



# The Future of Radio

The future of FM and AM services and  
the alignment of analogue and digital regulation

Discussion document

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## Section 1

## Executive Summary

- 1.1 Last year, following consultation, Ofcom published a report called *Radio – Preparing for the future*. That report set out Ofcom's view on the public purposes of radio and a strategic framework for the future regulation of the industry. Alongside these we also published an outline of what we thought a healthy radio market in the UK would look like. We stated our ambition to encourage a market-driven approach aimed at delivering a wide range of innovative UK-wide commercial stations, a wide range and diversity of local and regional commercial services, and community services for every community that wants one, all supported by multimedia services where viable. These services should be provided alongside a strong independent BBC.
- 1.2 Since we published that report, there has been much coverage in the press of the problems faced by commercial radio - from the financial situation of GCap to the first instance of a local commercial radio licence (the one for Stroud) being revoked at the licensee's request.
- 1.3 Some people may argue that these problems are due to cyclical factors and that the industry will recover in the next advertising upturn. But we believe the changes happening in the radio industry may be more structural and may need to be addressed in the interests of listeners.
- 1.4 The radio market is now facing a number of challenges:
  - 1.4.1 ***Competition from other technologies is growing – although localness on radio remains important to many listeners.*** Overall listening hours have been robust; but while listening to national commercial radio stations is up, listening to local commercial radio is down. And across all sectors, the number of young adults who listen to radio is falling as they consume media in new ways, through social networking on the internet or by downloading music and listening to iPods and other similar devices. Nevertheless over half of the population still listens to local commercial radio every week and Ofcom's research for *Radio – Preparing for the future* suggested that people still value the local information that such stations provide.
  - 1.4.2 ***Radio advertising is stalling as advertisers switch to internet advertising.*** Despite overall listening remaining constant, radio advertising growth has stalled both in absolute terms and as a share of all display advertising. We believe this is being driven partly by a process of structural adjustment in favour of new media. Rapid growth in radio advertising revenue up to 2000 has given way to decline in real revenue and static or declining share of the advertising market - commercial radio revenues fell by 7.8% (£44m) year-on-year to Q1 2006. This is against an overall display advertising market that has, in real terms, been declining since Q1 2005. Meanwhile internet advertising has grown rapidly over the last five years. In 2004, internet advertising overtook radio advertising and is forecast to become the third largest advertising sector (behind regional newspapers and TV) in 2007. Forecasts suggest this trend is likely to continue, putting huge pressure on the commercial radio sector – and in particular on local stations – although the radio industry may be able to access some new sources of revenue to offset the loss of spot advertising to some extent.

- 1.4.3 ***Digital radio is taking an increasing share of radio listening putting greater pressure on local analogue stations.*** Listening to radio on digital platforms has been growing. As of June 2006, 16% of all commercial radio listening was via digital platforms: based on current trends, we forecast that this will grow to around 90% in ten years time. Ofcom has specifically allocated more spectrum to DAB to facilitate the provision of more local and national radio choice for every part of the UK. The Digital Radio Development Bureau (DRDB) forecasts that by 2010 half of all households will have DAB; digital radio via television will be ubiquitous by 2012 and broadband internet take-up is growing rapidly allowing people to listen to streamed radio services from all over the world. Satellite radio may also be launched in the UK in the next few years and other platforms may emerge offering yet more choice and bringing more competition. The pattern of local licensing which has been built-up over a number of years may have been sustainable in a steady state world, but as new platforms emerge the financial pressures on smaller stations in particular are growing. While many analogue stations also broadcast digitally, there is more competition for them on digital platforms, and there is a real threat to the survival of those (particularly smaller) stations not carried on digital platforms.
- 1.5 Some people may go on to argue that even if all of this is true and the changes are structural, nothing more need be done. Digital radio listening is growing, new technologies and consumption patterns will supplant FM and AM radio listening - this is driven by consumer choice. There are new opportunities for businesses to engage with consumers; existing players can choose to be part of this new world or to carry on with their existing business models. Market forces will prevail and provide the best outcome for consumers. They will point to the fact that, unlike television, where alternative uses for the analogue spectrum have driven digital switchover, there is no groundswell of demand for FM and AM frequencies to be given up for other things and argue that analogue radio services should be left simply to take their chances under the existing regulations.
- 1.6 However, we believe that there are two main reasons why we might want to consider further action now:
- 1.6.1 ***The regulatory burden on analogue local commercial radio may be unsustainable*** – UK analogue commercial radio was established by Parliament primarily as a local radio system. It would have been possible to use the spectrum differently to provide an alternative policy outcome with a greater number of national services and far fewer local services. The cost to the industry of following the local model arguably has been high, but may have been outweighed by the public benefits it delivered. As competition from other platforms develops, there is a question as to whether this model is sustainable. The regulation of analogue local commercial radio, based around Formats to ensure diversity, localness requirements and ownership rules to ensure plurality was designed for an analogue world. The principles behind these three planks of regulation, as set out by Parliament, and the public purposes of radio may still remain valid today, but the way in which they are implemented may be in need of a radical overhaul if they are still to deliver their aims. The regulation of analogue radio is more restrictive than that of DAB digital radio, which is in turn more restrictive than digital radio on other platforms. If digital listening comes to predominate over the next few years, the current analogue radio regulatory regime may no longer be appropriate or sustainable, and the extent to which local commercial radio should provide the desired public purposes and the way in which we

regulate to achieve these policy goals may need to change in the interests of listeners.

- 1.6.2 ***The flexibility to free-up spectrum*** - The existing analogue (FM and AM) licences are about to start coming up for re-advertisement in a rolling process that will last for many years. Under the current regulatory regime, set out in the legislation, new licences could tie-up the spectrum for up to another 24 years.

New technologies mean that there are other potential uses for the VHF Band II spectrum currently occupied by FM radio (such as mobile TV, more digital radio or data services). FM radio re-uses a limited number of frequencies in a patchwork across the UK to deliver around 300 local BBC and commercial services and five UK-wide networks. Any alternative uses for those frequencies would require large chunks of that spectrum to be freed-up simultaneously – something a rolling re-licensing process does not allow for. We have no immediate plans to switch off FM radio and would not do so without fully considering the impact on consumers, but in the long-term other services may make more efficient use of the spectrum used by existing FM radio services and may provide a better consumer outcome. This could mean an end to the broadcasting on FM of those commercial and BBC services which are also available on digital. On the other hand it may be that even in the long term the best use of VHF Band II spectrum will remain FM radio, perhaps with a different mix of services from today, such as more community services. We simply do not yet know what the best use for this spectrum might be in ten years time, but we need to start thinking now about how to give ourselves future flexibility to do different things when the time is right.

There are also other uses for the Medium Wave spectrum currently occupied by AM radio (in particular for DRM digital radio). For technical reasons, the need for frequencies to be freed-up simultaneously is not so great for Medium Wave and it may be possible to switch-off some AM services and re-use the spectrum for other things earlier than it is for FM services. Again, the costs and benefits would be taken into account before a decision was taken.

- 1.7 In addition, Ofcom has a statutory duty to carry out a review of the new community radio sector next year. This review will cover the licensing, funding and ownership rules surrounding community radio, but it will also cover the relationship between small commercial services and community services, with the aim of ensuring the best outcome for listeners.
- 1.8 In April this year we began a series of debates about the future of radio regulation with key stakeholders in the industry – the large and small radio groups, the Radiocentre, the CMA and individual community stations. We have been analysing the market and developing our own ideas and some further ideas have come out of those debates with stakeholders, but before we produce any proposals for consultation, we want to widen the debate to include those whose voices have not yet been heard.

## What we would like from you

- 1.9 This report does not set out any proposals on what changes should be made and we are not looking for your detailed thoughts at this stage about potential changes.

- 1.10 But we have identified areas that we think might be considered for changes. In particular, we believe that it may be appropriate to look at the role of Formats and localness provisions in analogue local commercial radio, the radio ownership rules, the rules around community radio and the options for achieving flexibility in the future to use the spectrum currently used for analogue radio in different ways.
- 1.11 So we would like to know whether you agree with Ofcom that the issues faced by the broadcast radio industry, either those set out in this discussion document or others that you may wish to raise, warrant further consideration and the development of proposals to ensure that listeners' interests are protected over the coming years.
- 1.12 If it is decided, following full consideration of any responses received to this discussion document, that some further action is required, we will then aim to develop a range of proposals for consultation, some of which we may be able to implement under the current legislation, but some of which may have to wait for new legislation.
- 1.13 For the time being, however, we welcome your thoughts on the matters addressed in this document. Details of how to respond are in Annex 1.

## Section 2

# Introduction

- 2.1 Commercial radio in the UK has existed for over 30 years. Over that time it has grown from a handful of stations to over 300 local stations offering a choice of local AM and FM commercial services in almost every part of the UK and three national analogue services. Digital radio has been introduced offering listeners still more choice. The commercial radio industry has had to adapt and evolve to cope with increased competition and changing listener tastes. But while the regulation of radio has also evolved over the years, changes in the media are now happening so quickly that it may be time for a more radical rethink of radio regulation.

## Ofcom's statutory role

- 2.2 Any consideration of Ofcom's role in the regulation of radio in the UK, needs to be based upon Ofcom's statutory duties and responsibilities. Ofcom's principal statutory duty as set out in section 3 of the Communications Act 2003 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. Ofcom is also required to secure (amongst other things):
- 2.2.1 the optimal use for wireless telegraphy of the electro-magnetic spectrum;
  - 2.2.2 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
  - 2.2.3 the maintenance of a sufficient plurality of providers of different television and radio services.
  - 2.2.4 Under section 85 of the Broadcasting Act 1990 Ofcom is required to secure the provision of a diversity of national analogue services (of which one must consist mainly of speech and another must consist wholly or mainly of non-pop music), and a range and diversity of local services.
  - 2.2.5 Ofcom is required (under section 314 of the Communications Act 2003) to ensure that in local analogue radio services programmes consisting of or including local material are included in such services but, in the case of each such service, only if and to the extent (if any) that Ofcom considers appropriate in that case; and where such programmes are included in such a service, what appears to Ofcom to be a suitable proportion of them consists of locally-made programmes.
  - 2.2.6 Ofcom is also responsible for licensing and regulating community radio services.

## Public purposes and a strategic framework

- 2.3 Last year, following consultation, Ofcom published its views on the future of radio in *Radio – Preparing for the future*. That document set out Ofcom's view on the public purposes of radio and its strategic framework for the future regulation of radio.



2.4 Based on its statutory duties, last year Ofcom conducted audience research to consider the question of why we intervene in the radio market. This suggested a number of public purposes for the radio sector as a whole – BBC, commercial and community - which provide reasons for intervening in the radio market.

- Sustaining citizenship and civil society
- Promoting education and learning
- Stimulating creativity and cultural excellence
- Representing the UK, its nations, regions and communities
- Bringing the UK to the world and the world to the UK
- Promoting social gain

2.5 We believe these provide a comprehensive set of public purposes for which intervention may be required. We also believe that plurality in the provision of the services which deliver these identified public purposes is important, and therefore we do not believe it is sufficient to leave the achievement of these aims to the BBC.

2.6 We used these public purposes to develop a strategic framework for the future regulation of radio. This framework has three elements:

- To enhance choice, diversity and innovation for consumers at the UK, national, regional, local and community levels. In the short-term, this means we need to:
  - ensure a wide range of services in the commercial sector and, in particular, the provision of local material, by regulating in the most effective way possible;
  - encourage the development of more choice and competition by licensing new analogue and digital services and encouraging the growth of digital radio; and
  - encourage the growth of a strong commercial sector, capable of extending range and choice and investing in the future.
- To secure citizens' interests through the provision of radio designed to meet public purposes. The public purposes will be met in different ways by different sectors, taking into account:
  - the need to achieve a balance between the public and commercial sectors and clear boundaries between them;
  - the amount of public funding and intervention required to meet the public purposes;
  - the importance of plurality of provision of radio designed to deliver those purposes; and
  - the need to encourage the development of a thriving community radio sector.

- To do this with as little intervention in the market as possible, consistent with meeting our objectives:
  - based, where possible, on the range and quality of services provided to consumers, rather than intervening to determine production methods;
  - in a way that is as consistent as possible across media and across platforms; and
  - adapting regulation to changes in the market and increasing levels of competition.

2.7 Alongside this framework we also published, following consultation, an outline of what we thought a healthy radio market in the UK would look like. Our aim is to encourage a market-driven approach, alongside a strong independent BBC, aimed at delivering the following benefits for consumers:

- A wide range of innovative **UK-wide** commercial stations - providing competition for the BBC, and plurality of provision in all major genres; both UK-wide services, and specific services for the nations.
- A wide range and diversity of **local and regional** commercial services - catering for local tastes and interests, with a particular focus on local news, providing a sense of community and serving local communities, but also providing local programming of more specialist interest.
- Community services for every **community** that wants one - Providing programmes for special interest groups (including ethnic and religious communities), providing a sense of identity in local communities, with community involvement and participation, broadcasting community information and allowing for debate.
- All supported by **multimedia** services where viable - On-demand, downloads, archive, text and graphical information.
- Available **where and when audiences want**, on devices which offer real consumer benefits.

