

GUARDIAN MEDIA GROUP

Response to Ofcom Consultation: PSB Review Phase 2 – The Digital Opportunity

Thursday December 4th 2008

Overview

GMG welcomes the opportunity to engage with Ofcom on the future of public service broadcasting through the second phase of the PSB Review.

Our responses to Ofcom's individual questions are informed by a number of core principles:

- Plurality of public service broadcasting, the fixed point of the BBC at its centre, remains of great value to UK citizens and consumers.
- Government and regulators must ensure that markets are organised to deliver sufficient financial incentives for commercial providers to invest in high-quality public service content.
- Only where such incentives cannot be created through the market should regulators use further public money to support the provision of public service content.
- The distribution of public funds is by its nature bureaucratic and needs to be subject to a very clear governance regime – the BBC Trust in its current form does not provide the blueprint for governing other PSB operators such as Channel 4.

Section 4: Models

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

We share the view that plurality is essential in a democratic society, as it delivers diversity of voice and enhanced reach, and ensures competition, quality and innovation. Whereas plurality of voice is commercially delivered in most media sectors (such as newsprint and online) the entry costs of television, caused by scarcity of broadcast spectrum, imply that fewer commercially viable public service voices can exist. As such, a range of funding mechanisms is required to ensure continued diversity of voice in some commercially non-viable public service broadcast genres.

We note Ofcom's Analysis 1 suggesting that the public share this view, with over 70% of respondents believing plurality is important in genres of particular relevance to our submission, which include News, Current Affairs, National / Regional News, Current Affairs About My Nation / Region.

There are currently decreasing returns associated with the provision of high-quality content in these genres, partly as a result of the current economic recession which has undermined advertising-based revenue models, and partly due to the long-term structural changes of digital transition and globalisation. Many argue that this will inevitably lead to market failures in the provision of such content not only in traditional broadcast media, but also increasingly in digital media.

We do not believe that such market failure is inevitable. Regulators and government can take actions, short of direct public subsidy, to ensure the correct commercial incentives are in place to sustain high-quality content across digital platforms.

¹ Figure 10, PSB Review Phase 1

Such actions could include:

- Reconsideration of the rules governing media ownership to allow consolidation where this would increase rather than decrease plurality of public service content provision
- Recognition by competition authorities that consolidation within local media markets is, in most cases, no longer a threat to competition, but rather is necessary to ensure continued choice for readers and advertisers
- Public support to build out digital infrastructure, both in building out a universal broadband infrastructure and in supporting broadcast TV and DAB radio infrastructure
- A clearer definition of the boundaries within which the BBC, BBC Worldwide and other public service broadcasters will operate
- A more meaningful offer of partnership from the BBC (detailed, explicit, transparent) and use of BBC assets to support commercial operations

The fundamental long-term challenge for industry players and regulators is how to ensure that those companies investing in the creation of high-quality content are commercially rewarded for doing so. Currently, the lion's share of online revenue associated with the creation of such content is captured by powerful search providers and advertising networks (accounting between them for approximately 60% of total UK online ad revenue), who do not reinvest their proceeds in high-quality UK content. Whilst not a core consideration for this review, addressing this issue will have longer-term and more sustainable benefits than simply injecting further public money into the online ecosystem.

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

We favour Model 2 – a refined BBC/Channel 4 model – for Public Service Broadcasting.

For the majority of genres, such as comedy and factual, where broadcast market failure could exist and plurality is required, we believe that Channel 4 is the right agency to deliver a broadcast remedy, driven by its public ownership, its history of delivering high-quality, innovative programming and its desire to remain at the heart of public service broadcasting in the UK.

As Ofcom notes, there may be some genres, such as Regional News and Non-News broadcasting, where Channel 4 is less well placed, and that may be better served by a different organisation through a contestable funding model. Where the citizen and consumer requirements can be tightly defined, such as the provision of local and regional news on predefined platforms for specific geographic areas, commissioning a third party to supply content could be practicable. Where needs are more difficult to prescribe and where creative risk-taking is desirable, such as in the case of challenging drama or comedy, we believe that money is best channelled through existing PSB players, and the BBC and Channel 4 in particular.

Regarding the alternative refined models proposed:

- **Model 1** – an enhanced Evolution model – is an improvement on the Evolution model presented last time. It is not, however, possible for us to assess whether the changes here are sufficient to solve the long-term funding issues raised by the commercial PSBs. This proposal also includes the extension of Channel 4's remit to "innovate and provide distinctive public service content across platforms". While we believe that Channel 4 is well placed to provide remedies in broadcast in some genres, it is not de facto best placed to deliver public service content online.
- **Model 3** – a refined competitive funding model would require a new public body to be created to allocate all funding. There is a danger that this organisation could break the crucial relationship between the audiences and the creative organisation delivering the content.

