of commercial and non-commercial goals would introduce conflicting incentives which could pull the focus of the fund towards safe

programming in order to secure funds. Evidence of this can be seen in New Zealand's contestable fund. Producers needed to obtain approval by an administrative body to secure funding and as a result they produced safe formulaic content to ensure they were approved quickly.⁵⁰

- 5.9 There are certain genres which may benefit from contestable funding, such as Children's content. Although Pact only conditionally supported development of the Young Audiences Content Fund if Ofcom were given powers to compel broadcasters to invest in children's content. The PSBs' investment in children's content has been in constant decline for over a decade. In 2002, the PSBs spent a combined £163m on first-run hours of children's content, and £63m of this came from the commercial PSBs⁵¹. By 2019, this spend had declined to £78.9m.⁵² This substantial decline has meant the UK market for children's producers has rapidly shrunk and is struggling due to the lack of investment, however consumer demand for quality children's content remains the same as ever before. Pact has long argued against this decline in investment however, given the strict rules around advertising of children's content and HFSS advertising, it is no surprise that the commercial PSBs argue that it's no longer financially viable. Pact was pleased with the announcement of the Young Audiences Content Fund and welcomed the additional £57m investment into the children's content sector. To date the scheme seems to have been a success, especially in terms of providing development funding but it's too soon to tell whether the fund has increased the provision of children's content. Contestable funding should not be used as a replacement for broadcaster investment in first run UK originations and is unlikely to make up for the fall in investment by the PSBs, particularly in the case of children's content.

Question 6: What do you think about the opportunities for collaboration we have referred to? Are there other opportunities or barriers we haven't identified? p 54

- 6.1 Pact supports additional data and pooling of knowledge that would help the broadcasters improve their VOD platforms, user recommendations and help to understand their audiences better. However, Ofcom must understand that often this data is commercially sensitive for suppliers and if this issue is further developed as a policy a full impact assessment will need to be carried out.
- 6.2 Pact members benefit from a healthy PSB system and the content investment the PSBs provide. It's important that a healthy system is maintained and continued into the future.
- 6.3 Pact acknowledges that prominence is important to the PSBs and has conditionally supported the policy pending market impact analysis. However, Ofcom fails to take into consideration that for many platforms, such as Amazon Firestick, the PSBs BVODs are usually the first apps to appear and are the most popular.
- 6.4 Pact consider that there is not enough evidence within Ofcom's consultation to understand whether an increase in collaboration for example between the PSBs and others such as Facebook or theatre organisations like the Royal Shakespeare Company will have a positive impact on the market. Ofcom need to be aware that

⁵⁰ Frontier Economics report on Contestable licence fee funding for Pact, 2017, p29

⁵¹ Children's analysis (PSB Annual Report), Ofcom, December 2014

⁵² Ofcom Media Nations Interactive Data 2020

substantial changes to the market via PSB collaboration can have an impact on competition. Any changes which risk distorting the market need to be subject to consultation and substantial research, including an impact assessment.

- 6.5 Ofcom state that 'strategic relationships could help ensure that PSM reaches all audiences, is easily discoverable and could support the delivery of PSM in the global market.' However, it's not clear why PSM needs to be delivered globally. In fact, Ofcom does not state why it needs to be delivered globally. In addition, if the new framework is set up for the end goal of satisfying a global audience, the original purpose of PSM in the UK is being lost. PSM values are centred around the UK market, not a global market. It's important to understand that the international commissioning market and the international distribution market are two very different things.
- 6.6 The PSBs do not need to try and serve international audiences through a global distribution platform because indies are selling programmes internationally and through presale agreements bringing in additional finance to the system to help pay for high-quality programming to satisfy UK audiences. As Ofcom recognises BBC Studios and ITV Studios also benefit from this system of harnessing the global markets. As we outlined above last year both entities brought in over £3 bn in revenues once you include international revenues. There is nothing stopping BBC Studios and ITV Studios to continue bringing in investment and revenues through its commercial arms on an international stage and likewise indies will continue to help deficit financing programmes by exploiting their own IP in international markets. Indies invest the money they raise through international revenues to develop ideas to bring to the UK market, which benefits the PSBs at no additional cost.

Question 7: What are your views on the opportunities for new providers of PSM? p 60

- 7.1 Pact does not have a particular view on the new providers of PSM being suggested. However, we are concerned that if there were to be new providers of PSM, they would not have the reciprocal PSB obligations. In order to get the advantages of being a PSB, such as prominence, you must also have the obligations, the Terms of Trade, indie quota, commitment to nations and regions and diversity etc. Supporting the domestic production sector is seen as a key role for PSBs across the world⁵³ and maintaining the Terms of Trade, nations and regions and indie quotas in the UK are one of the key ways to support the sector. Supporting domestic production through these interventions also benefits the PSBs and could potentially benefit any new providers of PSM. These interventions are the key component of independent producers' business models and allow them to grow sustainable businesses of scale. As producers scale up their businesses they often invest in the training and recruitment of new and existing employees. Not only do these employees often go on to work for broadcasters bringing these skills and expertise with them, but ensuring the sector has a suitable supply of highly skilled workers to meet demand is vital for the production of high quality content.
- 7.2 Ofcom's rationale for intervention is because audiences, particularly young people, are turning away from the PSBs. Ofcom claims there is a risk that younger audiences will not engage with the PSBs as they value different services and types of content.