## Steps already taken to implement the strategy

2.8 In order to begin to achieve these goals, Ofcom has already announced:

- The allocation of spectrum to DAB to deliver most of these goals, including a second national radio multiplex to provide more diversity at a national level, and more local radio multiplexes to facilitate local DAB services in every part of the UK. However, we recognised that DAB (or existing FM) will not allow for the delivery of all of these goals, and other technologies (for example, DRM) may be required to deliver them all.
- A move from input to output regulation, allowing more automation, the use of news hubs and some co-location.

2.9 In doing so, we have also taken into account Ofcom's spectrum policies as well as its radio ones.

- 2.10 Ofcom has also awarded licences to 107 community radio stations in the past two years, and has now invited applications for the second round of licensing.
- 2.11 The above strategy has been set and implementation has begun, so why do we need another review of the future of radio so soon?

## Section 3

# The challenges facing the industry

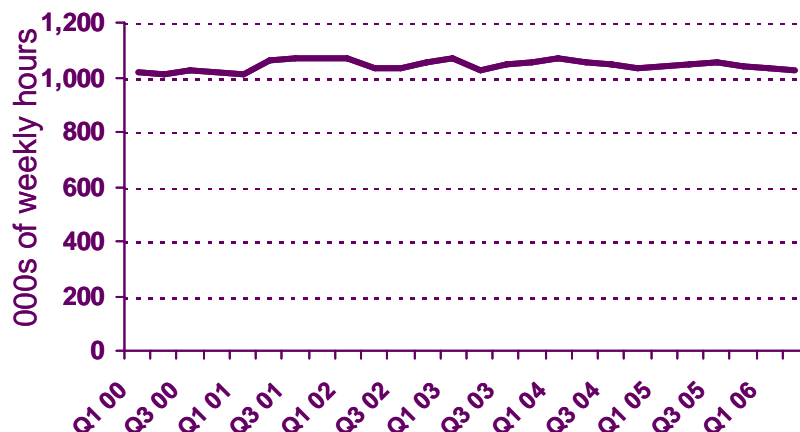
- 3.1 The radio industry today is facing a world where the media, communications and entertainment are changing at a faster rate than at any time in its history. As a result, the industry is having to invest in new technologies and re-invent its role in the 21<sup>st</sup> century.

**The BBC is taking a larger share of radio audiences and advertisers are moving to the internet**

**Overall listening is relatively constant; but there are early signs of a decline particularly among young adults**

- 3.2 Overall radio audience figures have been constant over the past six years (Figure 1). While this disguises significant changes in demographics and sectoral shifts in listening, there is no sign yet that overall radio listening is set to decline. The robustness of radio listening is helped by the nature of radio - much listening is ambient and less easily substitutable for other activities and radio provides the companionship which cannot easily be matched by other media.

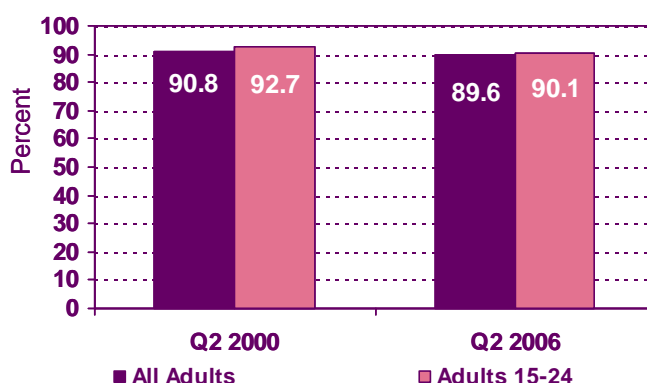
**Figure 1: Total hours of listening to radio 2000-2006**



Source: *Rajar*

- 3.3 Traditionally radio reaches a higher proportion of young adults than the population as a whole, but this difference is beginning to disappear (Figure 2). In addition, 16-24 year olds listen to less radio per week than the population as a whole (18h 18m per week versus 20h 06m). The future of listening by this key group as they get older is difficult to predict.

**Figure 2: Percentage of each group listening to radio each week (15 minute reach)**

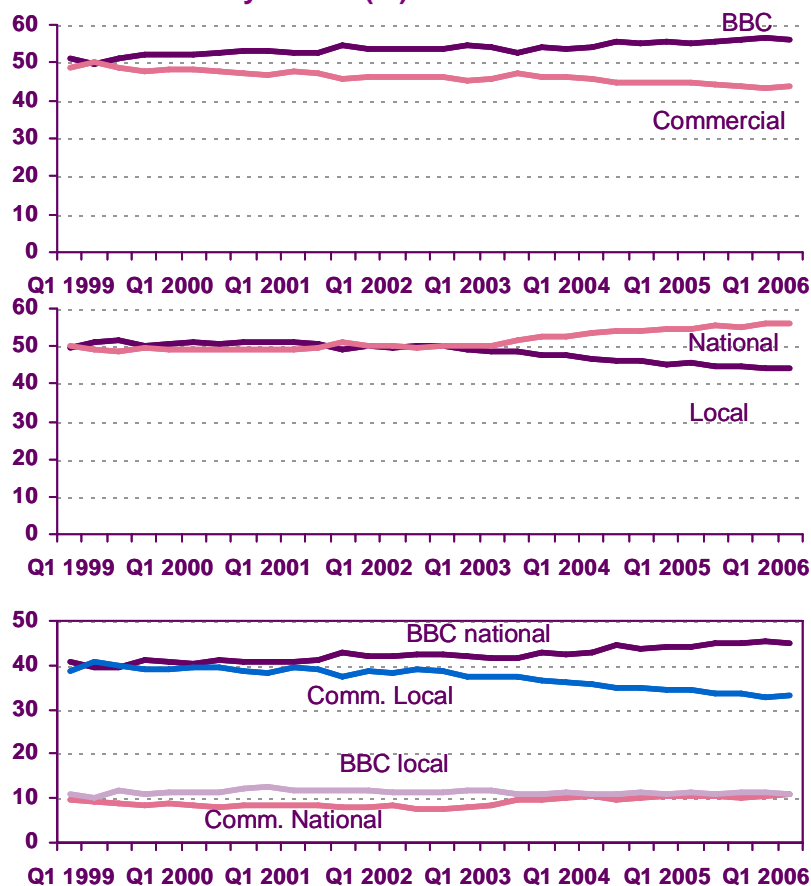


Source: *Rajar*

### Commercial radio has lost audience to the BBC

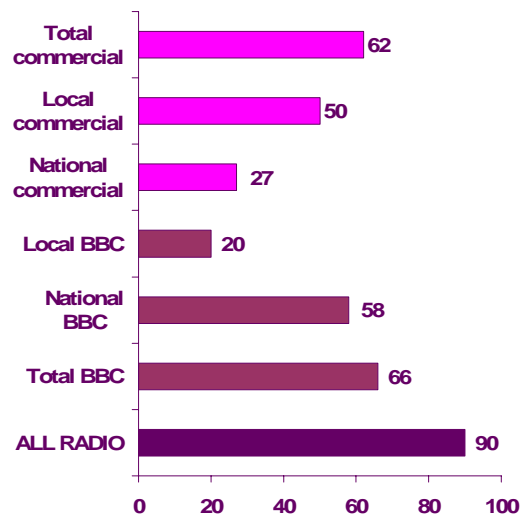
- 3.4 During the late 1990s, commercial radio and the BBC attracted approximately equal shares of listening, although commercial radio tended to have a greater share than the BBC. However, commercial radio has lost share to the BBC over the last seven years. This trend may be plateauing as BBC share has dipped in the last two quarters (Figure 3). As new national digital stations have emerged, the share of national stations has increased. Until 2003 there was approximate parity in the audience shares of local and national radio stations. In only two years, a 10-point gap has emerged. The BBC has been the main beneficiary of this development, but national commercial stations have also recorded share gains since 1999.

**Figure 3: Audience share by sector (%)**



- 3.5 However, although its reach has fallen slightly over the past six years, local commercial radio is still listened-to by over half of the UK population every week (reach was down from 55% in Q2 2000 to 50% by Q2 2006), while the reach of national commercial radio has risen from 23% in Q2 2000 to 27% in Q2 2006, largely as a result of new national digital stations emerging.
- 3.6 The total reach of commercial radio is still almost two-thirds of the UK population, although it has fallen over the same six-year period from 66% to 62% (Figure 4).

**Figure 4: Weekly reach by sector Q2 2006 (% of UK population listening each week)**

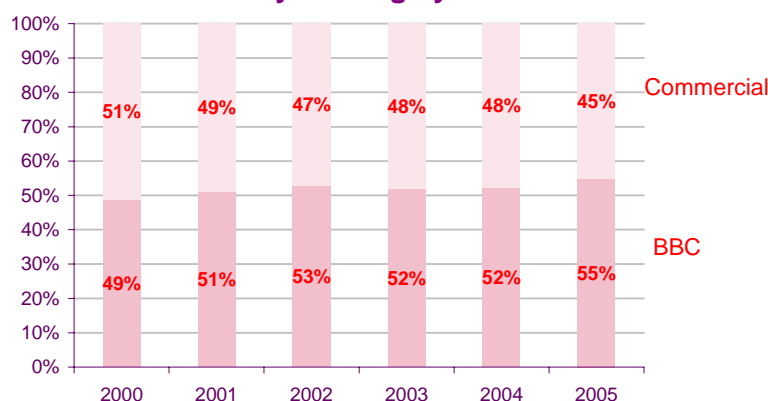


Source: Rajar

### Much of this trend can be explained by an expanding BBC

- 3.7 The BBC invests heavily in radio services and has in recent years launched a number of new national radio services on its digital multiplex. Existing services are also in receipt of significant increases in funding, with expenditure on radio estimated to have risen by £19m in 2005, from approximately £610m to £630m. The scale of the BBC's operations allows for cost savings due to centralisation and economies of scale. Cross media pooled costs (e.g., news gathering) allow BBC radio access to content at a reduced rate compared to stand alone radio companies. In the UK, radio makes up a lower proportion of display advertising than in other countries. This may be due in part to the role played by the BBC.

**Figure 5: Share of total industry funding by sector**

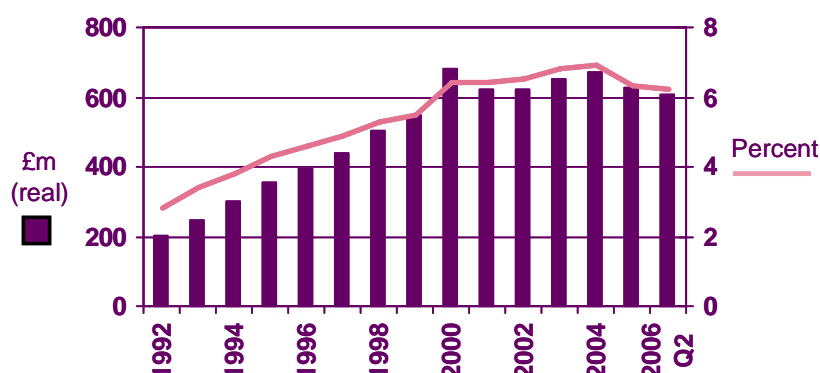


Source: BBC figures are Ofcom estimates; commercial figures from Ofcom licensees

## But while the BBC has invested more in radio, commercial radio advertising growth has stalled

- 3.8 The rapid growth in radio advertising revenues before 2000 has given way to a decline in revenues and a stagnant or declining share of the overall advertising market. This must also be set against the backdrop of an overall display advertising market that has been declining in real terms since Q1 2005. Although larger stations are still making money, even they are under pressure. Commercial radio revenues fell by 7.8% (£44m) overall year-on-year to Q1 2006; local revenues fell by 14%, national revenues by 6.6%. Commercial radio's share of total display advertising fell to 6.2% (its lowest since 2000) (Figure 6).

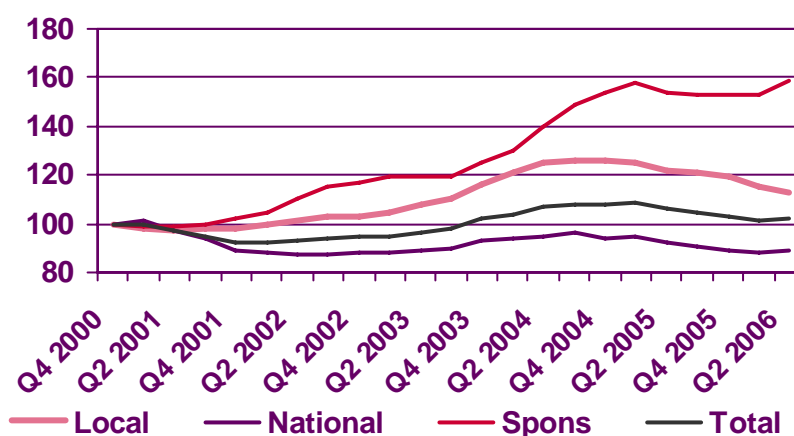
**Figure 6: Radio advertising – amount and share of total advertising market**



Source: RAB

- 3.9 Local stations gain revenues from a mix of national and local advertising and sponsorship. National advertising revenues have performed particularly poorly over the past few years, although recent trends suggest this may be growing again at the expense of local advertising (Figure 7). Anecdotal evidence from advertising agencies suggests that national advertisers are re-allocating their advertising spend from regional campaigns to national targeted niches. Sponsorship growth may be being fuelled by firms' desire to move away from spot advertising, which technology allows them to do via different platforms.

