



Local commercial analogue radio licence durations

Statement on changes to Ofcom's policy

Statement

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Contents

Section		Page
1	Executive Summary	1
2	Introduction	4
3	Policy options and consultation responses	8
Annex		Page
1	Statutory framework	26
2	Commercial Issues	30

Section 1

Executive Summary

- 1.1 Ofcom is responsible for the licensing of local commercial analogue radio stations. This includes re-advertising, re-awarding and renewing licences, if appropriate, in accordance with relevant legislation.
- 1.2 When Ofcom advertises a local commercial analogue radio licence, or re-advertises such a licence when it nears its expiry date, it can set a licence length of up to twelve years. Where a licensee also provides a service on a relevant DAB multiplex, it is eligible for an uncontested renewal of its analogue licence.
- 1.3 Our current policy, which we consulted on in 2007, is that re-advertised licences will be granted with an expiry date of 31 December 2015 or for five years, whichever is longer. This policy was considered the best option to maintain flexibility ahead of any new legislation regarding digital switchover. The common end date and subsequent shorter licence length were designed to ensure that we would not licence analogue stations far beyond a possible digital switchover.
- 1.4 The Digital Economy Act 2010 (“the 2010 Act”) introduced some changes to the way commercial radio is regulated. In particular, it allows the Secretary of State to nominate a date for digital switchover of certain services, requiring Ofcom to vary the length of relevant licences so that they end on that date. It also allows licensees who offer digital services on a relevant DAB multiplex to renew their analogue services for a further seven years.
- 1.5 Because of these changes, on 15 July 2010 Ofcom published a consultation on proposed changes to the duration for which local analogue commercial licences are granted (“the Consultation”). This is available at <http://stakeholders.ofcom.org.uk/binaries/consultations/local-licence-duration/summary/local-licence-duration.pdf>. The Consultation set out a number of policy options for setting the duration of re-advertised licences, including our preferred option – that local licences are re-advertised with a length of seven years. The desired outcome is a system which is fair to all, provides flexibility for the future, relative certainty for licensees and does not distort DAB incentives.
- 1.6 We received seven responses to the Consultation, most of which disagreed with our preferred option and instead favoured either a differential approach (with a variety of criteria suggested) or a duration of twelve years for all licences. One response was anonymous, and another completely confidential.
- 1.7 This statement sets out our policy decision on the duration of local analogue commercial licences.

Ofcom’s decision and next steps

- 1.8 We have assessed the policy options in light of the analysis presented in the Consultation and the responses we received.
- 1.9 While we understand why some respondents argued for a differential approach, we do not believe that such an approach would be appropriate. We have been unable to identify any criteria which can be consistently applied and deliver the desired outcome. A case by case approach might be very difficult to implement and could create uncertainty and perceived unfairness. Adopting a significantly different approach between sets of stations is also likely to treat some stations unfairly.

Moreover, all the suggestions we received proposed particularly long licences for stations likely to remain on analogue spectrum after any digital switchover. This would restrict the flexibility available to Ofcom to fulfil our spectrum management duties, or for Government to introduce a new regulatory regime.

- 1.10 This leaves a choice between the maximum twelve year duration and a shorter length, including the seven year option that we proposed in the Consultation.
- 1.11 We note that there is strong industry support for twelve years, given the greater certainty this would provide to operators. We appreciate the points about viability that have been made to us and, as we stated in the Consultation, we consider it important to offer potential licensees the opportunity to make a reasonable return on their investments, to ensure that operators are prepared to apply for licences and can maintain provision of a service. For this reason, we believe it would be appropriate to give licensees greater certainty than they are afforded by our current five year policy.
- 1.12 By considering the impact that licence duration might have on the nature and scale of initial start-up costs as well as the pattern of on-going operating costs and revenue flows, we concluded in the Consultation that licence periods of less than five years might significantly influence the commercial viability of radio broadcasters. Periods greater than five years might give commercial radio stations a better chance of recovering their total expenditure during the licence period depending on the way their business is structured and planned. No respondent provided quantitative evidence to contradict the analysis and conclusions. We therefore need to balance the consideration of station viability against other factors given that, in our view, licence durations shorter than twelve years but above our current five year policy are unlikely to prevent operators from earning a sufficient return on their investment and providing a high quality service for listeners.
- 1.13 Flexibility remains an important consideration, even taking into account the provisions of the 2010 Act. There remains a great deal of uncertainty around the future direction of the sector. Some stations are likely to continue on FM following a digital switchover, and it is important that Ofcom retains the ability to make changes to secure the optimal use of this spectrum in the future and maximise benefits to citizens and consumers. Major exercises (such as re-planning remaining licences in order to make the most efficient use of the FM band) would be more appropriately and effectively carried out following the expiry of licences rather than partway through licence periods, and so would be facilitated by having licences that were shorter than twelve years.
- 1.14 Such flexibility would also be useful if Government decided to introduce a new regulatory regime for those stations remaining on analogue frequencies, allowing high quality services to flourish and serve listeners' needs effectively. Having a shorter licence period is likely to increase Government and Parliament's flexibility to introduce a new regime, to the extent that the regime may include provisions that it would be difficult or undesirable to introduce partway through a licence period.
- 1.15 Respondents have suggested that we overestimated the incentives of stations to cease to provide a DAB service. Although we accept some of these arguments, we still believe that a significant difference between the length of new renewals and the duration of a re-advertised licence would distort incentives to continue to offer DAB services, given the additional years of revenue that would be on offer. Stations would of course be mindful of the risk of not being successful in a contested re-advertisement. But this may be a risk worth taking for some operators if they believed that the licence would be uncontested in any award process or that as an incumbent they would be highly likely to win any such contest. Stations which opted for re-

advertisement rather than renewal because of the longer licence length on offer might cease to provide a DAB service, which could reduce consumer choice.

- 1.16 We appreciate the concerns of respondents, and have considered their arguments carefully. However, the factors in favour of a shorter licence length – incentives in the case of stations providing a DAB service and flexibility in the case of stations which are likely to continue on analogue frequencies – coupled with our view that seven years is a sufficient period in which to earn a reasonable return on an investment, lead us to conclude that a seven year licence duration is more appropriate at this time.
- 1.17 Local commercial radio licences which are re-awarded will be granted for a period of seven years.
- 1.18 We expect to review this policy should the Secretary of State nominate a date for digital switchover, or in the event of other significant radio policy developments (such as Government setting out proposals for any new regulatory regime).
- 1.19 In the Consultation we said that we were postponing all re-advertisements previously scheduled in our timetable until a new policy on licence duration was adopted. We are publishing an updated timetable with this statement.

Section 2

Introduction

Background – the licensing process

- 2.1 Ofcom is responsible for the regulation of the commercial radio sector. One of our functions in this area is the licensing of local commercial analogue radio stations. This includes advertising, awarding and renewing licences in accordance with relevant legislation.
- 2.2 Under the Communications Act 2003 ("the 2003 Act"), we have a general duty to secure "the availability throughout the United Kingdom of a wide range of television and radio services which (taken as a whole) are both of high quality and calculated to appeal to a variety of tastes and interests" and to secure "the optimal use for wireless telegraphy of the electro-magnetic spectrum". In addition, under the Broadcasting Act 1990 ("the 1990 Act"), we have a duty to secure the provision of "a range and diversity of local services". In order to fulfil these duties, our general approach is to re-advertise existing local commercial analogue licences as they approach their expiry dates.
- 2.3 When Ofcom awards a local analogue radio licence, it can set its length at up to twelve years. Before 2007 Ofcom generally advertised licences for the statutory maximum of twelve years.
- 2.4 Where we propose to re-advertise a local licence, we can first publish a notice stating that we propose to grant a further licence in the area, and inviting 'declarations of intent' to apply for the licence. If only the incumbent registers an interest, the licence is re-awarded under a 'fast-track' procedure. If there is interest from other potential applicants the licence is advertised in an open competition, with the applications being assessed against statutory criteria in a 'beauty contest', designed to best meet the needs of listeners.
- 2.5 Some licensees can opt to have their licences renewed rather than re-advertised. A licensee who is providing a local digital sound programme service on a 'relevant' local radio multiplex service¹ is entitled to apply for a renewal of its licence on one occasion for a period of twelve years. Renewals, in contrast to re-advertisements, are uncontested.

The existing policy on licence duration

- 2.6 In our 2007 consultation, *The Future of Radio*², we considered the potential for the VHF Band II and medium wave spectrum to be made available for uses other than analogue radio broadcasting. Because of this possibility, we proposed that licences should be re-advertised with an expiry date of 31 December 2015, noting that by this time new legislation offering a greater degree of flexibility might be in place.

¹ A local radio multiplex service with a coverage area which to a significant extent includes the coverage area of the local service provided under the local licence (section 104A of the 1990 Act).

² The Future of Radio, Ofcom, 17 April 2008,

<http://stakeholders.ofcom.org.uk/binaries/consultations/futureradio07/nextphase.pdf>, from paragraph 5.82 onwards

- 2.7 In the resulting statement in 2007, *The Future of Radio: the Next Phase*³, we acknowledged the arguments made by respondents in relation to this proposal, including the suggestion that a licence may become so short as to dissuade any operator (including the incumbent) from applying. We also considered at what point the costs of running a licence award process became disproportionate when compared with the value of the licence to the successful applicant. We concluded that a licence should be granted for a minimum period of five years, in order to make it long enough to be viable, yet short enough to allow the flexibility to free-up spectrum.
- 2.8 Consequently, we decided that all local commercial radio licences which were re-advertised under the existing statutory framework would be granted for a five year period or with an expiry date of 31 December 2015, whichever was longer. Since publishing our statement we have re-advertised and re-awarded around 30 licences under this policy.