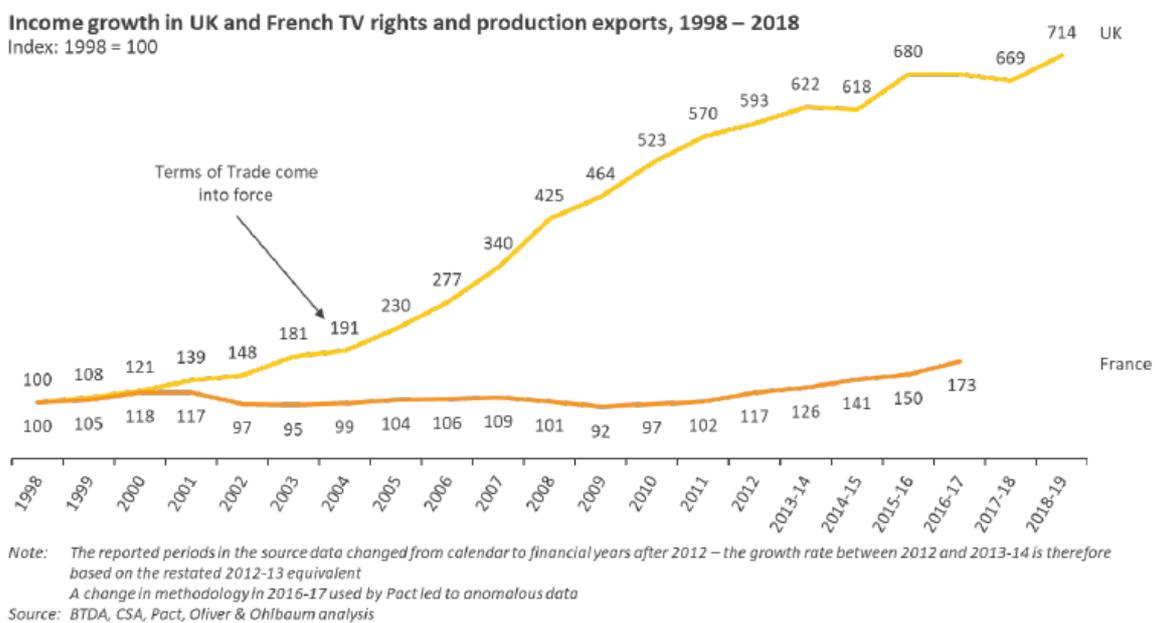
⁵³ International Perspectives on Public Service Broadcasting, EY Report for Ofcom, October 2020

However, the PSBs still remain hugely popular with UK audiences. On average audiences watched broadcast TV services for 67% of the 4 hours and 50 minutes spent consuming video in 2019.⁵⁴ While young audiences do spend less time watching broadcast TV services than the average, they still watch around 1 hour 20 minutes per day, which is above the 1 hour spent watching SVOD⁵⁵. Ofcom are also neglecting the editorial issues at play here, PSBs' main challenges lie in ensuring there is a strong content offer and editorial process to attract young audiences. Distribution issues or how content is funded have little to do with meeting this challenge.

7.3 The SVoDs are already investing in the UK and commissioning more content. This is because the UK production sector is internationally renowned for high quality content that viewers love, but also more importantly because of the environment that already exists in the UK. The current system is carefully balanced and allows indies to exploit their IP and use the revenues to invest in research and development of ideas, which appeal to both SVoDs and UK broadcasters.

7.4 Ofcom uses Canada and France as examples of how Governments are encouraging the provision of new content and securing PSM delivery. In Canada, there is a levy scheme to fund domestic production and France uses a provision in the Audio-Visual Media Services Directive to impose a levy on the SVoDs to fund local production. However, this is not something the UK should be seeking to emulate.

Figure 7: Income Growth in UK and French TV programme rights and production exports 1998-2018



7.5 Both France, whose audiovisual sector is 50% smaller than the UK's,⁵⁶ and Canada's production sector, whose volume of TV production is worth around \$2.73 billion (around

⁵⁴ Public Service Broadcasters and the UK Production Sector O&O Report for Pact, March 2021

⁵⁵ IBID

⁵⁶ The contribution of the UK-based film, TV and TV-related industries to the UK economy, and growth prospects to 2025, O&O, September 2018

£1.5bn)⁵⁷, are less successful in comparison to the UK. Levies on SVoDs can actually have the opposite effect and lead to a reduction in investment.

⁵⁷ Profile 18: economic report on the screen based media production industry in Canada, Prepared for the Canadian Media Producers Association, Department of Canadian Heritage, Telefilm Canada, Association québécoise de la production médiatique, March 2019