**Figure 7: Radio revenue by type**

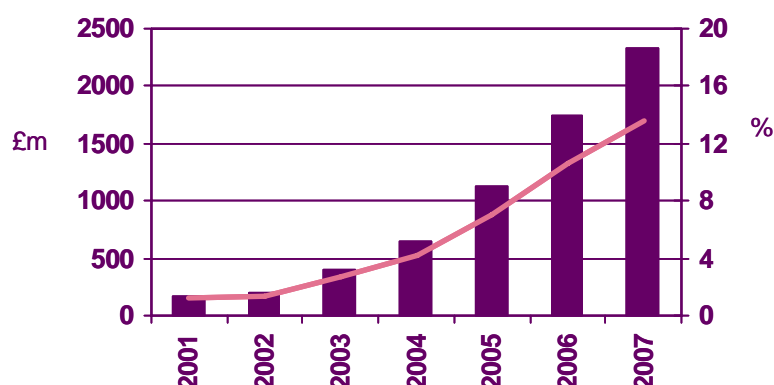


Source: RAB / Ofcom licensees

## There appears to be a process of structural adjustment in advertising in favour of the internet

- 3.10 While radio advertising has been declining, internet advertising has grown rapidly over the last five years and is forecast to continue to grow at a similar rate (Figure 8). In 2004, internet advertising overtook radio and is forecast to become the third largest advertising sector, behind regional newspapers and TV, in 2007.

**Figure 8: Internet advertising – amount and share of display advertising**



Source: Advertising Association

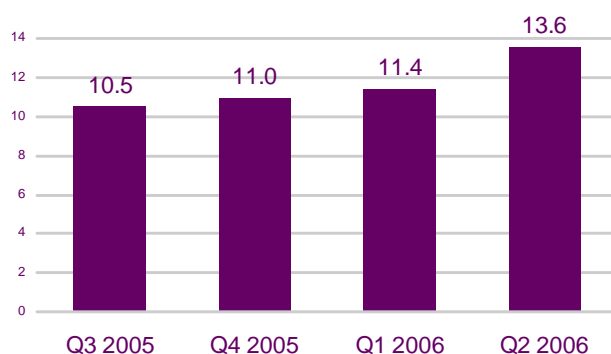
- 3.11 As far as radio is concerned, these trends may be cyclical to some extent and there may be more that radio can do to win new revenues, such as a move from spot advertising to sponsorship or the increased use of music downloads, but a straw poll of advertising agencies suggests they have little optimism that commercial radio can participate in the growing new media sector of marketing investment.
- 3.12 So, while local commercial radio may remain popular, the decline in its attractiveness to advertisers may mean that the current business model for commercial radio – particularly for local stations - may not be sustainable.

## Digital platforms are taking an increasing share of radio listening

- 3.13 After a very slow start, for the reasons we set out in *Radio – Preparing for the future*, listening on digital platforms is increasing in the UK. By Quarter 2 of 2006:
- Digital radio accounted for 13.6% of all listening - up from 6.5% a year earlier (Figure 9)
  - 15.3% of the adult population lived in DAB households - up from 11.1% six months before
  - 38.9% had listened via TV; 21.5% did so at least once a week
  - 22.8% had listened via the Internet; 2.5% at least once a week
  - 1.9 m (14.8% of mp3 owners) listened to radio programme “podcasts”.



**Figure 9: Percentage of radio listening via digital platforms (DAB, digital TV, the internet)**



Source: *Rajar*

- 3.14 Within the overall constant level of radio listening over the past six years, digital platforms are taking an increasing share (Figure 10).

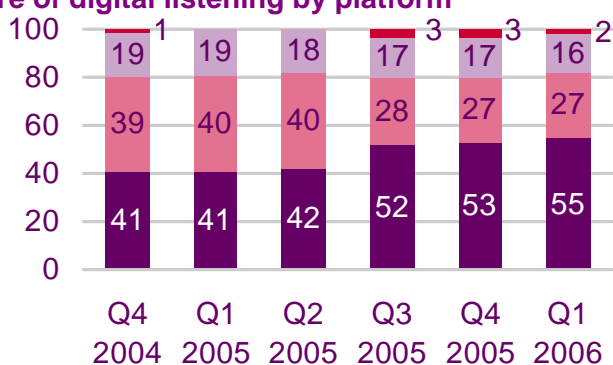
**Figure 10: Total radio listening by platform**



Source: *Rajar*

- 3.15 Although DAB penetration is currently lower than other platforms offering digital radio (digital TV and the internet), DAB's share of digital radio listening continues to grow. This may be due to the fact that DAB is the only digital platform which currently offers the same degree of portability and mobility as is offered by analogue radio (Figure 11).

**Figure 11: Share of digital listening by platform**



Source: *Rajar*

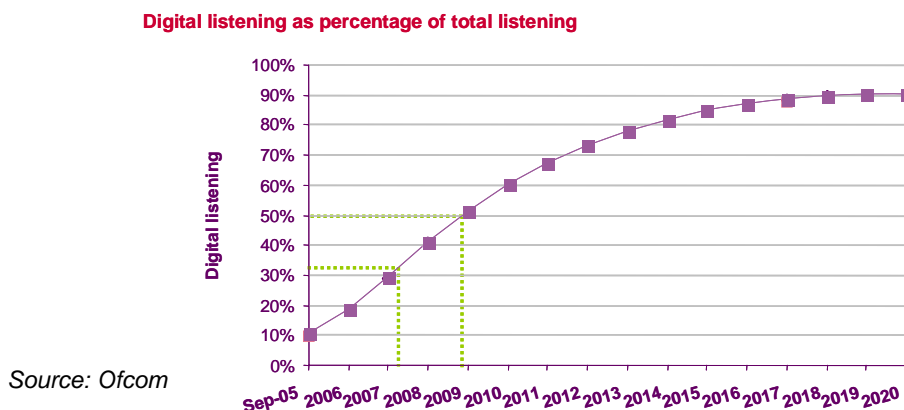
Legend: ■ DAB ■ DTV ■ Internet ■ Non-attributed

- 3.16 The Radio Advertising Bureau (RAB) platform listening survey showed that as of June 2006, 16% of all commercial radio listening was via digital platforms. This represents growth of 46% compared to November 2005.

### DAB forecast take-up

- 3.17 By 2010, the Digital Radio Development Bureau predicts that DAB household penetration will have increased to 50%.
- 3.18 Despite the increasing competition from other forms of audio entertainment, independent forecasts for Ofcom suggest that digital listening will predominate within a few years.
- 3.19 Digital listening across all digital platforms (DAB, TV, internet) currently accounts for 13.6% of all radio listening, and is growing at around 8 percentage points per year (Figure 12). If this rate of growth continues, this could see:
- 33% of all radio listening being digital by around 2008
  - 50% of all radio listening being digital by around 2010

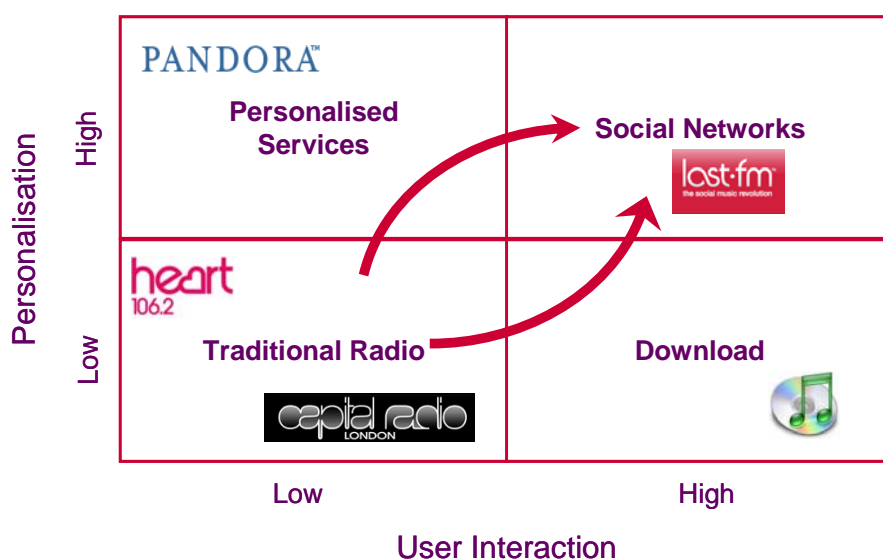
**Figure 12: Projected growth in digital listening**



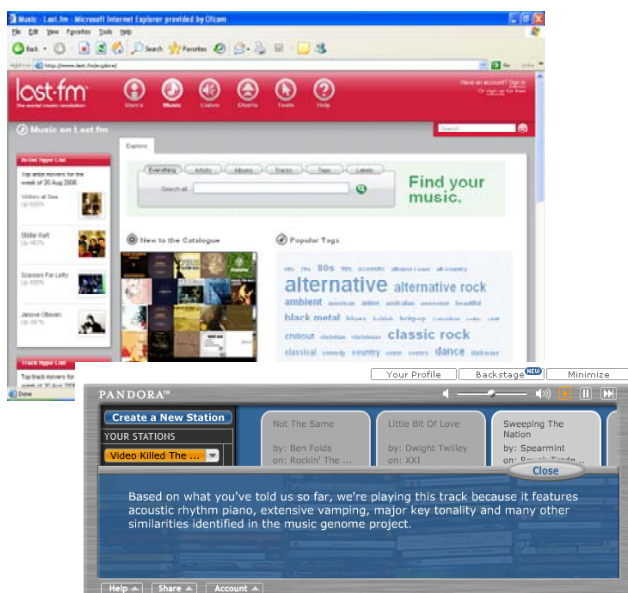
### A shift in the business model opens-up new opportunities

- 3.20 As well as a shift to digital listening, the traditional broadcast market is beginning to be complemented by new ways of listening to audio content. New entrant services are offering listeners the ability to create their own radio stations, download their own content, or to communicate and share content with friends or other members of social networks. New mobile devices with enhanced storage capacity and connectivity compared with previous generations of devices are making it far easier to access on demand music or speech content. Over time, increasing penetration of 3G and fixed and wireless broadband will create new opportunities for audio content distribution.

**Figure 13: A move towards personalisation and interactivity**

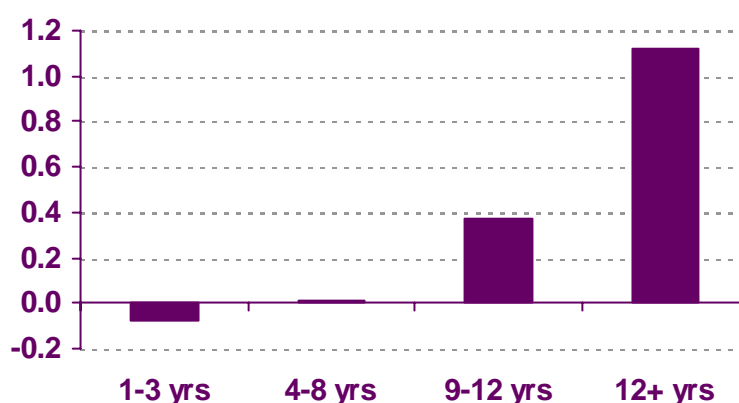


- 3.21 In addition to audio services, the internet has brought many new ways for people to find information and debate local issues, and over time will perhaps reduce the significance of broadcast radio in delivering local content.
- 3.22 For the current broadcast radio industry, these trends offer opportunities to develop enhanced services building on established brands and audience relationships, but they also suggest that traditional analogue broadcast business models may come under pressure and that some of the public purposes which previously only local analogue broadcast radio could meet may now be able to be secured in other ways.