Rationale for reviewing our current policy

- 2.9 The previous Government's Digital Britain White Paper of June 2009⁴ proposed a Digital Upgrade for radio once certain criteria had been met. This policy envisaged all services carried on the national and local DAB multiplexes ceasing broadcasting on analogue. At the same time, a new tier of ultra-local radio, consisting of small local commercial stations and community stations, would occupy the vacated FM spectrum. Radio services on MW would either upgrade to DAB or, if they are within the ultra-local tier, to FM.
- 2.10 The future of this policy is a matter for Government. The Government has recently expressed its support for this approach, and has set out its expected future work in the Digital Radio Action Plan⁵.
- 2.11 The Digital Economy Act 2010 ("the 2010 Act") facilitates a future process of digital switchover. Specifically, it allows the Secretary of State to nominate a date for digital switchover for certain services and requires Ofcom to vary the length of relevant licences so that they end on that date⁶.
- 2.12 The 2010 Act introduces⁷ a further renewal of up to seven years for any licensee who has renewed for twelve years⁸, or who provides a digital sound programme service and has had their licence granted after 8 April 2010.
- 2.13 All licences renewed under this section can be varied to end on a date nominated by the Secretary of State for digital switchover of the service. Alternatively, if no date is nominated, notice may be given to Ofcom by the Secretary of State under section 105A of the 1990 Act setting a termination date (of not before 31 December 2015) in

³ The Future of Radio – the next phase, Ofcom, 22 November 2007, <http://stakeholders.ofcom.org.uk/binaries/consultations/futureradio07/summary/nextphase.pdf>, from paragraph 5.15 onwards

⁴ Digital Britain Final Report, DCMS, June 2009, <http://webarchive.nationalarchives.gov.uk/+/http://www.culture.gov.uk/images/publications/digitalbritain-finalreport-jun09.pdf>

⁵ Digital Radio Action Plan, DCMS, 8 July 2010, <http://www.culture.gov.uk/publications/7227.aspx>

⁶ Further information is provided in Annex1, Statutory Framework

⁷ As new section 104AA of the 1990 Act

⁸ Licences granted after 8 April 2010 are only eligible for renewal under s104AA of the 1990 Act (see Annex 1)

relation to such services⁹. Renewed licences can therefore be terminated either in the event of digital switchover or in the absence of such developments.

- 2.14 This new legislation reduces the need to set a common end date to facilitate a future digital switchover. As noted above, this was a key rationale for our existing policy.

The Consultation

- 2.15 We considered that the introduction of termination provisions in the 2010 Act was so significant that it justified reviewing the existing policy on licence duration. Consequently, on 15 July 2010 Ofcom published a consultation on proposed changes to the duration for which local analogue commercial licences are granted ("the Consultation")¹⁰.
- 2.16 In the Consultation, we set out four main options for setting the duration of re-advertised licences:
- Setting a further common end date for re-advertised licences, returning to the issue if and when there was greater certainty about a specific switchover date and the regulatory regime that would be in place after such an event;
 - Offering the maximum duration of twelve years for all re-advertised licences;
 - Choosing a different fixed length (of less than twelve years) for all re-advertised licences; and
 - Adopting a differential approach, where licences are offered for different durations based on a pre-determined set of criteria (such as previous DAB renewal, for example).
- 2.17 As part of our analysis, we also highlighted our preferred option – that all local commercial analogue licences are re-advertised with a length of seven years. We set out our view that seven years would provide an appropriate balance between the benefits of shorter or longer fixed licence durations. It would retain an element of flexibility, would give stations a better chance to recover their total investment during the licence period than the current length of five years, and would not adversely affect incentives for stations to continue to operate DAB services (as it matches the period of newly offered renewals).
- 2.18 This statement sets out our policy decision on the duration of local analogue commercial licences, based on the analysis presented in the Consultation and responses we received.

Other regulatory developments

- 2.19 This statement should also be seen in the wider context of related Ofcom projects and consultations. The 2010 Act allows limited deregulation of radio content, in particular allowing local stations to co-locate and share programming (effectively, to

⁹ Further information is provided in Annex 1

¹⁰ Local commercial analogue radio licence durations, Ofcom, 15 July 2010, <http://stakeholders.ofcom.org.uk/binaries/consultations/local-licence-duration/summary/local-licence-duration.pdf>

merge) within larger areas defined by Ofcom. Following our consultation last year, the statement published on 15 April 2010 sets out our new policy on localness¹¹.

- 2.20 In response to both the Digital Radio Action Plan and our general statutory duty to secure a range and diversity of services, we are currently undertaking research into the small scale commercial and community radio sector. This will provide evidence and data about the value these services provide to audiences, giving a greater understanding that can help inform future licensing and regulatory decisions. We expect to publish the results of this research towards the end of this year.
- 2.21 We have recently consulted on commercial communications in radio programming¹², proposing significant deregulatory measures – we expect to publish a statement in due course.

¹¹ Statement on commercial radio localness regulation, Ofcom, 15 April 2010, http://stakeholders.ofcom.org.uk/binaries/consultations/radio/statement/Localness_statement.pdf

¹² Broadcasting Code Review: Commercial Communications in Radio Programming, Ofcom, 28 June 2010, <http://www.ofcom.org.uk/consult/condocs/bcrradio2010/>

Section 3

Policy options and consultation responses

- 3.1 In this section we present a synopsis of the analysis that we put forward in the Consultation. We then summarise the views of respondents and set out Ofcom's consideration of these responses.
- 3.2 We outline at Annex 1 our relevant duties as set out in legislation. In the Consultation, we stated that our overall objective was to ensure that there is a range and diversity of local commercial radio services available, serving the interests of consumers and citizens. Our aim is to determine an appropriate approach to the duration of re-advertised licences to support this objective.

Criteria to consider and assessment approaches

- 3.3 In the Consultation, we outlined a number of factors that might be directly affected by the length of a licence. We identified a set of criteria, related to these factors, that we proposed to use to assess the impact of our policy options on different stakeholders.
- 3.4 These criteria were:
- **Flexibility** – we highlighted that we needed to take into account the possibility of changes to the regulatory framework for commercial radio in the future. Certain approaches to licence duration would give us greater flexibility to maximise benefits to citizens and consumer by securing the optimal use of the spectrum, or maximising flexibility for Government and Parliament to set an appropriate regulatory regime for stations remaining on analogue bands after digital switchover.
 - **Viability** – we noted that a licence has to offer applicants the opportunity to make a reasonable return on their investments to ensure that operators are prepared to apply for the licence and can maintain provision of a service. We noted that any decision on licence duration could have an effect on the financial viability of stations and therefore the variety of services available to listeners. The Consultation included an annex with a more detailed assessment of the impact licence duration might have on capital investment, business contracts and recouping initial start-up costs. We also recognised that the exact relationship between licence duration and the viability of a station is unclear. It may be that there is a linear relationship between the two – the prospect of viability for a station becomes ever more likely as licence length increases. Alternatively, given the lifespan of certain assets which need to be replaced, it may be that there is a particular licence length at which a station becomes viable, and allowing a longer licence duration does not significantly affect this.
 - **Competition for licences** – to secure the best range of local commercial radio services, it is useful to have a broad choice of proposed services from which to select a licensee (i.e. competition for licences). In our view, there is likely to be a trade-off between setting a licence duration long enough to encourage a number of applicants for a re-advertised licence, and one short enough to afford regular opportunities for the competitive selection process. Additionally, licence duration is likely to have some effect on the purchase of stations (another form of competition for licences), as it will affect the attractiveness of existing stations to potential buyers

- **Incentives** – we noted that the length of a licence may change radio stations' incentives to offer DAB services, having a knock-on effect on consumer choice. DAB digital radio is currently the only platform which offers the benefits of digital radio free-to-air, to mobile and portable receivers, and which can guarantee a range of local and UK-wide services to the vast majority of the UK. Because of these consumer benefits, we have previously stated that it is important to put in place the conditions to allow DAB digital radio to expand and thrive in the digital age¹³. The duration of a re-advertised analogue licence might distort the incentives of a number of stations which also provide a DAB service and are eligible for the new seven year renewal under the 2010 Act. For instance, offering re-advertised licences for a period significantly longer than seven years might incentivise operators to opt for re-advertisement rather than a renewal. As a consequence they might withdraw their provision of DAB services.
- 3.5 We stated that we would evaluate the options identified against these criteria, noting the impact they may have on radio listeners, radio stations (incumbents and new entrants) and radio multiplex operators¹⁴. The Consultation invited respondents to comment on the criteria (in particular on our general assessment of the relationship between licence length and economic viability) and our assessment of the options, including on our preferred proposal on the approach and length of re-advertised licences.
- 3.6 Our consultation document represented an Impact Assessment, as defined by section 7 of the 2003 Act, which was largely qualitative in nature. We asked respondents to submit any quantitative evidence they had to support their arguments. Here we discuss the evidence that was submitted (which was largely qualitative) so that this section – taken together with Annex 2 of this statement – represents our assessment of the impact of our proposals.
- 3.7 Ofcom is required by statute to have due regard to any potential impacts of our proposals on race, disability and gender equality. We stated in our consultation that on the basis of our initial screening we considered that a full Equality Impact Assessment was not required, and respondents have not suggested that our proposals will have an impact on race, disability and gender equality. Accordingly, we have not carried out a full Equality Impact Assessment.