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?

We very much support the role of Channel 4 in public service broadcasting and acknowledge that changes to its funding will be required for Channel 4 to continue to broadcast a similar quality and breadth of public service content. However, we see substantial investment by Channel 4 online as unnecessary and we believe it potentially risks doing more harm than good to the UK media landscape.

The receipt of public funding clearly carries with it significant responsibility and must be accompanied by appropriate obligations. This implies that a sufficiently robust governance framework would need to be designed for Channel 4 and any other recipients of direct public funding. It should not be assumed that the BBC and its governance by the BBC Trust represents a suitable model for Channel 4. As we have outlined in our responses to the BBC Local inquiry, and to the House of Commons Select Committee, we have serious concerns about the ability of the BBC Trust to act as an effective regulator of the BBC's activities. Although the Trust last month acted to stop the BBC Executive's plans to spend £68m on local online video – a move that would have undoubtedly crowded out private sector investment in local content – we retain fundamental concerns regarding the Trust's ability to act as both supporter and regulator of the BBC. In our view, these roles will always be in potential conflict. Strategy should be set by the Executive, regulation should be conducted by a separate body.

We strongly challenge the notion that Channel 4 is the default best agency to either allocate new funds or to spend funding to deliver public services objectives online. The solution to Channel 4's broadcast funding problems should not be in the form of cash funding for an increased online presence. Whilst many of the proposals in Channel 4's 'Next on 4' document are eye-catching, including its plans to invest over the next two years up to £50 million in digital content and services through its 4IP programme, the organisation's track record of online transition to date has been patchy, particularly when compared with the achievements of the BBC and online newspaper sites. The reach of channel4.com, for instance, is significantly lower than that of guardian.co.uk. The only Channel4.com property to deliver significant audiences, albeit for only 2-3 months per year, is in entertainment, with its Big Brother website.

In summary, Channel 4 has an important role to play in public service *broadcasting*, providing pluralism and a distinctive voice; however, we believe that this important but advantaged role should remain restricted to broadcasting. We believe that the remedy should always match the cause; seeking to address Channel 4's *broadcasting* funding gap through diverting public funding to Channel 4 for online investment fails to address the root causes of its broadcasting challenges.

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?

We think it is right to question the public service obligations of ITV1, Five and Teletext after 2014. The level of financial challenge that ITV will experience by that point, and probably beforehand, requires more than incremental change. The importance of plurality in regional content that Ofcom has identified suggests that at least one non-BBC source of local news is required. However, since ITV is a commercial operation with a requirement to deliver returns to shareholders and has stated that it is not able to make regional news and content commercially viable, it may not be best placed to provide this service. This needs to be carefully considered since it may result in a systemic under-delivery of content demanded by citizens and consumers (e.g. regional broadcast content).

However, if *alternative* providers could be supported in delivering Regional / Local public service objectives, the loss to society of ITV's proposed changes would be mitigated, allowing ITV more freedom to pursue its objectives and meet the needs of its shareholders.

Five currently receives a financial benefit from its PSB status. Given our support of Model 2, we find it hard to understand why Five should retain its privileged position. Given the strengths of online in delivering information and search results (one PSB genre) we agree with Ofcom's questioning of the continued need for intervention to ensure the existence of Teletext.

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?

As we mentioned in our response to question 2 of section 4, where the citizen and consumer requirements can be tightly defined, such as the provision of local and regional news on predefined platforms for specific geographic areas, commissioning a third party to supply content could be practicable. Where needs are more difficult to prescribe, such as in the case of drama or children's programming, we believe that money is best channelled through existing PSB players, and the BBC and Channel 4 in particular.

Direct funding of public service content would require a new public body to be created to allocate funding. As Ofcom's Phase 2 Review document notes, several stakeholders have already raised concerns that the creation of a new body could "chill" creativity. We have similar concerns.

Ofcom's description of how competitive funding could operate clearly requires further detailed thought. The nations, regions and local news tender used as an example by Ofcom in Figure 29 of the consultation could be appealing if the regulator was truly convinced that market failure existed. One thing that is not made clear by this example is how the considerations of commercial players who did not want to bid for public money would be taken into account given the increased competition from a brand-new, publicly-funded entity.

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?

We agree with Ofcom's findings that news from the nations and regions continues to play an important role. However, we believe that the future provision of Regional News and Non-News PSB content in the UK is a cause for serious concern. Ofcom's research shows that, overall, the importance to consumers of regional content has been increasing since 2004². The regional problem is most acute for Regional and Local News (as distinct from Non-News).

Firstly, there is systematic under-provision of local PSB content demanded by citizens and consumers – Regional / Local News is the joint third most important genre of PSB content (78% of respondents believing it to be important) but only 53% of respondents are satisfied with present provision³.