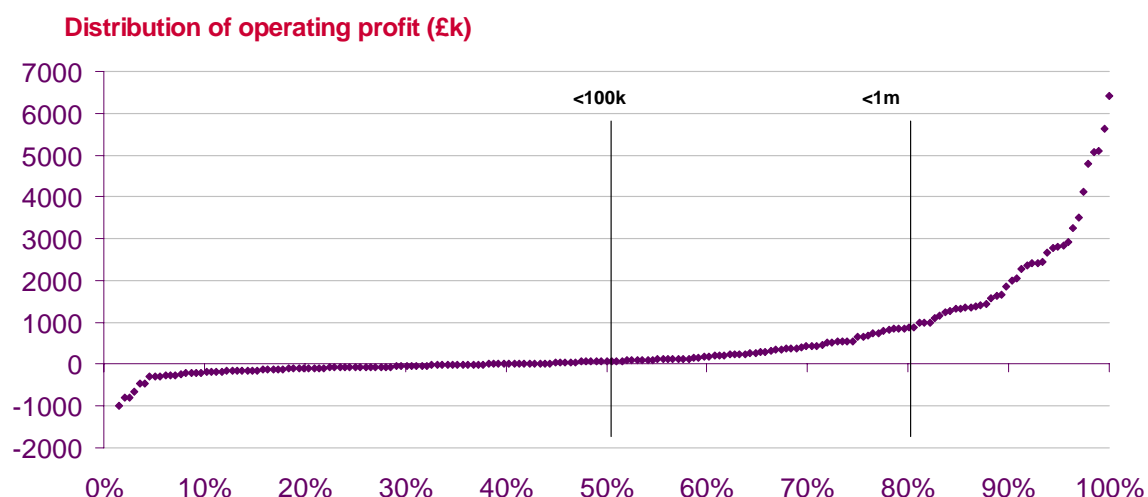
**As competition increases, the existing pattern and number of analogue stations may not be sustainable**

- 3.23 It can take a number of years for a radio station to become profitable – and some stations have yet to become so. (Figure 14)

**Figure 14: Average profits by age of local commercial station (£m per annum)**

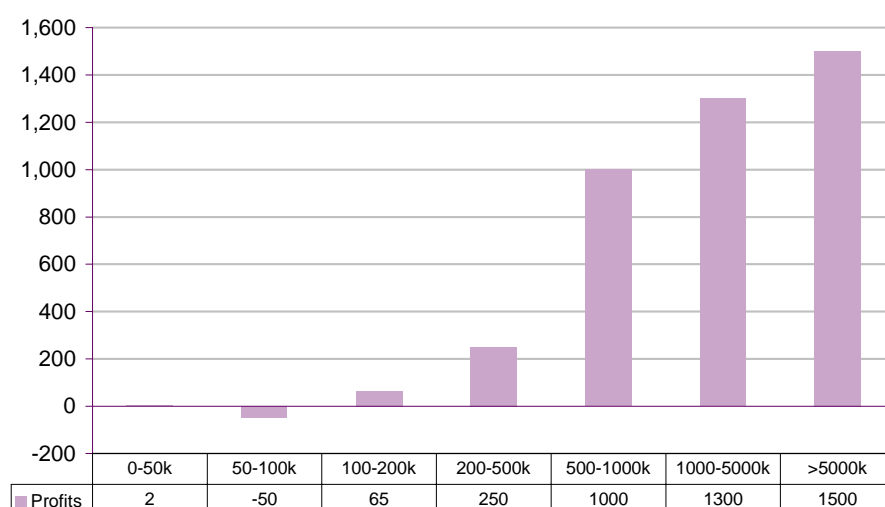
Source: Ofcom licensees

- 3.24 Even many profitable stations make only limited returns. 50% of licence-holding companies either lose money or make less than £100k per annum – about 40% lose money (Figure 15). Most of the figures which make up the chart are based on returns before the last two quarters of advertising slowdown and so the latest picture is likely to be worse than this.

**Figure 15: The distribution of operating profit at local commercial stations**

Source: Ofcom licensees

- 3.25 Profits are concentrated in the hands of larger stations, which are predominantly owned by major groups (Figure 16).
- 3.26 Analysis of analogue station revenues shows that all sectors of the radio industry have seen revenues decline in the past year (Figure 17). While this hits all stations, the effect on the smaller stations, many of which are already loss-making is particularly hard. Indeed one of the smallest commercial licences, for Stroud, has already been handed back to Ofcom by its former holder, although conclusions about the whole small radio sector should not be drawn from the experience of one station, where other factors may have been involved.

**Figure 16: Profits by size of local commercial station (based on population coverage)**

Source: Ofcom licensees

3.27 However, the five-year trends show a more positive picture and most of the decline has come in the past year. While it is not possible to say how much of this decline is cyclical and how much structural, the evidence of a structural shift in favour of the internet is beginning to become apparent.

**Figure 17: Change in breakdown of airtime revenues by size of local commercial station – 2005-06**

Change 2005-2006 %	0-50K	50-100k	100-200k	200-500k	500-1000k	1000-5000k	5000k+	Total
Local	-5%	-2%	-3%	-5%	-11%	-5%	-22%	-8%
National	-5%	12%	9%	-13%	-11%	-5%	-8%	-7%
Sponsorship	-3%	15%	3%	-5%	-8%	-2%	2%	-2%
Total	-5%	4%	0%	-8%	-11%	-4%	-8%	-6%

Source: Ofcom licensees

3.28 Over the past six years, local commercial radio's share of total radio audiences has declined from 38.7% to 32.6%. If these trends continue at the current rate, local commercial radio's share by 2016 could be down to 22.2%. The impact of this on local commercial radio revenues could be significant.

### **Traditionally, radio stations have been seen as vulnerable to downturns as a largely fixed cost business**

3.29 Estimates suggest that radio businesses face a fixed cost base of around 70% of total costs, allowing little scope for rationalisation and thus a high degree of exposure to changes in revenue (Figure 18). This pattern is true across the wide range of differently-sized stations. The percentage of fixed costs is similar across the range of commercial radio, from the smallest stations to the largest.

**Figure 18: Typical breakdown of costs for a radio station**

	% of total costs	Comment
<b>Variable</b>		
Sales commission	13%	Commissions paid to both internal staff and external agencies. Variable with revenue.
Royalties	15%	Variable with sales
Other direct costs	2%	Includes costs of commercial production and sponsorship
<b>“Fixed”</b>		
Staff (non-programming)	25%	Tends to be high sales-staff churn, especially among smaller stations
Marketing	5%	This may be very low at small stations, but can be significant at larger and new licences
Transmission	5%	Fixed, usually 12 year contracts
Programming	20%	Many presenters are employed on a freelance basis allowing stations to flex costs. Also includes costs of jingles, licences, prizes, etc
Premises	10%	Principally rent and rates for the studio and office space
Admin	5%	General office and other office costs

Source: Ofcom estimates

However, some elements of the revenue base may be more variable than traditionally assumed. For example, staffing costs may contain some flexibility due to high churn and automation may offer scope to reduce presenter costs. Taken together this flexibility could create potential to adjust to a structural downturn in revenues although potentially at the expense of programme quality and hence listening in the long term.

- 3.30 While there may be scope for flexibility across all stations, the flexibility of smaller stations is likely to be much more limited than that for the larger operations, so emphasising the pressure these stations face.

## Section 4

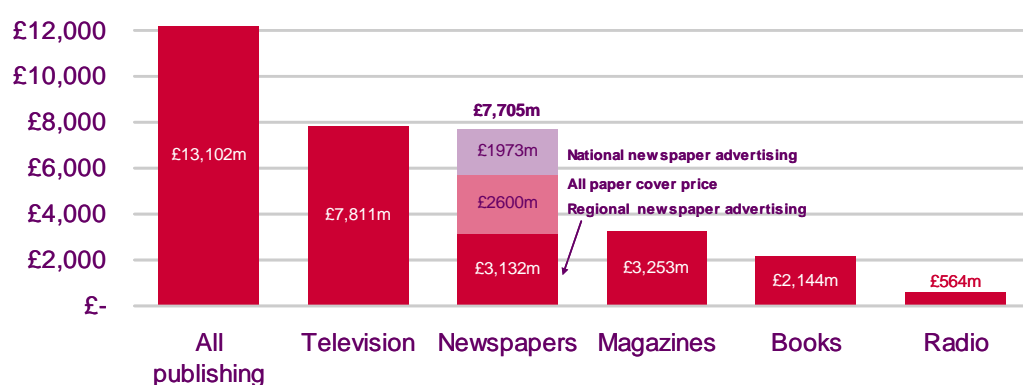
# The regulatory burden

## Radio is a small industry

- 4.1 The commercial radio industry in the UK is small, relative to other media industries. For example, local newspaper advertising revenues are over five times those of the commercial radio industry, while newspaper revenues as a whole are 13 times the size of radio's. Similarly commercial television revenues are 14 times the size of radio's (Figure 19).

**Figure 19: Relative size of different media industries**

Market revenue in 2004 (£m)



Source: Advertising Association, operator returns

- 4.2 This picture is not so dramatic in other countries. For example, in the United States, commercial radio revenues are £16 billion, while television's are £75 billion – a ratio of less than 5 to 1. The comparatively small (in revenue terms) size of the commercial radio industry in the UK compared to television is likely to be due in large part to the significant presence of the BBC in the radio market in the UK.

## Public policy intervention in the UK radio market is substantial

- 4.3 Intervention in the UK radio market is significant. The BBC, which accounts for over half of all radio audiences and almost half of all revenues (via its share of the licence fee) is by some margin the largest intervention.
- 4.4 In establishing commercial radio in the 1970s, Parliament decided, for public policy reasons, that it should primarily be comprised of local rather than national services.
- 4.5 While there are three national commercial licences, the primary policy of developing local analogue commercial radio has continued over the past 30 years and was strengthened by Parliament in the Communications Act 2003, which gave Ofcom a duty to secure an appropriate amount of localness in commercial radio. Each local station is required to provide a service which caters for local tastes and interests and is distinct from the output of other local commercial radio services. This requirement is enforced by including details of the programme service in the station's licence (a 'Format'). This policy represents a major intervention in the market. The three

national commercial analogue stations are also tied to specific formats (two of which are, in broad terms, mandated by Parliament), designed to increase choice.

- 4.6 Each sub-sector of the radio industry – national, local, community, analogue, digital – has its own set of regulations, which are considered below.

## Formats

### Analogue local commercial radio

- 4.7 Every analogue local commercial radio licence, from that held by the smallest station (serving fewer than 2,000 people) to that held by the largest (serving over 7 million), includes a Format which sets out the type of programming the station is required to provide. This is how Ofcom ensures that the character of the station is maintained during the licence period, and is the main way in which Ofcom meets its duty to secure *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*
- 4.8 The Format not only sets out the type of programming that the station will broadcast – the type of music, the amount of speech, the number of news bulletins, etc – but also specifies the amount of local material and the amount of locally produced programming the station must provide. Formats have been simplified in recent years, but are still one page long, and generally include some quite detailed requirements (Figure 20).
- 4.9 The Format is written by the licensee itself (as part of its application for the licence) and is an important part of the station's licence, as it forms the basis of Ofcom's content regulation designed to secure certain outcomes (as opposed to the Broadcasting Code, which all stations must adhere to and which is designed to prevent certain outcomes).
- 4.10 A licensee may request a change to its Format, but in order for Ofcom to consider whether to allow the change, the licensee's request must meet at least one of four statutory criteria. These are that:
- 4.10.1 the change would not substantially alter the character of the service (if it would Ofcom must formally consult on the change)
  - 4.10.2 the change would not lead to a narrowing of the range of programmes available
  - 4.10.3 the change would be conducive to the maintenance of fair and effective competition
  - 4.10.4 that there is evidence of significant demand or support for the change
- 4.11 If the request meets at least one of these criteria, Ofcom will decide whether to allow the request. Ofcom consulted on its procedures for considering Format changes in *Radio – Preparing for the future*.



Figure 20: Example analogue local commercial Format

Format Outline Form OfW 307

STRAY FM	
<b>Format Outline</b>	
<b>Station Name</b>	Stray FM
<b>Licence Area</b>	Harrogate area (as defined in licence advertisement)
<b>Frequency</b>	97.2 MHz
<b>Hours of Broadcast</b>	24 hours a day (locally made for at least 14 hours weekdays, 12 hrs Sat, 12 hrs Sundays)
<b>Definitions</b>	
<b>Speech</b>	excludes advertising, trails, sponsor credits and the like and will be calculated over the period specified.
<b>Music</b>	percentages are calculated as a percentage of the total tracks broadcast in the specified period.
<b>Peak time(s)</b>	refers to weekday breakfast and afternoon drive output, and weekend late breakfast.
<b>Daytime</b>	is 0600 to 1900 weekdays and 0800 to 1400 weekends.
<b>Locally made</b>	refers to output produced and presented from within the licence area and must include peak time.
<b>Character of Service</b>	
<b>A TUNEFUL MUSIC-LED STATION FOR 25-54 YEAR-OLDS IN HARROGATE AND THE SURROUNDING AREA, HIGHLY FOCUSSED ON LOCAL NEWS AND ISSUES.</b>	
<b>Detail</b>	
<p>Local current affairs coverage is an important ingredient in the station, which is the voice of Harrogate, Boroughbridge, Knaresborough, Ripon and Wetherby. It will include features about local leisure and sporting activity as well as local politics, education and social issues for the area. Speech will not drop below 20% of daytime output.</p> <p>Bulletins with local news will be broadcast at least hourly during daytime, including at least one extended bulletin of at least 15 mins. duration each weekday. (This requirement may alternatively be met by airing a magazine-style programme combining music and news-based speech over a longer period of up to one hour, provided that overall speech minutage remains the same). National news should also feature at other times.</p> <p>The music will be quality popular songs from the last four decades with no decade dominating the output. During non daytime specialist shows will feature genres of music which complement the main music mix for at least 14 hours a week. A networked overnight programme may be aired within local hours between 0100-0600 daily, provided this has live presentation throughout and localised idents/jingles etc. This must originate from a station within the TLRC group.</p>	

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## DAB digital radio

- 4.12 Every multiplex licence contains details of the stations the licensee is required to provide. Each station detailed within the multiplex licence has its own Format. In contrast with analogue licences, a DAB station Format is much simpler, consisting only of a short description specifying the character of service (Figure 21)

**Figure 21: Example of a DAB Format**

<b>Chill-out</b> (DSPS provider: GCap Media Digital Ltd)	<b>24 hours</b>
<p>A music service called Chill playing music in a chill-out format – a relaxing, uplifting and varied mix driven by melody and harmony, chosen for its ability to reflect and create a mood rather than for its chart success. Musical influences will include ambient, acoustic songwriters, trance and smooth jazz.</p> <p>Approximately 100% music.</p>	

## Other platforms

- 4.13 Radio services licensed by Ofcom to be carried on digital satellite television (i.e. Sky), cable or digital terrestrial television (i.e. Freeview) have no Format requirements, while radio services on the internet are not regulated in any way.