Consultation responses

- 3.8 The key points raised by respondents in relation to this analysis are summarised below. We take the same approach in each section of this statement headed "Consultation responses".
- 3.9 We received seven responses¹⁵ to the Consultation, including submissions from UKRD, Town and Country Broadcasting, Lincs FM, RadioCentre and Absolute Radio. One response was anonymous, and another completely confidential.
- 3.10 Absolute Radio's submission was a single line expressing support for RadioCentre's response. Therefore in sections below where we refer to RadioCentre's submission, we are outlining views with which Absolute Radio agrees.

¹³ For example, see paragraph 5.76 of Radio – Preparing for the Future, Ofcom, 19 October 2005, http://stakeholders.ofcom.org.uk/binaries/consultations/radio_review2/p2.pdf

¹⁴ We did not propose to assess the impact on radio advertisers as our starting assumption was that the impact should be broadly neutral (given that they would still have access to the basic advertising medium).

¹⁵ Responses can be found at <http://stakeholders.ofcom.org.uk/consultations/local-licence-duration/?showResponses=true>

- 3.11 Generally, respondents agreed with the criteria against which the options would be assessed or did not highlight any objections to these criteria.
- 3.12 UKRD stated that it 'agreed broadly' with the criteria identified. Town and Country Broadcasting expressed explicit agreement with our inclusion of competition for licences as a factor.
- 3.13 RadioCentre's response dealt extensively with each of the criteria. Most of its comments focused on the relationship between these criteria and different licence lengths, and as such are dealt with in the sections below.
- 3.14 RadioCentre also raised significant points in relation to the flexibility criterion. It argued that recent changes in legislation and statements of Government policy regarding the future of analogue radio broadcasting had removed the need to issue shorter licences in order to retain legislative and regulatory flexibility. The 2010 Act means Government can effectively terminate any licence awarded from now on in the event of a digital switchover, and in RadioCentre's view this represents an appropriate method of implementing any necessary changes. The submission stated that longer licences had not prevented Ofcom or the Government from making regulatory changes in the past and that the consultation gave no indication of what changes might be prevented in future by longer licences.
- 3.15 In essence, this argument amounts to a rejection of our suggestion that future policy flexibility is a relevant criterion.
- 3.16 More generally, RadioCentre argued that any decision by Ofcom to depart from the statutory maximum period of 'no more than twelve years'¹⁶ should be based on a clear and compelling case.
- 3.17 Furthermore, RadioCentre argued that if the expectation of Parliament had been for licences to have a length of anything other than twelve years, this would have been stated during deliberations on the Digital Economy Bill. Instead, the Government and Parliamentarians had indicated support for longer analogue licences during the debates. Lincs FM also made this argument, adding that while legislation incentivised DAB take-up, it was inappropriate for Ofcom to use its discretion to penalise FM-only stations.
- 3.18 A number of respondents highlighted that not all of the criteria would be applicable to every licence. In particular, the issue of incentives was relevant only to those stations that had a path to digital.
- 3.19 Similarly, Town and Country Broadcasting suggested that the impact of licence length on the viability of a station was far less important for larger mainstream services, which 'generate a much higher return on investment'.

Consideration of responses

- 3.20 We view the small number of points raised about the criteria as indication that our framework for assessment of the options is considered by respondents to be largely correct.

Flexibility

- 3.21 We disagree with RadioCentre's assertion that future policy flexibility is not a relevant criterion. Ofcom is required by statute to secure (amongst other things) the optimal

¹⁶ Section 86 of the 1990 Act

use for wireless telegraphy of the electro-magnetic spectrum. Given the possible changes to the industry in the near future due to digital switchover, and the continued uncertainty about the date of switchover, future flexibility is important in allowing Ofcom to fulfil its duties in the way that best serves the interests of citizens and consumers.

- 3.22 For instance, in a post-switchover world, it might be appropriate to conduct a re-planning exercise in specific localities or on a wider basis, in order to optimise the use of FM spectrum for the purposes of radio broadcasting securing improvements in the availability of services for listeners. Similarly, the Government's Digital Radio Action Plan tasks the Coverage and Spectrum Planning Group (of which Ofcom is chair) with considering and identifying future uses for the MW spectrum and any vacated FM spectrum – it could be that such considerations lead us to conclude that existing licences need to be re-positioned in order to make most efficient use of this band.
- 3.23 While we agree that regulatory changes can be made during the lifetime of a licence – for example, the recent reduction in localness regulation – we consider that more major exercises such as those outlined above would be more appropriately and effectively carried out following the expiry of licences rather than partway through licence periods, and so would be facilitated by having licences that were shorter than twelve years.
- 3.24 We also do not agree that the termination provisions in the 2010 Act, by themselves, provide sufficient flexibility for possible future changes to the commercial radio regulatory regime. Licences awarded from now on can be terminated if the Government decides that it is no longer appropriate for the service to continue to be provided in analogue form. Which licences are selected is a matter for Government, but there is a strong expectation that some stations will remain on FM. Indeed, Government has recently stated that *'FM will remain a platform for small local and community radio for as long as these services want it'*¹⁷.
- 3.25 Additionally, the Digital Radio Action Plan tasks the Government Policy Group with developing *'recommendations on the future regulatory regimes'* for those small local and community stations remaining on analogue after switchover¹⁸.
- 3.26 So Government's position is that stations remaining only on FM will not have their licence terminated as part of any switchover, but could come under a different regulatory regime in the future. Having a shorter licence period is likely to increase Government and Parliament's flexibility to introduce a new regime, to the extent that the regime may include provisions that it would be difficult or undesirable to introduce partway through a licence period.
- 3.27 More generally, and aside from the switchover process, it might also be that Parliament deems it appropriate to move towards a more liberalised approach to radio licensing (such as auctions and the ability to trade spectrum) in the future. We would also note that Government plans to begin the legislative process for a new Communications Bill in 2012¹⁹.
- 3.28 With the likely changes that a digital switchover would bring, it is imperative that Ofcom retains the ability to secure the optimal use of the spectrum in the future, thus maximising the benefits to citizens and consumers. Such flexibility would also be useful if Government decided to introduce a new regulatory regime for those stations

¹⁷ See Ed Vaizey's speech to Intellect Conference, 8 July 2010

¹⁸ Task 1.10 of the Digital Radio Action Plan (estimated completion date of Q3 2012).

¹⁹ DCMS Structural Reform Plan, 15 July 2010

remaining on analogue frequencies to allow high quality services to flourish and serve listeners' needs effectively.

- 3.29 For these reasons, we consider flexibility to be a crucial criterion, and continue to view the impact of each option on this factor as important in our assessment.

Other issues

- 3.30 We agree that any decision on licence duration should be based on clear and compelling arguments. However we differ from RadioCentre and Lincs FM in that in our view, as the Broadcasting Act 1990 gives Ofcom discretion to grant licences for 'no more than twelve years', we are not bound to any particular length as a 'default' position. The burden of proof is no higher for another approach than it is for a duration of twelve years.
- 3.31 Neither Government nor Parliament has indicated explicit support for twelve year licences. Statements made during debates on the Digital Economy Bill note that there are 'clear arguments' for longer licences - but that is in relation to our existing five year policy - and that Ofcom has discretion over the matter²⁰. As part of the process of determining a policy on licence duration, we have identified and discussed the arguments in favour of longer licences.
- 3.32 Ofcom is committed to supporting the evolution of radio²¹, and much of our current work is focused on this. In 2009 we invited views and evidence as to whether we should re-examine the definitions and use of formats²², and this invitation remains open with the issue still under consideration. Similarly, we are in the process of conducting a major research project on small scale commercial and community stations, with a view to establishing an evidence base to assist Government in assessing the options for the future of the sector as part of the Digital Radio Action Plan.
- 3.33 We agree with respondents that not all of the criteria we identified are applicable to every licence, and this was a key reason for our examination of the differential approach. When analysing the options we are mindful that some factors may not apply to particular stations, and weight our considerations accordingly.

Option 1: a further common end date

- 3.34 Our decision in 2007 to adopt a common end date for all re-advertised licences was in part prompted by the desire to retain flexibility for the sector. By opting not to issue licences far into the future, we were allowing for regulatory flexibility should Government decide to implement a digital switchover policy.
- 3.35 Although the 2010 Act provides the legislative means to facilitate a digital switchover, there is still a large degree of uncertainty around the future regulatory environment for analogue radio. Consequently, the Consultation assessed the option of setting a further common end date and returning to the issue when we have greater clarity.
- 3.36 We considered that a benefit of this option would be the policy **flexibility** it would provide, allowing (for example) the construction of a new regulatory framework for local commercial stations that remained on analogue frequencies even after a digital

²⁰ Hansard (Lords), Digital Economy Bill Committee Debate, 3 February 2010, column 279 and Hansard (Commons), Digital Economy Bill Debate, 6 April 2010, column 855

²¹ See paragraphs 4.44-4.48 of the Ofcom Annual Plan 2010/11

²² Proposal 8 in <http://stakeholders.ofcom.org.uk/binaries/consultations/radio/summary/condoc.pdf>, Radio: the implications of Digital Britain for localness regulation, Ofcom, 31 July 2009

switchover. We viewed the effect of this approach on **viability, competition for licences and incentives** to be varied – essentially, the impact would depend on how far from the agreed common end date any given licence was re-advertised.

- 3.37 We also pointed to several difficulties with this option which were highlighted in 2007 and remained pertinent. In particular, we noted that there was no firm indication at present as to what an appropriate end date would be, and we would not be able to tailor this end date to changing circumstances. As before, there would probably be a need to set a minimum licence duration to ensure that stations had a reasonable opportunity to earn a sufficient return on their investment and so applications were received, or risk spectrum being left unused.