Secondly, plurality of voice is also crucial to the consumer – 76% of respondents believe plurality is important (the third highest score of all genres), implying competition to the BBC is essential for Regional / Local News.

These issues (a mismatch between demand and satisfaction and the necessity for plurality) are also present, albeit to a lesser degree, in the Regional and Local Non-News genre.

Against this backdrop of continuing importance of Regional / Local content, dissatisfaction with present provision, the ongoing need for plurality, and ITV's desire to step back from its regional obligations, we see a substantial risk of market failure in the present and future broadcast of Regional / Local PSB content.

We are significantly less concerned about market failure in online local content, where there is a substantial commercial presence (albeit one in the early stages of growth) serving local audiences with high-quality content. This sentiment was illustrated by the BBC Trust last month when it stopped plans by the BBC to expand into online local video, potentially dissuading further investment by commercial publishers. There is an argument that there is a potential threat of future market failure, one solution to which could be contestable funding to stimulate investment in online content. We would be keen to participate in this ongoing debate, but believe that a straightforward and more immediate remedy to some of the issues faced by local and regional commercial publishers would be to address the artificial regulatory barriers that are currently preventing the industry from consolidating further.

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

We will leave it for those closest to these matters to debate this issue more thoroughly.

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

We welcome Ofcom's decision to make available geographic-specific lots of interleaved spectrum around major urban towns and cities. We have illustrated, through our Channel M local television service in Manchester, how public service content can be delivered through local TV services. These services have the potential to help compensate for any decrease in public service provision by ITV in such urban areas.

² Ofcom PSB Review Phase 1, paragraph 3.41

³ Ofcom PSB Review Phase 1, figure 20

We agree with Ofcom's assessment that the economics of local TV are fragile and that sustainable broadcast models are unlikely to exist beyond large urban centres. This is why we have been arguing for the gifting of spectrum to support the development of such services. We appreciate Ofcom's consideration of this matter and its careful design of spectrum lots to increase the likelihood of their suitability for local TV.

Where local TV is not the answer, broadband has the potential to, in part, close the public service gap that might be left by a retreat by ITV from its regional commitments. However, as the BBC Trust's investigation of BBC Local concluded, broadband video is by no means universal either in coverage or adoption and so for many current ITV Regional viewers, broadband will not provide an appropriate substitute.

Section 6: Funding

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

We broadly agree with Ofcom's assessment of each possible funding source and its analysis of possible advantages and disadvantages. Whilst there are many different flavours, interventions fall into four broad categories:

- Increased public funding for PSBs (either via direct public funding or an increase to the licence fee).
- Redistributing funding and/or assets from the BBC and commercial PSBs.
- A levy on industry players.
- Reduced regulatory burdens on PSBs.

In the current economic climate it is difficult to see how increasing public funding or imposing a levy on industry players could be realistically achieved.

As stated earlier in our response, reducing regulatory burdens, in particular removing artificial barriers to consolidation, ought to be the starting point. Care obviously needs to be taken to ensure that reducing regulation does not threaten the provision or quality of the public service content being provided.

Where further intervention is required to sustain public service broadcasting, and where plurality is under threat, it would make sense to consider a redistribution of funding or regulatory assets from the BBC and other commercial PSBs.

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

See answer to previous question.

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

We believe that the gifting of regulatory assets is the most appropriate solution to Channel 4's funding issues. Using this mechanism would ensure the independence of the broadcaster while encouraging competition with both the BBC and commercial broadcasters. Any shortfall that might arise from the use of gifted regulatory assets could be made up using a portion of the 'switchover surplus' from the television licence fee.

The proposal for Channel 4 to take a stake in BBC Worldwide is an interesting idea; however, it could prove problematic. We would have concerns over governance of a BBC Worldwide entity controlled by both the BBC and Channel 4. Under the regulation of the BBC Trust we have already seen BBC Worldwide venture into areas that put public money at risk and reduce the incentives for investment by commercial publishers. This expansion included the launch of BBCGreen.com, a new site unconnected to existing BBC content, which is competing for a share of advertising revenues in a market which is yet to fully develop, and the acquisition of a 75% stake in Lonely Planet, the travel publisher now competing in the consumer magazines market. While the C4/BBC Worldwide proposal warrants further debate, it would need to be under a significantly improved and tightened governance model. We would also be concerned that such a JV could lessen competition between the BBC and Channel 4 and thereby act against the interests of plurality.

We are somewhat surprised that a market solution to Channel 4 has not been more explicitly considered through this consultation. The possibility that the economics of public service broadcasting would be enhanced by consolidation amongst the existing PSB operators warrants more detailed exploration. Whilst we do not have the ability to model the economics, this might be a significantly less complex solution to the existing public service broadcasters' current problems.

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?**

We will leave it to those closer to these matters to debate this issue more thoroughly.