## Community radio

- 4.14 For community radio services, the method by which Ofcom secures that the proposals made in a licence application are implemented, is by including in each licence a set of 'key commitments'. This is the equivalent of the Format included in every commercial radio licence, but is far more detailed and includes, as well as the nature of the programme service to be provided, details of the licensee's commitments in respect of training and delivering social gain. The detailed nature of these commitments derive from the statutory requirements for community radio, which state that all such services must:
- 4.14.1 Be provided primarily for the good of members of the public or of particular communities and in order to deliver social gain, rather than primarily for commercial reasons or for the financial or other material gain of the individuals providing the service
  - 4.14.2 Be intended primarily to serve one or more communities (whether or not it also serves other members of the public). (A community is defined as either people who live or work or undergo education or training in a particular area or locality, or people who have one or more interests or characteristics in common).
  - 4.14.3 Not be provided in order to make a financial profit, and uses any profit produced wholly and exclusively to secure or improve the future provision of the service or for the delivery of social gain to members of the public or the target community
  - 4.14.4 Offer members of the target community opportunities to participate in the operation and management of the service
  - 4.14.5 Be accountable to the target community.

- 4.15 The statutory criteria to which Ofcom must have regard when making licence award decisions are also more detailed for community radio than for commercial radio, and unlike for commercial radio services, each community radio licensee must produce an annual report demonstrating how it has complied with the characteristics specified in its licence.

## Localness – local material and locally-made programmes

### Analogue local commercial radio

- 4.16 Another element of each station's Format is the amount of localness it is required to provide. Localness consists of two elements: the programme content (local material) and where that content is made.
- 4.17 Many local commercial radio stations recognise that localness is the key to their success. Being relevant to the communities they serve is what differentiates them from national stations. Some of the most successful local stations are those which have the most "local" content in their programming.
- 4.18 However, the financial picture for local radio is not a consistent one across the UK. Some local stations, particularly those in rural areas or where there is less competition, are highly profitable while many other local stations struggle financially.
- 4.19 The Communications Act 2003 gave Ofcom a specific duty for analogue local commercial radio services to "secure that:
- 4.19.1 *programmes consisting of or including local material are included in such services but, in the case of each such service, only if and to the extent (if any) that Ofcom considers appropriate in that case; and*
  - 4.19.2 *where such programmes are included in such a service, what appears to Ofcom to be a suitable proportion of them consists of locally-made programmes"*
- 4.20 "Locally-made" is defined in the legislation as being programmes made wholly or partly at premises in the area or locality for which the service is provided. Ofcom currently carries out this statutory duty via a combination of Formats and also published guidelines which set out the means by which Ofcom believes localness best can be delivered.

### Co-location of local analogue commercial stations

- 4.21 While we believe it is important for local stations to be based in their licensed area wherever possible, in *Radio – Preparing for the future* we said we would allow co-location in exceptional circumstances. In considering such exceptional circumstances, the sort of things Ofcom may take into account are:
- Size of station: there may be stronger case for co-location where at least one of the stations has a licensed area with a population of fewer than 250,000, and especially those under 100,000, although we would not rule out requests from larger stations.
  - Distance and affinity between the areas: there is likely to be a stronger case for co-location where the stations concerned are not too far apart geographically and are able to demonstrate a cultural affinity between the two areas.

- Financial: there may be a stronger case for co-location where stations can demonstrate that co-location is required to ensure the financial viability of the stations concerned.

4.22 However, there may be other factors to be taken into account and Ofcom will treat each co-location request on a case by case basis.

4.23 Co-location has already been allowed in a number of cases for smaller stations – e.g. Bridlington and Scarborough – and in exceptional circumstances for larger stations – e.g. Paisley and a central Scotland regional station.

## **DAB digital radio**

4.24 There are no specific statutory requirements relating to the provision of local material or locally-made programmes on DAB digital radio. One of the criteria to which Ofcom must have regard when awarding a local radio multiplex licence is the extent to which the proposed line-up of services caters for the tastes and interests of people living in the area, but this does not necessarily secure any local programming.

4.25 The majority of local programming currently provided on DAB digital radio derives from simulcasts of stations already on analogue frequencies in the area, although some digital-only stations do provide some local or regional news (or have committed to doing so when the penetration of DAB receivers has reached a specified level).

4.26 If analogue radio were to cease, the radio multiplex operators could request Ofcom's consent to a change in the line-up of their services. Currently Ofcom has no express statutory duty to secure localness on digital radio.

## **Other platforms**

4.27 Some local stations, particularly community stations, broadcast on the internet and some local services are carried on Sky and cable, but there are no localness requirements for radio carried on these platforms.

## **Community radio**

4.28 Much of the essence of community radio concerns localness. Although there are some stations which provide for communities of interest, the way that services are licensed means that these are also limited by geography. However, coverage of community radio services is far from ubiquitous, partly because the sector is a new one, but also because the spectrum for community radio is currently limited.

## **An alternative public policy would have been possible**

4.29 We have noted above that intervention in the UK radio market is significant and in commercial analogue radio results largely from a public policy decision that local radio is important. But it would have been possible to adopt a different public policy goal for commercial radio in the UK.

4.30 In *Radio – Preparing for the future*, we considered two other countries where public policy and regulation is different from the UK: France and the United States. In France, the regulation around localness has been significantly relaxed. In the United States, there is no publicly-funded radio. However, in both of these countries, there is still some significant intervention.

## France

- 4.31 The French equivalent of the BBC, Radio France, offers four national networks (France Inter, France Info, France Culture and France Musique) and 43 local stations (broadcasting under the moniker France Bleu). For many years France had enjoyed commercial radio in the form of stations based in Luxembourg (RTL, 1931) and Monaco (RMC, 1945), as well as the national Europe 1 service (1955), broadcasting from Germany.
- 4.32 Several hundred local commercial radio stations were licensed in the early 1980s. These were later allowed to consolidate into 19 quasi-national or regional networks, offering a range of formats. As in the UK, there is some format regulation (broadcasters need permission from French radio regulator the CSA for major format changes).
- 4.33 Much local radio in France has disappeared as a result of this consolidation, although in addition to the networks there are several independent commercial local stations, 84 of which have formed a trade association called Les Indépendants, in order to attract national advertising. However, many parts of the country have no local radio service other than that provided by Radio France.
- 4.34 Some network stations are required to provide varying degrees of local programming at certain times, depending upon their category of licence (of which there are five different types). Stations relaying entirely national networked output are not allowed access to the local advertising market, while those benefiting from local advertising revenues have to provide at least some local programming.

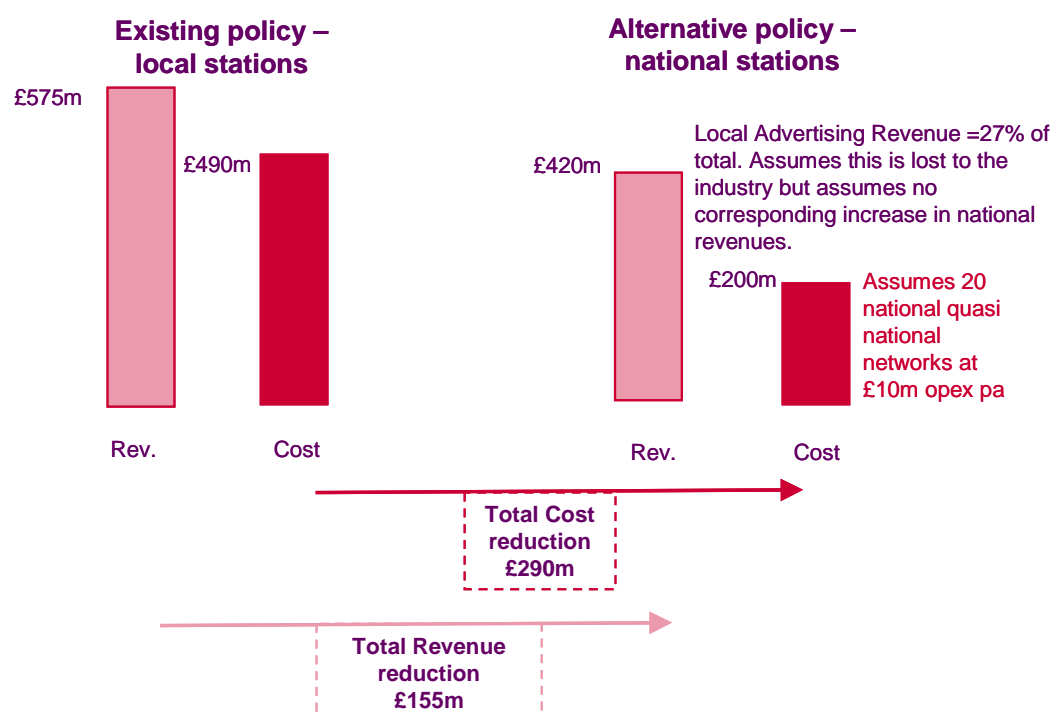
## The USA

- 4.35 In the United States there are no publicly-funded radio services, and there are no national analogue radio services (national radio has only recently arrived in the US, courtesy of the XM Radio and Sirius satellite subscription radio providers). All analogue radio is local although there are syndicated programmes, particularly talk shows. Most radio is commercial, although the National Public Radio (NPR) service offers syndicated programming, including news, documentaries and classical music (including programming from the BBC) to more than 800 independently operated, non-commercial NPR affiliates across the country. Each affiliate carries a mix of national NPR programming and its own local programmes. NPR is funded by donations from the public and business.
- 4.36 As in the UK, the choice available to listeners varies around the country, with those living in the cities having the greatest choice.
- 4.37 There is no format control on stations, which are free to change their format at will. As a result they can respond to changes in demand in the market. So, without the presence of publicly-funded radio, does the US market offer as much choice as the highly-regulated market in the UK?
- 4.38 In general, we found that the market in each city may be able to provide much (but not all) of what we enjoy in the UK, but only if the market is large enough. In practice, due to spectrum limitations in the UK (which are partly due to the UK's geographical proximity to other countries and partly caused by the extent of population density and pattern of settlement in the UK), this would probably mean that in order to provide anything approaching the choice available in New York City, the UK radio market would need to become a national one.

## What could an alternative policy have delivered in the UK?

- 4.39 Rather than opt for a primarily local commercial radio model, albeit with three national stations, a different policy for commercial radio could have been followed in the UK.
- 4.40 There are any number of alternative policies that could have been followed for radio in the UK, with different mixes of local and national services and different sets of obligations, each with its own set of financial and citizen and consumer outcomes. But let us take a highly simplified example. What follows is not presented as a robust analysis of a realistic alternative but rather is intended to make a general point.
- 4.41 In this highly simplified example let us assume that, alongside the BBC, Parliament had decided that the choice of different types of content for the greatest number of people would be maximised by developing a range of national or quasi-national services, rather than local commercial services.
- 4.42 The available FM and AM frequencies would allow for perhaps up to 20 quasi-national networks, few of them with truly national coverage, but concentrating on the major population centres. This is somewhat similar to the French model but without the local programming that regulation in France ensures.
- 4.43 Let us further assume that each of these commercial national or quasi-national stations broadcast its programmes across the UK from a single location with no local material.
- 4.44 The cost of running a national commercial radio station is between £8m and £16m, depending upon the type of content. Let us assume an average cost of around £10m per annum, so the total cost of running all of the UK's commercial radio services, across FM and AM, might be up to £200m per annum. This compares with the current aggregate cost of UK commercial radio of around £490m per annum.
- 4.45 This highly simplified calculation would imply that that the additional costs resulting from the existing public policy in UK commercial radio are perhaps around £290m per annum (or around half of the total revenues of UK commercial radio).
- 4.46 The size of revenues this alternative model would generate is even less certain. At its extreme, the industry may achieve the same level of national advertising revenues as now, but with none of the local advertising revenues which the current system provides. Local advertising currently accounts for 27% of total advertising, representing £155m per annum and this revenue would be lost to the industry.
- 4.47 Again this is a highly simplified assumption, as in reality the presence of many more national or quasi-national stations may result in a higher level of national advertising income than the current model. Also, even without local content, national services could attract local advertising, just as ITV and Channel 4 have done in television, despite having overwhelmingly national schedules. So the impact on total advertising of the alternative policy is also likely to be overstated in this example.
- 4.48 Bearing all of these caveats in mind, this highly simplified example could imply that, taken together, the cost and revenue factors the difference between existing public policy and this alternative approach, in terms of the cost to the radio industry, could be around £135m per annum (i.e. the difference between £290m and £155m) (Figure 22).