Consultation responses

- 3.38 Generally, respondents agreed with our assessment of the common end date option.
- 3.39 RadioCentre noted that such an option would not be fair or consistent, as it is not clear what an appropriate common end date would be and any date selected would be fairly arbitrary in nature. It also agreed that operators would be affected differently depending on when their licence was due to expire in relation to this date.
- 3.40 RadioCentre said that flexibility would not in fact be a benefit of this approach, as Ofcom and Government will have the discretion to make necessary policy changes regardless of licence duration.
- 3.41 Lincs FM agreed that the original argument for ‘near’ common end dates no longer applied as the Secretary of State will hold sufficient powers to terminate analogue licences if DAB migration is planned.
- 3.42 One respondent suggested that a common end date set significantly in the future would give sufficient time to convert all radios to a digital format.

Consideration of responses

- 3.43 We agree with the arguments raised by respondents highlighting the disadvantages of the common end date approach.
- 3.44 Given the provisions of the 2010 Act which facilitate a digital switchover, we do not think that the benefit of a period in which to replace existing radios is a relevant consideration when deciding our approach to analogue licence duration.
- 3.45 As we stated in the Consultation, we believe that setting a common end date for all licences would have a varied effect on station viability, competition for licences and the incentives of licensees. The impact would depend on how far from the agreed common end date any given licence was re-advertised. We are of the view that such an approach would provide significant flexibility for Ofcom to fulfil its spectrum management duties. However we recognise the negative impact on licensees in terms of inconsistency and do not therefore favour setting a common end date.

Options 2 and 3: a fixed licence duration of either the full twelve years (option 2) or less (option 3) for all re-advertised licences

- 3.46 Before adopting our current policy in 2007, Ofcom licensed analogue stations for the statutory maximum of a twelve year period. In the Consultation we considered whether there was a case for reverting to issuing licences for a full twelve years.

- 3.47 We suggested that twelve years would provide the maximum permissible period for licensees to make a reasonable return on their investment, although we noted that the termination provisions of the 2010 Act meant that any benefits in terms of **viability** would be uncertain, reducing the importance of this factor.
- 3.48 We also highlighted two key disadvantages of this twelve year option:
- Firstly, it would license stations far into the future, so limiting the **flexibility** to introduce a new framework for any stations remaining on FM after a digital switchover (or for other unforeseen policy objectives).
 - Secondly, there could be an **incentive** for stations currently on DAB to cease broadcasting on the platform and forego their right to an uncontested seven year renewal in return for a new twelve year analogue licence not tied to DAB. They may do this if they believe that the licence would be uncontested in an award process or that, as the incumbent, they would be highly likely to win any such contest. A reduction in DAB services could be detrimental to listeners.
- 3.49 We concluded that the overall effect on **competition for licences** would be unclear – although a longer licence would be more attractive to new entrants, the opportunity for contested re-advertisements would be restricted to once every twelve year period.
- 3.50 The Consultation went on to note that we could set a policy whereby we licensed all analogue stations for the same period, choosing an appropriate duration based on the needs of listeners, now that the need for a common end date has diminished. We considered the effect that longer or shorter licence lengths would have on our criteria.
- 3.51 We noted that a shorter licence duration would retain more **flexibility** should changes to the regulatory framework for commercial radio be deemed appropriate. Conversely, a longer licence length would reduce the flexibility available by licensing further into the future and restricting the timescale in which a new framework could be adopted.
- 3.52 We highlighted that a key impact of shorter licence durations could be on station **viability**. The costs and revenue of a radio station are likely to change over time, and particularly short licence durations may have a damaging effect on the ability to finance a station and the ability for operators to generate a reasonable return on their investment, to the detriment of listeners. A longer licence duration might increase the economic viability of a radio station, however we noted that it is unclear whether the relationship between licence duration and viability is a directly linear one.
- 3.53 The effect on **competition for licences** of longer or shorter licence durations was, in our view, unclear. Shorter licence lengths would mean more frequent rounds of competition, allowing new entrants the opportunity to apply for licences. However shorter licence durations may not give new entrants a reasonable opportunity to earn a sufficient return on their initial investment, thus discouraging potential operators from applying for licences or from purchasing existing stations. Longer licence durations would give fewer opportunities to enter the market through the re-advertisement process. But the value of a longer licence may encourage more entry when licences are re-advertised, or more entry through the acquisition of existing stations.
- 3.54 We discussed the **incentives** of stations to provide DAB services under this option, noting that they would depend on how the licence duration relates to the length of newly offered renewals. If the re-advertisement length was the same as or less than the maximum renewal length of seven years, stations that provide a DAB service would be strongly incentivised to continue doing so, retaining the full benefits for

consumers of a diversity of services. If the re-advertisement length was longer than the renewal length, these stations may opt for a re-advertisement, possibly ceasing to provide their digital service. The greater the difference between the duration of re-advertised licences and renewals, the stronger the incentive either way.

- 3.55 We examined in detail the effect on our criteria of two specific licence durations – our *de facto* existing policy of five years and a seven year policy which matches the maximum DAB renewal contained within the 2010 Act. We did, however, note that the overall analysis could help guide the assessment of a wider range of licence lengths.
- 3.56 We also produced a table (Figure 1 below) which set out a comparison between twelve, seven and five year licence periods discussed in options 2 and 3, intended to provide an indication of the relative performance of each of the different licence durations rather than an absolute measure. The table serves to illustrate the trade-off between policy flexibility and station viability: while longer licences may increase station viability, they will tend to reduce policy flexibility.

Figure 1 **Impact summary**

Criteria	5 years	7 years	12 years
Policy flexibility	✓ ✓	✓ ✓	✓
Station viability	✓	✓ ✓	✓ ✓
Competition for the licences	-	-	-
Incentivises stations to retain DAB services	✓	✓	✗

Note: '✓' means the licence length has a positive impact on the criterion (more ✓'s mean a more positive impact); '✗' means we have a concern (e.g. twelve year licences may significantly change the incentives for radio stations to provide DAB services); '-' means it is unclear whether the impact will be positive or negative.

- 3.57 Our analysis of these two options led us to conclude that seven years would provide an appropriate balance between the benefits of shorter and longer licences.

Consultation responses

- 3.58 Respondents on the whole disagreed with our assessments of these options. Most submissions argued that the disadvantages of the twelve year approach that we had highlighted were not applicable to all stations, or had been overstated. Respondents also felt that the advantages of twelve years to stations had not been fully explored or given sufficient weight.

- 3.59 In tandem with this, most respondents rejected our assessment of the benefits of shorter licences. Town and Country Broadcasting described our view that seven years provided an appropriate balance of the benefits as 'a fudge'.
- 3.60 RadioCentre referred to its argument that Ofcom and Government would retain significant discretion to make necessary policy changes and so the **flexibility** benefits we had identified for shorter licences were not relevant considerations.
- 3.61 Most respondents felt that our analysis of the effect on **viability** of different licence durations did not place enough weight on the advantages that longer licences would bring.
- 3.62 RadioCentre argued that the most significant costs faced by a radio station are those that need to be planned and recouped over the longest period. The best chance of keeping large costs such as property and transmission low would be to spread such costs over an extended period of time. As such, longer licence duration was of key importance to the viability of a station.
- 3.63 RadioCentre also contended that shorter licences would exclude new entrants from the market, given the capital and up front expenditure involved (most notably transmission costs, which would be 'prohibitively expensive' in RadioCentre's view).
- 3.64 Both RadioCentre and UKRD noted that licence duration had an effect on funding and investment arrangements. For instance, potential investors (who often look for medium term investments) would be difficult to attract to a station with a shorter licence as there would be less certainty that licences would be secured for the lifetime of the investment.
- 3.65 In addition, RadioCentre highlighted that commercial radio groups often seek funding for their whole portfolio of stations, and that the funding that they seek is based on the average licence term of the stations in question. It commented that longer licences would have a clear benefit in cases such as these.
- 3.66 Some submissions, including UKRD's, suggested that our assessment of viability was driven by historical data and as such should not be relied on as the basis for policy decisions. Ofcom's assessment of applicants' business plans which we referred to in the Consultation was, in respondents' views, conducted when the industry was far healthier than today. Furthermore, it was argued that some applicants may have overstated the prospective commercial success of their stations in the past.
- 3.67 UKRD, RadioCentre and Lincs FM all highlighted that commercial radio revenues and profitability have declined significantly due to structural and cyclical changes in the sector, and that the current trading environment remained difficult. Respondents also pointed out that a large number of commercial radio stations remain unprofitable, increasing the need for longer licences.
- 3.68 In response to our assertion that the effect on **competition for licences** was largely unclear, RadioCentre argued that demand for licences, both in terms of applications and potential purchases, is likely to be greater if licences are longer in duration, and therefore provide the prospective owners with a more attractive proposition.
- 3.69 Town and Country Broadcasting agreed, arguing that it had been demonstrated that five years was too short a licence length to generate competition for smaller scale licences (although the response did note that this was untested for larger licences).