**Figure 22: The cost of our UK public policy goals in radio**



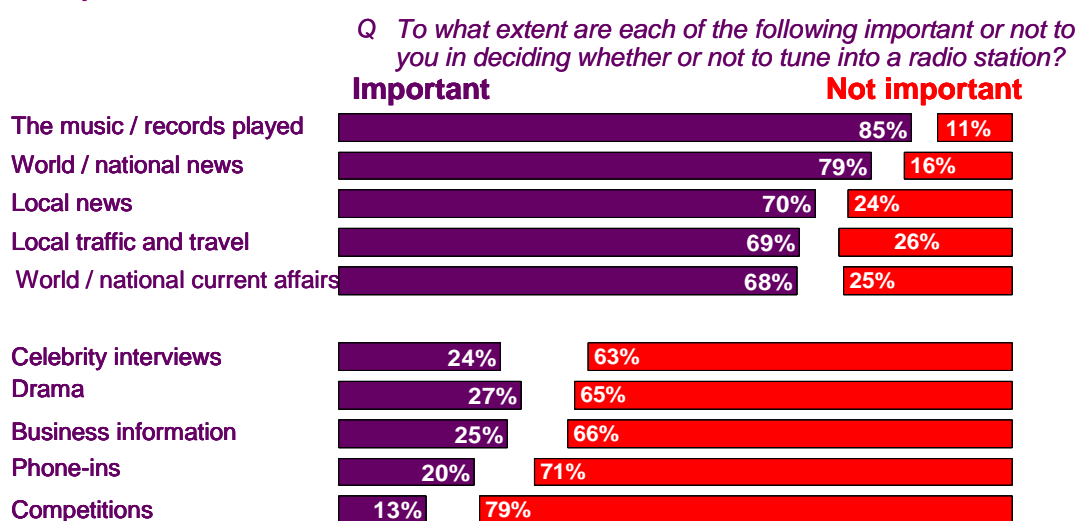
- 4.49 We recognise that this is a highly simplified example and many alternative assumptions could be made to produce different outcomes. The point of the example is simply to demonstrate that other possible policies could have been implemented which could have resulted in a lower cost industry with greater margins, and that the implicit cost to the industry of current public policy we have, is significant relative to the size of the industry.
- 4.50 However, so far this example has only considered the producer side of the equation. One of the main objects of the existing public policy is to deliver the benefits to citizens and consumers of local programming catering to their tastes and interests in every part of the UK. So how important are these benefits?

## The public policy benefits

- 4.51 The public policy we have followed in the UK has ensured that almost every part of the UK has at least one commercial local station, catering for local tastes and interests, providing local news and ensuring a plurality of local voices alongside the BBC. Given that television in the UK has never been local and that even regional commercial television has been in retreat in recent years, local commercial radio has provided the only source of broadcast local news and information as an alternative to the BBC.
- 4.52 In *Radio – Preparing for the future*, we carried out research into what listeners expect from their local station and when they expect it to provide local programming. The research suggested one of the main reasons people listen to radio is for local news, weather and traffic (Figure 23). While the level of listening to local stations has fallen slightly in recent years, there are no signs that local radio will not remain important for many listeners for years to come – although local radio listening is likely gradually to transfer from analogue to digital platforms. While new sources of local news and travel may reduce the need for local radio to be required to deliver such output, the other attributes of local radio, such as providing companionship and a sense of belonging, are unlikely to be met by other media. There is no evidence so

far that some form of local radio will not have an important place in the media landscape of the future.

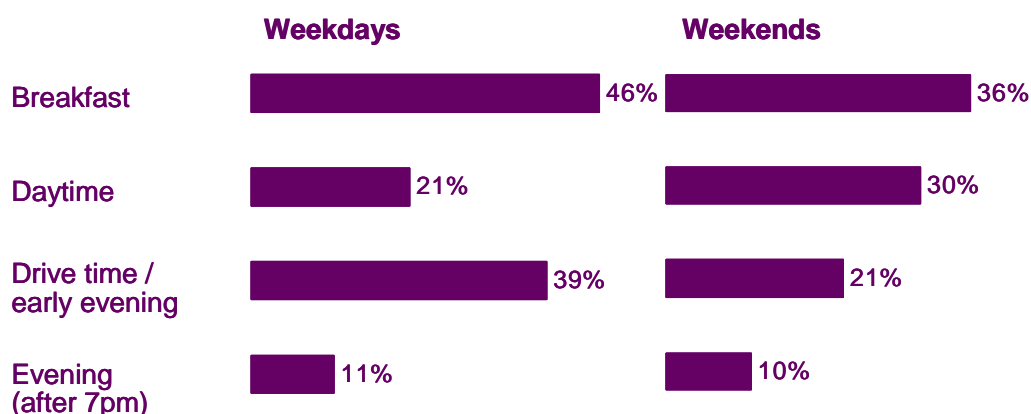
**Figure 23: Important characteristics of radio**



Base: All radio listeners (1,501)

- 4.53 The research also suggested that listeners want local programming at peak times, but that there is less interest at other times (Figure 24).

**Figure 24: At what times of the day is it important to you to be able to listen to local programming?**

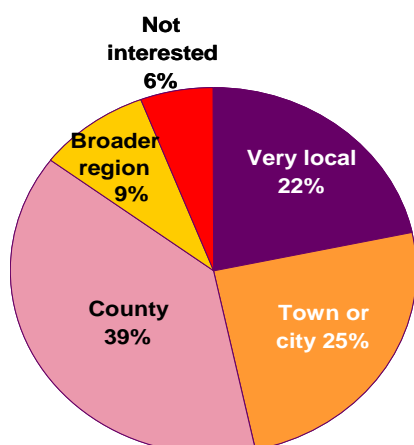


Base: All who listen to local stations (1,146)

- 4.54 This is supported by the fact that although the weekly reach of local commercial radio has fallen in the past five years from 54.4% of the population at the end of 2000, to 50.8% at the end of 2005, half the population still listens to local commercial radio. The evidence suggests that many people will continue to value local radio for the foreseeable future.
- 4.55 The research also asked people what sized area local radio should cover. Responses varied around the country, but 73% indicated a size roughly equivalent to local DAB multiplex areas. 22% wanted smaller stations (Figure 25).



**Figure 25: Which of the following best describes the area you would like your local radio to cover?**



*Source: Ofcom research*

- 4.56 This research suggests that commercial local radio is valued for its localness and that there are significant public benefits to be weighed against the costs to the industry of the public policy followed by the UK over the past 30 years.
- 4.57 A key question which would seem to arise from this brief analysis of the costs and benefits of UK public policy for commercial radio is whether the way that the public policy historically has been implemented, in terms of the licensing process (awarding licences by 'beauty contest' to the applicant judged best able to deliver a service which caters for local tastes and interests and broadens listener choice) and the use of Formats to ensure programming diversity and localness, is still the most appropriate way in which to achieve the public policy goals as listening shifts from analogue to digital radio platforms and community radio becomes established in the UK. Other potential questions which arise include whether the public policy is the right one, and what level of intervention in the market, if any, is required to deliver the required public policy objectives.

## Securing plurality through media ownership rules

- 4.58 A further area for consideration is the mechanisms by which the other main public policy objective for radio, namely plurality, is secured for the benefit of consumers and citizens. Ofcom has recently reported to the Secretary of State following a statutory review of the current media ownership rules. The one area which that report highlighted for potential further work was that of the ownership rules which apply specifically to the holding of commercial radio licences.

## Current rules

- 4.59 Currently, there are four types of rules relating to plurality of radio ownership:
- Cross-media ownership rules: limits on ownership of local radio, local newspapers and regional TV;
  - Local analogue services rules: a limit of 55% of points based on station ownership in any market with more than two commercial stations;
  - Local digital services rules: limits on ownership of individual digital stations in any market, taking into account overlaps between multiplexes;

- Digital radio multiplex rules: limits on:
  - ownership of local radio multiplex licences whose coverage overlaps by more than a certain percentage; and
  - ownership of national radio multiplex licences, where a person may hold only one national radio multiplex licence.
- There is also a public interest test which may be required by the Secretary of State in certain cases of proposed take-overs or mergers.

### **How the current rules work**

- 4.60 The current rules are set out in the Media Ownership (Local Radio and Appointed News Provider) Order 2003. They are based on the principle that there should be at least two owners of local radio stations, plus the BBC, in any market where there are more than two local commercial stations.
- 4.61 The rules exist due to concerns that otherwise all of the access to local news and information in an area could be controlled by a single operator, i.e. they exist for plurality reasons rather than economic competition reasons.
- 4.62 There are currently separate rules for analogue and digital services. Each set of rules is based on individual station markets. However, because almost every station's market is unique, with many overlaps between stations' markets, the calculation of the ownership limits has to be carried out on a case-by-case basis, and is far from transparent.
- 4.63 For radio multiplexes, there are rules preventing control of local radio multiplexes whose coverage overlaps, and to prevent one person from holding more than one national radio multiplex licence.

### **Why are there plurality rules?**

- 4.64 Access to diverse viewpoints is important because it enables democratic participation. Citizens need information on what is happening in their communities to enable participation in the democratic process; i.e. to make informed choices when voting, participate in public discourse, and have a forum to contribute their views, and obtain the information they need for markets to work properly.
- 4.65 It is also important for citizens to have access to a wide range of viewpoints. The more perspectives that citizens have on issues, the more likely they are to have information about the full range of issues, and the more likely they are to be fully informed about each individual issue. It is also important that one viewpoint does not dominate over others. If any one viewpoint has too much influence (for example, if one viewpoint has particular incentives to increase its influence, such as political bodies), that viewpoint can distort the democratic process.
- 4.66 Due to the importance attached to plurality by Parliament, Ofcom was given a duty to maintain a sufficient plurality of providers of different TV and radio services (s.3(2) Communications Act). The media ownership rules act as a proxy for plurality.

## Station ownership rules

- 4.67 These plurality arguments may still be relevant, but a possible question is whether the current rules secure the appropriate degree of plurality. The evidence of the importance of plurality in radio per se is contradictory:
- Local radio is not most people's primary source of local news (regional TV and local newspapers are seen as more important);
  - yet the majority of people say one of the most important things for radio to provide is local news.
- 4.68 Since the current radio ownership rules were implemented in 2003, the range of local news sources available to consumers has increased, particularly as a result of the increasing penetration of broadband. This might suggest that the radio ownership rules should be relaxed.
- 4.69 Furthermore, even if plurality is maintained, there may be a question as to how this is best achieved, and whether separate analogue and digital rules are sensible.

## Multiplex ownership rules

- 4.70 The arguments for the multiplex ownership rules are based on the principle that it is undesirable for one owner to control access to the stations on every multiplex in any given area. The rules are based in part on the percentage of overlap of adjacent multiplexes.
- 4.71 However, while many local multiplexes overlap with each other, these overlaps are generally incidental. It could be argued that the only overlaps that should matter are those where there are two or more multiplexes covering substantially the same area (this only applies to London at present) or where regional multiplexes exist (North West England, North East England, West Midlands, Yorkshire, Severn Estuary/South Wales and Central Scotland) and wholly overlap local multiplexes.
- 4.72 If new technologies, such as Digital Radio Mondiale, are introduced, then the ownership rules may need to be revised, as DRM services may be operated as either single services, or as multiplexes with two or more services.

## Cross-media ownership rules

- 4.73 Two recent Ofcom projects are relevant in this area:
- The radio advertising market project found that local radio and local newspapers are substitutes when it comes to advertising.
  - The review of media ownership project found that plurality of voice in a local area remains important, even though radio itself is not a primary source of news. Taking local newspapers and local radio together under common ownership could unacceptably diminish the range of voices in an area.
- 4.74 This suggests that cross-media ownership rules remain important, but there may be a case for considering local analogue and digital radio services together alongside other media.