- 3.70 We received mixed responses on the issue of the **incentives** of licensees to continue to provide DAB services. Several respondents, including RadioCentre, acknowledged that it was necessary to consider how the policy on licence durations might impact on the provision of DAB services. One respondent suggested that awarding analogue licences for seven years or longer may remove one of the incentives to be on the DAB platform.
- 3.71 However, a number of arguments were raised against our assessment. RadioCentre suggested that we had failed to consider a number of disadvantages associated with ceasing to provide a DAB service, regardless of the length of licence offered if stations opted for re-advertisement. These included:
- the fact that the licence in question may not be re-advertised at all;
 - the possibility of the suspension of a licence if a licensee ceased to provide a digital service;
 - the significant costs associated with a licence application; and
 - the risk of losing a re-advertisement contest.
- 3.72 RadioCentre argued that these factors meant the level of risk of opting for a re-advertisement was extremely high. As such, stations would be highly incentivised to stay on DAB regardless of any benefits they could obtain from a longer analogue licence.
- 3.73 Several respondents argued that weight should not have been given to the incentives factor, given that a significant number of stations did not currently provide DAB, nor were likely to in future. For instance, UKRD stated that the analysis was being driven by *‘an inappropriate and wrong-headed attachment to the impact of DAB licence arrangements which have, in essence, no bearing whatsoever in respect to FM licences which have no future route or, indeed, desire to route, to a DAB broadcast future’*. Lincs FM concurred, stating that where analogue licences had not been renewed by way of DAB commitment, there was ‘no logic’ for anything other than twelve years.

Consideration of responses

- 3.74 As outlined above from paragraph 3.21 onwards, we believe there are compelling reasons why **flexibility** remains an important consideration. Adopting a longer licence length would result in stations being licensed far into the future, restricting the potential to make changes to secure the optimal use of the spectrum. We consider that any major changes following a digital switchover would be more easily carried out after the expiry of licences rather than partway through licence periods. Consequently, shorter licences would impact more positively on this criterion.
- 3.75 We appreciate the issues of **viability** that have been highlighted to us, including points around expenditure, funding and investment. As we stated in the Consultation, we consider it important to offer potential licensees the opportunity to make a reasonable return on their investments, to ensure that operators are prepared to apply for licences and can maintain provision of a service.
- 3.76 In Annex 5 of the Consultation (using data from a study we published in 2009²³), we set out the different cost categories applicable to a typical local commercial radio

²³ UK Radio Impact of regulatory relaxations, Ofcom, 5 May 2009, <http://stakeholders.ofcom.org.uk/binaries/consultations/radio/annexes/annex8.pdf>

station, the likely scale of these cost categories and the planning periods typically associated with them. Specifically, we considered the impact licence duration might have on the nature and scale of initial start-up costs as well as the pattern of on-going operating costs and revenue flows.

- 3.77 We concluded that licence periods of less than five years might significantly influence the commercial viability of radio broadcasters, whereas periods greater than five years might give commercial radio stations a better chance of recovering their total expenditure during the licence period depending on the way their business is structured and planned. For this reason, we believe it would be appropriate to give licensees greater certainty than they are currently afforded by our five year policy.
- 3.78 No respondent provided quantitative evidence to contradict the analysis and conclusions presented in this annex²⁴. We include a final version at Annex 2, which is unchanged from that presented in the Consultation.
- 3.79 We agree broadly with RadioCentre's view of the wide variety of costs faced by operators. We set these out in Annex 2, and note that securing longer contracts with suppliers may reduce the annual cost of these contracts.
- 3.80 However we have not seen any evidence which indicates that the difference between contracts of seven or twelve years (or indeed any other length) has a material impact on a station's operations. As set out in Annex 2, the majority of costs faced by a radio station are planned for on a short to medium term basis (e.g. 1-5 years). While property leases (as we acknowledged in the Consultation) are often agreed for longer periods, they commonly include break clauses which stations may be able to plan in accordance with the length of any licence. Similarly, we are aware that existing analogue stations can renew their analogue transmission contracts on existing terms, and therefore will not be prejudiced by shorter licence periods. Incumbent operators are also likely to have staff, offices and other equipment in place, further reducing the costs which have to be spread over a long period of time.
- 3.81 We do acknowledge that licence length is likely to be more important to new entrants, however, given the higher level of capital expenditure, costs of initial start-up activities and uncertainty of revenue in early years. This is a factor that we weigh carefully against competing arguments in determining an appropriate length. Nevertheless, as set out in our Consultation, most of these costs are likely to be planned for or depreciated over a five year period.
- 3.82 In terms of being able to secure investment during the lifespan of a station, we would highlight that there will always come a time when a licence would be near its expiry date, regardless of its length, and stations have always needed to negotiate such a situation. We do acknowledge that for shorter licences that point would arrive sooner. We accept RadioCentre's point that funding is often sought by radio groups on the basis of the average length of their licences, and that a longer licence length would result in a higher average and greater funding opportunities. We therefore consider this as an argument in support of longer licence lengths.
- 3.83 The analysis of business plans which we referred to in the Consultation was indeed conducted some time ago. The lack of competitive licence re-advertisements has meant we are not able to conduct a similar exercise at this time. We used this analysis to highlight the expectation of most applicants that they would make an annual operating profit by year three of the licence period. No respondent indicated what, in their view, a more realistic period would be.

²⁴ RadioCentre provided quantitative evidence demonstrating the decline in revenue across the commercial radio sector through to 2009. We respond to these points in paragraphs 3.84

- 3.84 We acknowledge that the industry has faced significant economic challenges in recent years, but we note that the latest data suggests that revenue has recovered from lower levels in 2009²⁵.
- 3.85 None of the responses provided evidence to suggest that there is a clear and material link between the length of a licence and the level of profitability over the duration of the licence. Unprofitable stations are likely to be unprofitable for reasons other than having shorter licence lengths (for example, a longer licence length is unlikely to mean that quarterly advertising revenue is greater).
- 3.86 We would also highlight that this policy is not being set in isolation. The regulatory measures introduced in April of this year aid commercial radio financially²⁶ and address factors that are more closely related to the profitability of a licence (such as small size and the costly provision of local material) than licence duration. Similarly, we have recently proposed significant deregulation in relation to commercial communications in radio programmes²⁷, which if adopted would also be likely to benefit stations financially.
- 3.87 We noted in our consultation that a longer licence may encourage more entry when licences are re-advertised, or more entry through the acquisition of existing stations²⁸. However, we also highlighted that there is a trade-off between the attractiveness of any licence and the frequency of opportunity that new entrants have to contest any re-advertisement. RadioCentre does not address this point when considering **competition for licences**.
- 3.88 Similarly, we would highlight that potential buyers of existing stations are to an extent constrained by the formats and licence conditions that were set on the basis of the incumbent's application. New entrants wishing to provide a radically different proposition might be more likely to opt for a licence application as opposed to purchasing an existing station.
- 3.89 We therefore remain of the view that the effect of longer or shorter licences on competition for licences is unclear.
- 3.90 On the issue of **incentives**, we do not believe that all of the disincentives that RadioCentre highlights are applicable for stations. In particular:
- Our general policy is that we re-advertise licences when they come to the end of their duration²⁹. If there were a compelling case for a particular licence not to be re-advertised, we would engage with the incumbent prior to making our decision. An operator who had the option of securing a further renewal would always know the situation ahead of making its decision. We therefore do not think that the possibility of a licence not being re-advertised would act as a disincentive.
 - Stations that opt to come off DAB during the period of their current, renewed licence may indeed face the suspension of their service, given that DAB provision is a condition of their licence. However this does not constrain them in deciding to opt for a re-advertisement or renewal at the end of their licence, when they could cease to provide a DAB service.

²⁵ Revenue of radio licensees collected by Ofcom shows a 5.5% year on year increase in Q1 2010 for local commercial radio.

²⁶ Statement on Commercial Radio Localness Regulation, Ofcom, 15 April 2010

²⁷ Broadcasting Code Review: Commercial Communications in Radio Programming, Ofcom, 28 June 2010, <http://www.ofcom.org.uk/consult/condocs/bcrradio2010/>

²⁸ Paragraph 4.48, Local Analogue Commercial Licence Durations, Ofcom, 15 July 2010

²⁹ Paragraph 2.3, Local analogue commercial radio licence re-advertisement: notes of guidance for applicants, Ofcom, 28 November 2007

3.91 We accept that other disincentives are likely to be considered by operators:

- We acknowledge that a station would be mindful of the risk of not being successful in a contested re-advertisement, and noted this in the Consultation. However we highlighted that the risk may be considered worth taking by some stations, particularly if they believe that the licence would be uncontested in any award process or that as an incumbent they would be highly likely to win any such contest.
- We accept that the cost of an application was not discussed in the Consultation and that this represents an additional disincentive to operators. However operators are likely to off-set the cost of an application against the possibility of additional years of revenue above the number of years that would be granted on renewal.

3.92 We agree with respondents that the incentives argument is only applicable to certain licensees and afford it weight accordingly for those stations with a presence on DAB.

Option 4: a differential approach, with licence length set in relation to a station's circumstances

3.93 The local commercial radio market is diverse and in the Consultation we noted that the criteria against which we have assessed our options may have more importance for some stations than for others. For example, some smaller stations might have more difficulty generating advertising revenues than larger competitors, and as such might need a longer licence length to have a reasonable opportunity to earn a sufficient return and ensure their **viability**. Similarly, a number of stations are unlikely to be carried digitally, either because of their size, or because local DAB multiplexes do not map suitably to their analogue licensed area or have no spare capacity. The duration of re-advertised licences is unlikely to impact on the **incentives** of these stations, given that digital carriage is not an option for them.

3.94 Licence duration might therefore have an asymmetric impact on different stations. Consequently, we considered whether an approach more closely linked to the circumstances of individual stations might be appropriate.

3.95 The most radical version of this approach would be to consider what licence length to set on a case-by-case basis, taking into account factors such as the level of interest, the size of the coverage area, the digital options available etc. Such an approach might prove very difficult to implement, given that Ofcom would have to set out criteria against which licence lengths would be considered and assess these in the case of every licence. It would increase regulatory cost – there could be inconsistency and perceived unfairness.

3.96 An alternative could be a differential approach, offering different licence durations for re-advertised licences depending on a single pre-determined criterion. This would likely be easier to implement. The 'fairness' of the approach and the applicability of the criterion would be key considerations.

3.97 We considered a specific example of such a criterion, suggested to us by a licensee, namely whether previous holders of a licence have provided digital services and taken up renewal options. Any licence that has previously been the subject of a twelve year renewal could be offered (say) a seven year licence length, whilst all other licences would be offered for a period of twelve years.

3.98 This would mean that non-DAB stations would benefit from a long licence duration, which would probably serve to make the licence more attractive to operators. There

would, however, be less policy flexibility, with these stations being licensed far into the future. Licensees that had already taken advantage of a twelve year renewal would not be incentivised to seek re-advertisement, abandoning digital broadcasting in the process, as they would receive the same licence length through an uncontested renewal.

- 3.99 However, we highlighted that a tiered policy based on DAB provision would take back some of the renewal benefits a station had gained by offering DAB – they would lose out relative to other licensees for choosing not to provide a digital service anymore. Furthermore, any new applicants for these licences would have their licence duration determined on the basis of the decisions of previous licensees.

Consultation responses

- 3.100 Respondents on the whole were very supportive of this option. UKRD, and Town and Country Broadcasting favoured this approach. Lincs FM and RadioCentre indicated that they would accept it as a 'reluctant compromise' if Ofcom continued to place significant weight on the impact of a longer licence duration on the incentives of licensees.
- 3.101 As has been highlighted, most submissions suggested that one of our arguments in support of seven years – the possible effect on incentives to continue to provide DAB services – was not applicable for smaller stations that are unlikely to go digital. Respondents were strongly of the opinion that such stations should not have their licence duration determined by factors that are not relevant to them.
- 3.102 Both Lincs FM and RadioCentre indicated reluctant support for an approach which drew on the example we gave in the Consultation. Following this approach we would re-advertise for a seven year duration any licence that had previously been renewed for twelve years and had an option of a further seven year renewal. All other licences would be re-advertised with a twelve year duration.
- 3.103 RadioCentre responded directly to some of the drawbacks of a differential approach that we highlighted in the Consultation. The response suggested that the issue of new applicants having the duration of their licences determined on the basis of the action of previous licensees had a limited impact. Providing that such information was clear and transparent, and available to any potential applicant or buyer when reviewing the status of a licence and carrying out their due diligence prior to taking a view on the value of a licence, then no party would suffer.
- 3.104 RadioCentre also disagreed with our assessment that such an approach would 'take back' the benefits of renewal. The response argued that stations which had renewed would have already received the benefit of an uncontested renewal and would not now be disadvantaged, since they would receive the same licence length through re-advertisement as through a further renewal.
- 3.105 UKRD proposed a slightly different approach, whereby licences would be re-advertised with different durations 'based upon the likely future or operator choice of the station concerned'.
- 3.106 Town and Country Broadcasting argued that larger licences are more profitable and will be the subject of greater demand, while smaller licences struggle to make money. The response suggested that we should regulate these two groups differently, offering longer licences to stations that would most benefit by differentiating on Measure Coverage Area (MCA). The response therefore proposed that smaller stations should be given a full twelve years, whereas larger licences or networked local licences should be re-advertised with a duration of five years. It also

suggested that financial analysis and market knowledge was available to Ofcom which would indicate which licences would be particularly profitable and which would not.

- 3.107 One response suggested a similar approach, whereby ultra small scale analogue licences could be awarded for up to twelve years in instances where there was either no DAB multiplex in operation or proposed to launch, or where the MCA was less than 75,000. Shorter licence lengths would be offered in other areas.

Consideration of responses

- 3.108 We acknowledge that there is strong support for a differential approach from respondents and understand the reasons for this – that different stations may be affected in different ways by a policy on licence duration. Indeed, it was this which led us to examine a differential approach in the Consultation.
- 3.109 However, we do not believe that a fair and consistent approach to setting licence duration, which balances appropriately the factors we have identified as important, can be based on any of the criteria suggested.
- 3.110 For instance, the approach proposed by RadioCentre and Lincs FM – whereby licence length is based on whether an operator has previously taken advantage of a twelve year renewal – would have several drawbacks.
- 3.111 We have highlighted that flexibility remains an important factor in our considerations, allowing future changes to secure the optimal use of the spectrum for the benefit of consumers and citizens. We have suggested that this flexibility is particularly important in relation to stations that will continue on analogue frequencies after any digital switchover. We consider that potential changes (such as a major re-planning exercise) would be best facilitated by having shorter licences, whereas under the approach proposed by RadioCentre and Lincs FM those stations would be afforded a twelve year licence.
- 3.112 Furthermore, RadioCentre's modification of our suggestion – that stations unable to continue to offer a DAB service because there is no longer a multiplex available should also be re-advertised for twelve years – shows that even an apparently fixed criterion is likely to need to be adapted to circumstances.
- 3.113 We highlighted some difficulties with this approach in the Consultation, which we believe remain relevant even in light of respondents' comments. We note RadioCentre's point, in relation to new entrants, that all potential applicants would be aware of the duration of a licence prior to applying. We agree that this would be the case. However, applicants would nevertheless be competing for a licence which would have had its duration determined by the actions of a previous operator.
- 3.114 We disagree with RadioCentre's argument that such an approach would not unduly take back benefits that stations had acquired by opting for a renewal in the first place. Stations would not have known that taking the uncontested renewal would mean that they would be offered a shorter licence upon re-advertisement than if they had not taken such a renewal.
- 3.115 We also envisage problems with the approach suggested by UKRD – whereby licence length is based on the potential for securing DAB carriage in the future.
- 3.116 The purpose of our policy on licence length is not to 'coerce' stations into providing DAB – that remains a commercial choice for operators. Rather, we seek to minimise

any distortions to the incentives operators have to remain on the platform once they have taken the decision to provide such a service.

- 3.117 Furthermore, as set out in the Digital Radio Action Plan, the transition and radio switchover plan (set to be published in 2013) will include criteria which will be applied to determine which stations switch over³⁰. Ofcom does not seek in its policy on licence length to make a judgement about which stations should have a presence on DAB and which should not.
- 3.118 Again, such an approach would also see those stations remaining on analogue being licensed for a long period of time. We have highlighted that the flexibility point applies predominantly to such stations, as other stations are likely to have their licences terminated in any digital switchover.
- 3.119 Both Town and Country Broadcasting and one other respondent suggested a differential approach based on size – whereby licences with a lower MCA would be afforded a longer duration than larger licences. We do not feel that size is an appropriate criterion on which to differentiate, due to the particularly diverse nature of the local commercial radio market.
- 3.120 For instance, some larger licences may have a greater potential audience, but might operate in a particularly competitive local market and have a higher cost base. Similarly, there are some licences that, although covering a small population, are relatively unchallenged in their local market and benefit from favourable demographics to make them particularly profitable.
- 3.121 Consequently, such an approach could lead to particularly attractive licences being advertised for a very long period, and stations that would face significant competition and high initial costs only given a five year licence period.
- 3.122 Furthermore, the changes introduced by the 2010 Act have allowed many smaller stations effectively to merge and cut costs significantly, reducing the link between size and viability or profitability. We do not therefore believe that a differential approach based on size would be favourable.

Conclusions

- 3.123 Both our analysis and that of respondents suggests that the benefits of a common end date are unlikely to outweigh the disadvantages. As such, we will not adopt this approach.
- 3.124 We also do not believe that the differential approach is favourable. As outlined above, we cannot identify a criterion which can be consistently applied and deliver the desired outcome. The diversity of the radio market means that adopting a significantly different approach between sets of stations is likely to treat some stations unfairly. Moreover, all the suggestions we received proposed particularly long licences for stations likely to remain on analogue spectrum after any digital switchover. This would be likely to restrict the flexibility available to Ofcom to fulfil our spectrum management duties, or for Government to introduce a new regulatory regime.
- 3.125 This leaves a choice between the maximum twelve year duration and a shorter length, including the seven year option that we proposed in the Consultation.