## Community radio

- 4.75 For community radio, even though stations are very small-scale (generally limited to a five kilometre coverage radius) as we have seen above, the commitments included in each station's licence are quite detailed.
- 4.76 The Community Radio Order prevents a community radio station from being licensed if it would have a coverage area which overlapped by 50% or more with the measured coverage area of a commercial station which serves 50,000 adults or fewer. Although the Order does allow Ofcom to license a service which would overlap by 50% or more with a commercial service with 50,001 – 150,000 adults in its measured coverage area, the legislation does not allow Ofcom to permit such services to gain any income from advertising or sponsorship of programmes.
- 4.77 In all other cases Ofcom is required by legislation to include conditions in each licence which limit the proportion of income from advertising or sponsorship, and to ensure that a new community radio service does not unduly prejudice the economic viability of any other local commercial service.
- 4.78 Where the sale of spot advertising and sponsorship is allowed, there is an upper limit of 50% (or less, at Ofcom's discretion) on income from these sources taken together.
- 4.79 As far as ownership is concerned, no group is allowed to control more than one station.

## Issues

- 4.80 Given the public policy goals set by Parliament, and that research supports the fact that listeners still value localness on commercial radio, the main question we believe may need to be addressed for local commercial radio is whether the current regulatory tools used to ensure range, diversity, localness and plurality are the most effective ones. This main question could be further sub-divided into a number of subsidiary issues:
  - 4.80.1 If digital listening across a number of platforms comes to predominate, and the requirement for a diversity of different types of programmes is more likely to be met by national services on a number of digital platforms and by DAB local services, it may become increasingly anomalous to require analogue commercial stations to keep to their detailed Formats, which were designed to provide the diversity of programming required by Parliament. At some point, therefore, it may make sense to relax analogue Format regulation, although the timing of any such change would have to be carefully considered.
  - 4.80.2 While Ofcom has a duty to secure an appropriate amount of local material on each local station, and we welcome stations providing local content, to the extent it is serving local audiences, there is a question as to whether current Formats require too much local material to be provided. It could be argued that the statutory selection criteria, two of which focus on programming content, have led applicants to propose more local material in their licence application than either their audience research or financial resources would suggest is sensible, as a way of differentiating themselves from other applicants. The outcome of this process may not necessarily be in the best interests of listeners, who Ofcom's research indicates, may not necessarily value localness for all of the hours that some Formats currently

require. Perhaps Ofcom should simply require a minimum amount of local material from each station to secure public policy goals and let the market decide on provision over and above this minimum.

- 4.80.3 While we have allowed smaller stations to provide their 'locally-made' programming from outside the area they are licensed to serve by permitting co-location with other existing stations, should we extend this to all stations?
  - 4.80.4 The proposed introduction of AIP (Administered Incentive Pricing) to the spectrum occupied by terrestrial broadcasters, which is likely to lead to an increase in costs for stations, also implies that consideration may need to be given to how public policy objectives can continue to be secured in light of these increased costs.
  - 4.80.5 A possible question relating to the regulation of DAB digital radio local multiplexes is whether there should be statutory requirements relating to the provision of local programming (as is currently the case for local analogue commercial radio), or whether any such provision should be left to the market. Ofcom's initial view is that it would seem anomalous to have allocated spectrum specifically to provide local services on DAB in every part of the country but then not to ensure the provision of local programming on that spectrum.
  - 4.80.6 While recognising Parliament's intention in requiring ownership rules for analogue and digital radio stations and for multiplexes to ensure plurality, it may be that those rules could be simplified and aligned across analogue and digital platforms while still securing the required degree of plurality.
- 4.81 A separate but related set of issues relates to community radio. Although community radio is still in its formative stages in the UK, Ofcom has a duty to carry out a statutory review of the sector within two years of the launch of the first community radio service. As part of this review, we plan to consider the effectiveness or otherwise of all of the current statutory rules. In particular we plan to consider whether the characteristics set out in the legislation are too restrictive, and whether they could be simplified without losing the spirit of the legislation.
- 4.82 We would welcome views as to whether these are the right areas for consideration or whether there is anything else Ofcom should be considering.

## Section 5

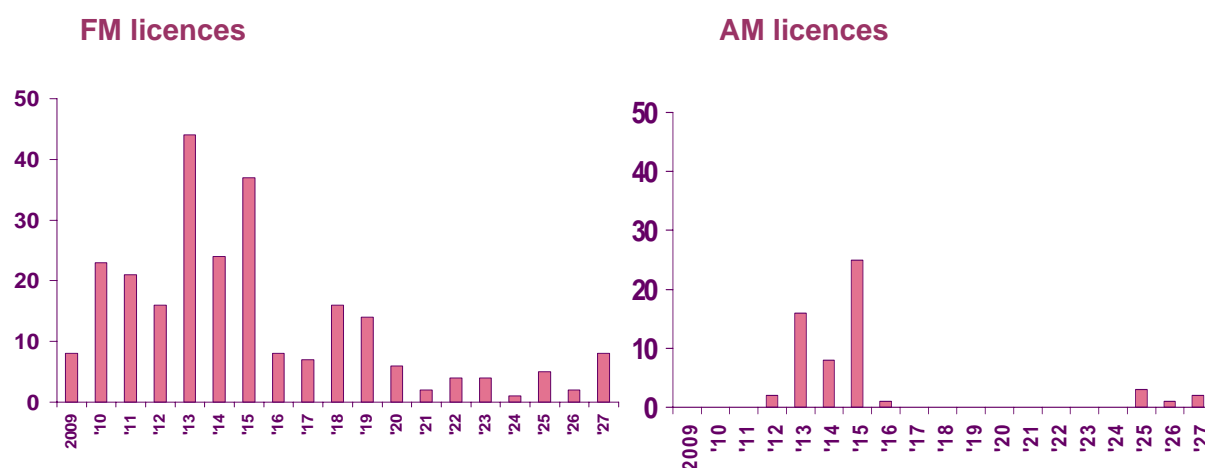
# The flexibility to free-up spectrum

## Analogue radio licences will begin to expire soon

### Analogue commercial local radio

- 5.1 There are currently 307 licensed (or planned) analogue local commercial stations (248 FM licences and 59 AM licences). These cover a variety of population sizes from fewer than 2,000 in places like Ullapool to over 7 million in the case of most London licences. All stations operate under the same regulatory regime.
- 5.2 The programme of licensing new analogue commercial radio stations is almost at an end. Licences have been awarded where there were available frequencies and evidence that potential operators wished to apply for them. They are awarded following a beauty contest which takes into account four criteria, set out in the legislation:
- 5.2.1 The ability of the applicant to maintain the service throughout the licence period
  - 5.2.2 The extent to which the proposed service caters for tastes and interests of people living within the area
  - 5.2.3 The extent to which the proposed service will broaden choice against the other local (non-BBC) service(s) already available in the area
  - 5.2.4 Evidence of local demand and support for the proposed service
- 5.3 Licences are awarded for up to 12 years. However, any licensee which also provides a digital radio service on a local DAB multiplex in the area is entitled to apply, on one occasion only, for a 12-year renewal of its licence.
- 5.4 When a licence expires, the current process is that Ofcom may pre-advertise the licence to test interest from potential bidders. If only the incumbent signals its interest, the licence need not be re-advertised and the incumbent is able to apply for a new 12-year licence under an abbreviated “fast-track” procedure. If other parties are interested, the licence will be advertised and awarded following a full beauty contest according to the criteria above.

**Figure 26: Number of licences expiring by year**



- 5.5 Existing licences are due to expire from 2009 in a process continuing for a number of years. Without any change to the legislation, the process of expiry and re-award could continue indefinitely (Figure 26).

### **Analogue commercial national radio**

- 5.6 There are currently three analogue national services: Classic FM, Virgin Radio and TalkSport. The first of these is broadcast on FM while the other two are broadcast on AM.
- 5.7 The existing licences are currently due to expire in 2011-12. If a new licence award competition is held, the incumbent receives no preferential treatment; the licence is auctioned to the highest bidder, unless there are exceptional circumstances. A new licence would be awarded for a period of up to 12 years.
- 5.8 The legislation requires that one of the licences must be for a service which is mainly speech. A second must be for a service which is “music that is not pop”. There is no statutory format restriction on the third.

### **Community radio**

- 5.9 Community radio licences are awarded for a five-year period. There are no provisions in the legislation for the renewal or re-advertisement of these licences.

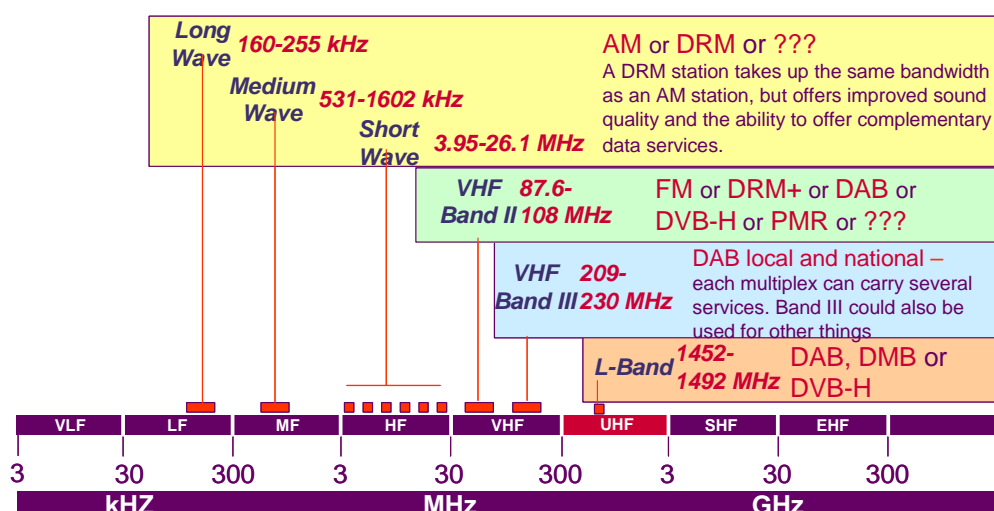
### **Issues**

- 5.10 If it is the case that the vast majority of radio listening will be via digital platforms in ten years time, then before embarking on a rolling re-licensing process for AM and FM commercial radio and tying up the spectrum for many years to come, it is worth considering whether we are making the most effective use of the spectrum in the interests of consumers.

### **New ways of using spectrum**

- 5.11 Broadcast radio services currently occupy a number of wavebands. The VHF Band II spectrum currently used for FM radio and the Medium Wave spectrum currently used for AM radio could be used for other things if no longer required for the existing services (Figure 27).

Figure 27: New ways of using spectrum

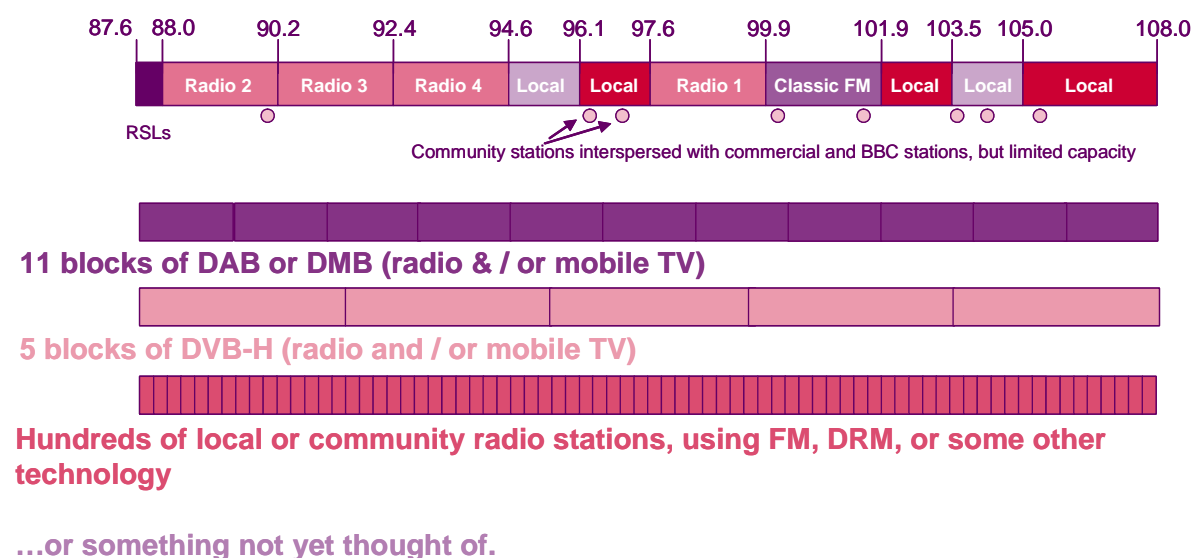


## VHF Band II

- 5.12 The majority of radio listening today remains on FM (VHF Band II), but the picture is changing rapidly. At some point over the next 10-15 years there may come a point where the vast majority of radio listening is via digital platforms and there may be greater value for consumers in using the VHF Band II spectrum for other things, rather than simulcasting the services also available on digital.
- 5.13 Already, the analogue services that account for over 90% of all listening are also carried on DAB. Most of these services are currently “simulcast” on FM, taking up most of the current FM spectrum.
- 5.14 This applies both to the spectrum currently used by analogue commercial radio and to that used by the BBC analogue national networks and local services.
- 5.15 Any change to the use of VHF Band II spectrum would not happen without a full review which considered the costs and benefits to citizens and consumers and took into accounts the needs of the more vulnerable members of society, many of whom rely heavily on radio services. Any review would also consider economic efficiency (the costs and benefits of alternative uses) and the switching costs for operators and consumers.
- 5.16 It is too early yet to say what the best use of the VHF Band II spectrum may be in the future. Indeed it may be that the best use for it remains FM radio, either for all existing services, or for those that have no route to digital, or for a much greater number of community services (for many of which there is currently a lack of spectrum).
- 5.17 But there may be alternative uses, such as more digital radio, perhaps for those stations that currently have no route to digital, or for mobile television, or for data services, or perhaps for something that has not yet been thought of (Figure 28).