³⁰ Task 1.14 of the Digital Radio Action Plan

- 3.126 We note that there is strong industry support for twelve years, given the greater certainty this would provide to operators. We appreciate the points about viability that have been made to us, including points around expenditure, funding and investment. As we stated in the Consultation, we consider it important to offer potential licensees the opportunity to make a reasonable return on their investments, to ensure that operators are prepared to apply for licences and can maintain provision of a service. For this reason, we believe it would be appropriate to give licensees greater certainty than they are currently afforded by our five year policy.
- 3.127 We have not, however, been presented with any evidence that suggests that our proposed seven year duration does not give sufficient opportunity for a reasonable return on investment. Additionally, there are other factors in play, and it is appropriate to take these into account as licence durations shorter than twelve years are unlikely to prevent operators from earning a reasonable return on their investment and providing a high quality service for listeners.
- 3.128 As set out above, we believe that flexibility remains an important consideration even taking into account the provisions of the 2010 Act. There remains a great deal of uncertainty around the future direction of the sector. Some stations are likely to continue on FM following a digital switchover, and it is important that Ofcom retains the ability to make changes to secure the optimal use of this spectrum in the future and maximise benefits to citizens and consumers. Major exercises (such as re-planning remaining licences in order to make the most efficient use of the FM band) would be more appropriately and effectively carried out following the expiry of licences rather than partway through licence periods, and so would be facilitated by having licences that were shorter than twelve years.
- 3.129 Such flexibility would also be useful if Government decided to introduce a new regulatory regime for those stations remaining on analogue frequencies, allowing high quality services to flourish and serve listeners' needs effectively. Having a shorter licence period is likely to increase Government and Parliament's flexibility to introduce a new regime, to the extent that the regime may include provisions that it would be difficult or undesirable to introduce partway through a licence period.
- 3.130 Respondents have suggested that we overestimated the incentives of stations to cease to provide a DAB service. Although we accept some of these arguments, we still believe that a significant difference between the length of new renewals and the duration of a re-advertised licence would distort incentives to continue to offer DAB services, given the additional years of revenue that would be on offer. Stations would of course be mindful of the risk of not being successful in a contested re-advertisement. But this may be a risk worth taking for some operators if they believed that the licence would be uncontested in any award process or that as an incumbent they would be highly likely to win any such contest. Stations which opted for re-advertisement rather than renewal because of the longer licence length on offer might cease to provide a DAB service, which could reduce consumer choice.
- 3.131 We appreciate the concerns of respondents, and have considered their arguments carefully. However, the factors in favour of a shorter licence length – incentives in the case of stations providing a DAB service and flexibility in the case of stations who are likely to continue on analogue frequencies – coupled with our view that seven years is a sufficient period in which to earn a reasonable return on an investment, lead us to conclude that the shorter period is more appropriate at this time.

Decision

- 3.132 Local commercial radio licences which are re-awarded will be granted for a period of seven years.

- 3.133 We would expect to review this policy should the Secretary of State nominate a date for digital switchover, or in the event of other significant radio policy developments.

Postponement of re-advertisements

- 3.134 A number of licence re-advertisements have been postponed due to our consultation. We are publishing an updated re-advertisement timetable with this statement³¹ which takes account of our new policy.

³¹ See <http://licensing.ofcom.org.uk/radio-broadcast-licensing/analogue-radio/apply-for-licence/re-advertisement/timetable/>

Annex 1

Statutory framework

Ofcom's general duties

- A1.1 Any decision about the policy which Ofcom should adopt on the re-advertisement of local analogue commercial radio licences needs to be based on consideration of Ofcom's statutory duties and responsibilities.
- A1.2 Ofcom has general duties set out in the 2003 Act.
- A1.3 Our principal general duty is set out in section 3 of the 2003 Act. It is to further the interests of citizens in relation to communications matters; and to further the interests of consumers in relevant markets, where appropriate by promoting competition.
- A1.4 To meet this duty Ofcom is required to secure, among other things:
- the optimal use for wireless telegraphy of the electro-magnetic spectrum;
 - the availability throughout the UK of a wide range of television and radio services which (taken as a whole) are both of high quality and calculated to appeal to a variety of tastes and interests; and
 - the maintenance of a sufficient plurality of providers of different television and radio services.
- A1.5 In performing the duty Ofcom must have regard to:
- the principles under which regulatory activities should be transparent, accountable, proportionate, consistent and targeted only at cases in which action is needed; and
 - any other principles appearing to Ofcom to represent the best regulatory practice.

Ofcom's specific duties and functions: local analogue radio

- A1.6 Under section 85 of the 1990 Act, one of Ofcom's functions is the licensing of national, local and community analogue radio stations.
- A1.7 Section 85 requires Ofcom, in performing those functions, to secure the provision of a range and diversity of local analogue services.

Advertisement and renewal of local analogue radio licences

- A1.8 The statutory framework for the advertisement and renewal of local analogue commercial radio licences is set out in Part III of the 1990 Act, which has been modified by the 2010 Act.

Advertisement

- A1.9 Where Ofcom proposes to grant a local analogue licence it must publish a notice inviting applications as set out in section 104 of the 1990 Act.

- A1.10 Where a local analogue licence is due to expire we may instead publish a notice under section 104B of the 1990 Act stating that we propose to grant a further licence and inviting declarations of intent to apply. If we receive a declaration of intent from a person other than the licence holder we must publish a notice inviting applications under section 104. If we receive a declaration of intent from the licence holder and no other person we must invite the licence holder to apply for the licence.
- A1.11 A licence to provide a local analogue service must be for a period of no more than twelve years (section 86 of the 1990 Act).

Renewals

Twelve year renewal

- A1.12 Before 8 April 2010, a local analogue licence³² could be renewed on one occasion for a period of twelve years if the applicant nominated a local digital sound programme service provided or to be provided by him and a relevant local radio multiplex service.
- A1.13 After the coming into force of section 32 of the 2010 Act on 8 April 2010, a local analogue licence which was granted before 8 April 2010 may be renewed under section 104A of the 1990 Act on one occasion for a period of twelve years if the applicant nominates a local digital sound programme service provided or to be provided by him and a relevant local multiplex service. A local analogue licence granted on or after 8 April 2010 may not be renewed under section 104A.
- A1.14 An application for renewal under section 104A may not be made before Ofcom publish a notice inviting applications for a licence to provide a relevant local radio multiplex service or more than 3 years before the licence would otherwise expire, and may not be made less than 3 months before the date Ofcom would need to publish a notice if we were to grant a fresh licence to provide the service.

Renewal of up to seven years

- A1.15 Following the coming into force of section 32 of the 2010 Act, a local analogue licence³³ which has been renewed for twelve years under section 104A or which is granted on or after 8 April 2010 may be renewed under section 104AA of the 1990 Act on one occasion for a period of not more than seven years.
- A1.16 The applicant must nominate a local digital sound programme service provided or to be provided by him and a relevant local multiplex service. Alternatively, under new section 104AB of the 1990 Act, in the case of a licence approved by Ofcom (an 'approved licence')³⁴, an applicant may make a 'national nomination', i.e. he may nominate a national digital sound programme service provided or to be provided by him and a national radio multiplex service.
- A1.17 An application for renewal may not be made more than 3 years before the licence would otherwise expire, and may not be made less than 3 months before the date Ofcom would need to publish a notice if we were to grant a fresh licence to provide the service.

³² Renewals are also available for national licences but are not discussed in this document.

³³ Renewals are also available for national licences but are not discussed in this document.

³⁴ The current list of approved licences is set out in

<http://www.ofcom.org.uk/consult/condocs/radio/statement/Addendum.pdf>

Extension and renewal of pre-transfer local analogue licences

- A1.18 Under section 253 of the 2003 Act, a person who holds a pre-transfer local licence (i.e. one which was granted before the radio transfer date³⁵ and which has not been modified under section 253 or renewed at any time on or after that date) is entitled to apply to Ofcom for a 4 year extension of the licence.
- A1.19 An application may not be made more than 3 years before the licence would otherwise expire, or less than 3 months before the date we would need to publish a notice if we were to grant a fresh licence to provide the service.
- A1.20 A pre-transfer local licence (including one for a period extended under section 253 of the 2003 Act) may not be renewed under section 104A of the 1990 Act if it has already been renewed under this section before the radio transfer date. Otherwise the renewal provisions described above apply.

Termination of local analogue licences

- A1.21 Section 86 of the 1990 Act provides that Ofcom may vary the period for which a licence is to continue in force only if the licence holder consents. However this does not affect the operation of the following provisions which have been inserted into the 1990 Act by the 2010 Act.

Digital switchover

- A1.22 The Secretary of State may give notice to Ofcom under new section 97A of the 1990 Act, nominating the date for digital switchover for the post-commencement services specified in the notice. A 'post-commencement service' is a local, national or additional service that is provided under a licence that was granted on or after 8 April 2010 or which has been renewed under section 103B (national licences) or section 104AA (renewal of local licences for up to seven years). The Secretary of State may nominate different dates for different services and may withdraw a nomination.
- A1.23 After a date for digital switchover has been nominated, section 97B provides that if the licence to provide the post-commencement service expires after the date for digital switchover, Ofcom must vary the licence so that it expires on or before that date. However Ofcom may not shorten the licence period so that it ends less than 2 years after the date on which it gives notice of the variation unless the licence holder consents. If the licence expires on or before the date for digital switchover, Ofcom may not vary it so that it expires after that date.

Variation of licence period following renewal

- A1.24 If the Secretary of State has not nominated a date for digital switchover of a relevant renewed service or has withdrawn the nomination, he may give notice to Ofcom under new section 105A of the 1990 Act fixing a termination date in relation to that service. A 'relevant renewed service' is a national service provided under a licence which has been renewed under section 103B or a local service provided under a licence that has been renewed under section 104AA (renewal of local licences for up to seven years). Different dates may be fixed for different services but the termination date may not be before 31 December 2015.

³⁵The date on which the Radio Authority's functions under Part III of the 1990 Act were transferred under the 2003 Act to Ofcom, i.e. 29 December 2003

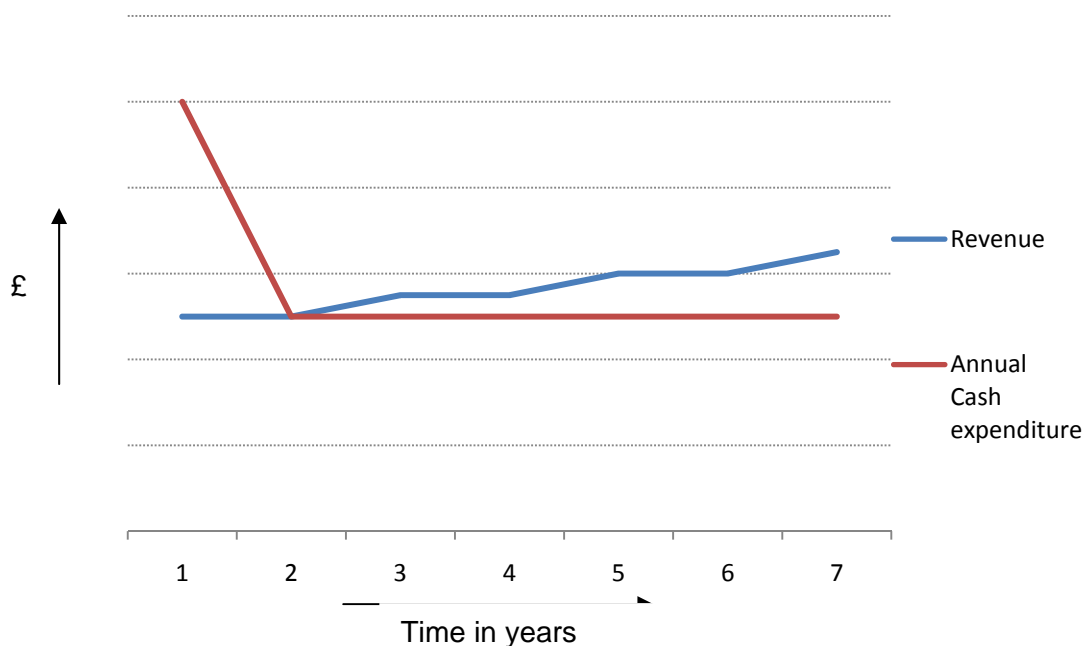
- A1.25 If the licence to provide a relevant renewed service expires after the termination date fixed for the service, Ofcom must vary the licence so that it ends on or before that date. However Ofcom may not shorten the licence period so that it ends less than 2 years after the date on which they give notice of the variation unless the licence holder consents. If the licence expires on or before the termination date, Ofcom may not vary it so that it expires after that date.
- A1.26 The Secretary of State must consider, before 31 December 2013, whether to exercise the powers in section 105A.

Annex 2

Commercial Issues

Introduction

- A2.1 The length of time for which a local analogue licence is granted has implications for the commercial viability of the broadcasting radio station.
- A2.2 A radio station is said to be economically viable if the revenues received over the licence period are more than the costs incurred over that period.
- A2.3 If the radio broadcaster is a new entrant, the revenues may increase over time as the station establishes a listener base and reputation.
- A2.4 Conversely the costs a radio station incurs may be higher in the early years as one-off capital purchases are required and initial start-up activities need to be carried out.
- A2.5 Below is an illustrative graph of a typical local analogue radio station which shows the annual cash expenditure and revenues of a radio station against the number of years it has been broadcasting.



- A2.6 This annex will focus on the following three points
- Capital investment: some of the initial capital equipment a radio station requires will last for several years. Normally the costs of this equipment should be recovered over the equipment's useful life. However if the licence period is shorter than the useful life then the costs of the assets will need to be recovered over the shorter period of the licence thus requiring higher revenues to break even in this period.

- Business contracts: in order to broadcast, a radio station will need premises, a transmission system, and various other activities carried out. The radio broadcaster may choose to contract with third parties to provide these services. The third party suppliers may offer lower annual fees in exchange for commitments to longer contract periods. However the contracts a radio station signs cannot exceed the licence period.
- Initial start up activities: a radio station commencing operations will perform a number of activities in the first years that once established it will not have to repeat. For example it will incur marketing costs establishing the brand and listener base. A longer licence period will allow these initial costs to be recovered over a longer period during which more revenue may be generated. This could reduce the risk of the venture because it will enable radio stations to have a longer period over which they can recover these initial costs.

Typical local analogue commercial station

A2.7 There is a wide range of local analogue commercial radio stations. The financial return these stations typically receive varies considerably. Some return sustained financial profit, whilst some continue broadcasting despite incurring financial losses.

A2.8 The broad range of these stations can be seen in the measures shown below:

Measure	Local analogue station (no DAB coverage)
Measured coverage area (MCA)	Up to 350,000 people
Annual revenues	Up to £2 million
Annual profits/losses	ranging from +£350,000 profit to - £200,000 loss
Number of Staff	ranging from 7 to 20 direct staff
Business planning cycle	5 years (taken from licence applications)

Costs spread over time and business contracts

A2.9 Broadcasting activities: Ofcom commissioned a UK radio 'flow of funds' report in May 2009.³⁶ Within this report the costs a 'typical' local radio station would incur was discussed. The table below is a summary table from this report.

Cost Category	Constituent cost	% of Annual accounting costs
Sales and marketing	External commission	1%

³⁶ UK Radio Impact of regulatory relaxations, Ofcom, 5 May 2009, <http://stakeholders.ofcom.org.uk/binaries/consultations/radio/annexes/annex8.pdf>

Cost Category	Constituent cost	% of Annual accounting costs
Transmission	In-house sales costs	15%
	Station marketing costs	6%
	Transmission	12%
Production	Programming	15%
	Commercial production	4%
Rights	Rights	9%
General & Admin	General & Admin costs	37%

- A2.10 The business planning timeframe: The costs a radio station incurs over time should be planned in advance to ensure optimum business efficiency and management. Due to the way costs may be incurred it may be preferable for a radio station to plan certain costs over certain timeframes to ensure the most efficient outcome.

The table below suggests possible planning period for activities a radio station performs

Cost Category	Actual Cost	Planning period	Description
Sales and Marketing	Staff	1-3 years	Staff costs are generally planned annually however being able to offer staff greater job security may attract better talent
	Advertising Equipment	1-3 years	Advertising equipment, for example stands may be purchased that could last over a number of years
Transmission	Annual charge	1 year	Annual transmission fees paid to a transmission provider
	Fixed term contract	>5 years	Annual transmission fees paid to a transmission provider under a long fixed term contract
	Fixed capital cost	>5 years	Transmission equipment such as radio antennas purchased and depreciated over a number of years
Production	Staff	1-3 years	Staff costs are generally planned annually however being able to offer staff greater job security may attract better talent
	Production equipment	1-5 years	Production equipment is generally depreciated over 5 years, however this may last several years longer.
Rights	Rights	1 year	Rights are paid annually with a

Cost Category	Actual Cost	Planning period	Description
General & Administration costs	Staff	1-3 years	fixed and variable element Staff costs are generally planned annually however being able to offer staff greater job security may attract better talent
	Property costs	>5 years	Offices and premises could be leased over long periods of time to seek reduced annual charges
	Office equipment	1-5 years	Office equipment is generally depreciated over 5 years

Initial start up activities

A2.11 A radio station must carry out a number of activities before it can go on-air.

A2.12 Below is an example of some of the one-off activities a radio station needs to complete before it can broadcast

- Purchase radio broadcasting equipment
- Find suitable premises
- Employ broadcasting and office staff
- Purchase transmission equipment or seek a third party to provide this service

A2.13 These activities do not need to be repeated once the radio station is broadcasting (although new equipment etc may be required).

A2.14 Local radio stations obtain revenue from three main sources

- National air time advertising. Local radio stations can carry national advertising. The size of this revenue is related to the reach and listener base of the radio station.
- Local business advertising. Local radio stations can obtain advertising revenue from local businesses. The size of the revenue generated is negotiated by the sales staff, however the bigger the audience and the more established the brand the easier it will be for sales staff to negotiate attractive sales deals.
- Sponsorship. Local businesses could sponsor programmes and radio events in return for specific advertising. Again more established radio stations may find it easier to win these types of deals.

A2.15 As shown above radio stations will have to engage in activities in the early years to ensure they can broadcast. These activities will incur significant costs which will then have to be recovered over the broadcasting period. Additionally radio stations will find it more difficult to attract advertising (the main source of revenue) in the early years of broadcasting when the station does not have an established listener base and client list.

Conclusions

- A2.16 The costs a radio station incurs in the early years of broadcasting will be greater than in later years due to the up-front capital investment and set-up activities the radio station needs to carry out.
- A2.17 The revenue a radio station attracts in the early years of broadcasting may be less than in the later years. This is because revenue is linked to the size of the listener base (which could grow over time) and the local business relationships the radio station establishes (which again could grow over time).
- A2.18 Therefore longer licence periods may increase the economic viability of a radio station as it will have more years of potentially increasing annual revenues to recover the initial up-front costs. This assumes the annual revenues in later years are larger than the annual costs, producing a positive contribution to offset the initial up-front expenditure.
- A2.19 The rate at which the revenue a local radio station generates increases over time (if at all) is very uncertain.
- A2.20 The business plans radio applicants have submitted for past analogue licences suggest initial up-front capital costs and activities required to broadcast are usually depreciated over 5 years, although in some cases this may be slightly longer. This may indicate that the initial costs of these assets are expected to be recovered by the revenue generated over a 5 year period.
- A2.21 The business plans radio applicants submitted for past analogue licences suggest radio stations generally seem to plan their business operations over 5 years. This may be due to the following factors –
- Broadcasting revenues are very uncertain over periods greater than five years
 - Radio stations generally forecast to break even over a five year period
 - Potential investors generally require a return on their investment within 5 years.
- A2.22 Radio stations may engage in contracts with third party suppliers to carry out activities on their behalf. Signing longer contracts with these suppliers may reduce the annual cost of the contracts.
- A2.23 Licence periods of less than five years may significantly influence the commercial viability of radio broadcasters.
- A2.24 Licence periods greater than five years may give commercial radio stations a better chance of recovering their total expenditure during the licence period depending on the way their business is structured and planned.