**Figure 28: Current VHF Band II use and some possible alternatives**



- 5.18 Even if some capacity were to remain reserved for small-scale commercial and community stations (assuming it is decided that it is appropriate to reserve spectrum for this purpose), most VHF Band II capacity could be released, to allow the market to decide upon its most economically efficient use (which could still be FM radio).
- 5.19 However, it is not necessary to analyse the alternatives now, as these will inevitably change by the time we are in a position to release the spectrum; for now, we simply need to be aware that there are alternatives and to maximise our flexibility for the future. This flexibility also needs to take into account the possibility of slower than expected digital radio take-up.
- 5.20 Many of the possible alternative uses for VHF Band II spectrum require the spectrum to be divided up in different ways from today. For example, a DAB or DMB multiplex requires 1.7 MHz of spectrum. Individual FM stations only take up 0.3 MHz of capacity, so unless many adjacent licences (both spectrally and geographically) expired at the same time, a rolling licence process would make allocation to DAB or DMB impossible, and market mechanisms would be prevented from working efficiently.
- 5.21 Because FM licences are re-advertised as they expire, and this is a rolling process, based on original licensing dates, there will never be a single point in time where all or most of the spectrum becomes available for alternative uses. To allow maximum flexibility for re-use will require the majority of the spectrum to become available at one time.
- 5.22 This implies a change to the re-licensing process so that the end dates of the vast majority of FM licences can be aligned (a review date would also have to be agreed with the BBC).

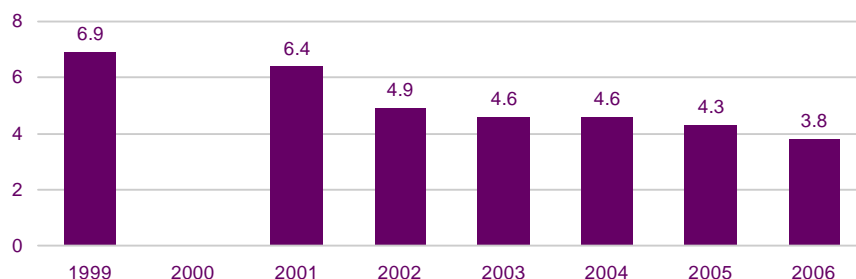
## Issues

- 5.23 Ofcom seeks views on whether we should now seek to ensure flexibility for the future planning of the VHF Band II spectrum, possibly by changing the way that we deal with existing FM licences as they expire. This question will need to be considered as we approach FM re-licensing, both for local and national FM commercial services.

## Medium Wave radio

- 5.24 Medium Wave is currently used for AM radio. Listening to many AM radio stations has declined rapidly in recent years, largely due to poor sound quality, although there are exceptions (Figure 29). The majority of AM stations (including the two INRs) are simulcast in their areas on DAB; more are likely to be simulcast on the new DAB local multiplexes soon to be advertised. Work carried out recently by Ofcom in the context of considering applications for extension from the three national analogue radio licences suggested national AM listening would continue to fall.
- 5.25 The UK has a number of high power frequency allocations, some of which are used for UK-wide stations (1215 kHz - *Virgin Radio*; 1053 & 1089 kHz – *TalkSport*; 693 & 909 kHz- *BBC Radio Five Live*) and some which are currently used for nations and local services (e.g. 882 kHz - *BBC Radio Wales*; 810 kHz - *BBC Radio Scotland*; 1341 kHz - *BBC Radio Ulster*; 1152 kHz - *LBC News*, *Capital Gold (Birmingham)*, *Magic (Manchester and Newcastle)* etc.; 1458 kHz - *Sunrise Radio*, *BBC Asian Net (Birmingham)*, *BBC Radio Newcastle* etc.; 1548 kHz - *Capital Gold (London)*, *Forth 2*, *Magic (Liverpool)* etc.)

**Figure 29: Share of total listening taken by local AM stations 1999-2006 (%)**



Source: RAJAR

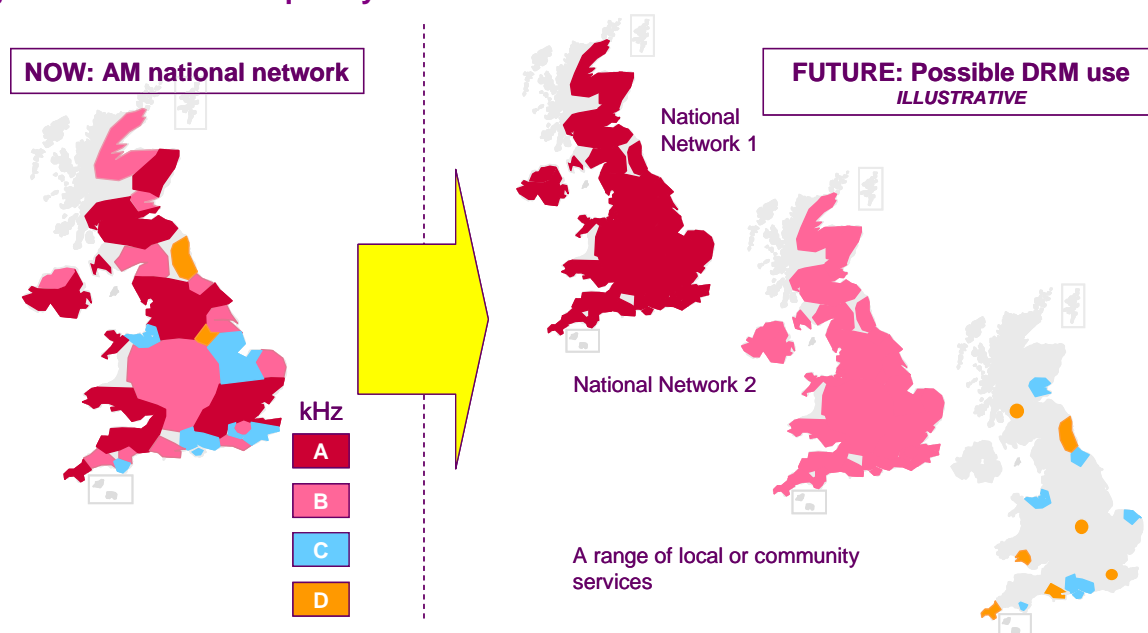
Note: The chart shows listening to these stations on any platform, including DAB, DTV and internet, so overstates actual listening on AM.

- 5.26 Generally, at least two frequencies are required to cover the whole UK on AM, to avoid interference between adjacent transmitters. Often a number of AM filler transmitters on different frequencies (in addition to the high power frequencies) are required to achieve national coverage.
- 5.27 The UK also has a number of frequency assignments offering medium-sized coverage, which are used for BBC and commercial local radio around the UK, and for filler transmitters for the national networks, as well a small number of community services.
- 5.28 There are currently 59 local AM licences.
- 5.29 There are also a few frequencies, which offer small-scale coverage and are used for long-term RSLs and some short-term RSLs.
- 5.30 While all of these frequencies require international clearance, they could be used in a different pattern from the current configuration, i.e. used to cover different areas.

## Other potential uses for Medium Wave: DRM

- 5.31 Although still at an early stage of development, one possible alternative to AM broadcasting is DRM (Digital Radio Mondiale). It offers much improved sound quality over AM on Medium Wave, Long Wave or Short Wave spectrum – many international broadcasters are already taking up the technology.
- 5.32 The technical characteristics of DRM coverage are similar to AM. It would be relatively easy to convert an AM transmitter to DRM. Coverage areas can be anything from a few kilometres radius to half a continent, depending on transmission power and frequency.
- 5.33 However, like AM, DRM on Medium Wave offers less good coverage in cities, particularly in steel-framed buildings.
- 5.34 Medium Wave is generally a cost-effective way to offer coverage to rural and remote areas – ***Therefore DRM could be a complement to DAB, rather than an alternative.***
- 5.35 A single Medium Wave frequency can offer a single good sound-quality DRM service plus data, or two lower sound-quality services.
- 5.36 The frequencies currently used for UK-wide services could instead be used to provide a greater number of DRM UK-wide stations plus a range of local or regional DRM services (Figure 30).

Figure 30: Possible frequency re-use for DRM



- 5.37 DRM could provide a potential digital migration path for those stations which have no other obvious transition route to digital, such as small-scale commercial stations and community stations, and may also provide a means to provide digital radio services to remote areas where DAB may never be viable. The extent to which regulatory intervention should be used to achieve such an outcome is also a matter that may be worth consideration.

## **Other technologies**

- 5.38 Other than AM radio and DRM, we are not currently aware of any other uses for Medium Wave spectrum. However, the advocacy for widespread use of power-line communications could be regarded as mutually exclusive with use for radio-communications in certain frequencies, because of the unintended but significant radiation of radio waves from power line transmission (PLT) systems. To that extent, it is an alternative use of the frequencies.

## **Issues**

- 5.39 As existing AM licences expire, we may wish to consider whether to re-allocate the Medium Wave frequencies they currently occupy for use by other technologies such as DRM. If we do so, we will also need to consider how these services should be licensed, as currently legislation may not easily allow for the licensing of such services.

## Annex 1

# Responding to this discussion document

## How to respond

- A1.1 This document does not represent a formal consultation as it does not include any proposals. However, Ofcom invites written views and comments on the issues raised in this document, to be made **by 5pm on 14<sup>th</sup> December 2006**.
- A1.2 Even though this is not a formal consultation, Ofcom strongly prefers to receive responses using the online web form at [http://www.ofcom.org.uk/consult/condocs/radio\\_future/howtorespond/form](http://www.ofcom.org.uk/consult/condocs/radio_future/howtorespond/form), as this helps us to process the responses quickly and efficiently. We would also be grateful if you could assist us by completing a response (see Annex 3), to indicate whether or not there are confidentiality issues. This response coversheet is incorporated into the online web form questionnaire.
- A1.3 Responses may alternatively be posted or faxed to the address below, marked with the title of the consultation.
- Peter Davies  
Director of Radio & Multimedia  
5th Floor  
Riverside House  
2A Southwark Bridge Road  
London SE1 9HA
- Fax: 020 7981 3806
- A1.4 Note that we do not need a hard copy in addition to an electronic version. Ofcom will acknowledge receipt of responses if they are submitted using the online web form but not otherwise.

## Confidentiality

- A1.5 We believe it is important for everyone interested in an issue to see the views expressed by consultation respondents. We will therefore usually publish all responses on our website, [www.ofcom.org.uk](http://www.ofcom.org.uk), ideally on receipt (when respondents confirm on their response coversheet that this is acceptable).
- A1.6 All comments will be treated as non-confidential unless respondents specify that part or all of the response is confidential and should not be disclosed. Please place any confidential parts of a response in a separate annex so that non-confidential parts may be published along with the respondent's identity.
- A1.7 Ofcom reserves its power to disclose any information it receives where this is required to facilitate the carrying out of its statutory functions.
- A1.8 Please also note that copyright and all other intellectual property in responses will be assumed to be licensed to Ofcom to use in order to meet its legal requirements. Ofcom's approach on intellectual property rights is explained further on its website at <http://www.ofcom.org.uk/about/accoun/disclaimer/>

## Next steps

- A1.9 Following the end of the discussion period, if it is decided to publish a full consultation document, this will be published in the first quarter of 2007.
- A1.10 Please note that you can register to receive free mail Updates alerting you to the publications of relevant Ofcom documents. For more details please see:  
[http://www.ofcom.org.uk/static/subscribe/select\\_list.htm](http://www.ofcom.org.uk/static/subscribe/select_list.htm)

## Annex 2

# Response cover sheet

- A2.1 In the interests of transparency, we will publish all responses to this discussion document in full on our website, [www.ofcom.org.uk](http://www.ofcom.org.uk), unless a respondent specifies that all or part of their response is confidential. We will also refer to the contents of a response in further publications, without disclosing the specific information that you wish to remain confidential.
- A2.2 We have produced a coversheet for responses (see below) and would be very grateful if you could send one with your response (this is incorporated into the online web form if you respond in this way). This will speed up our processing of responses, and help to maintain confidentiality by allowing you to state very clearly what you don't want to be published. We will keep your completed coversheets confidential.
- A2.3 Ofcom would encourage respondents to complete their coversheet in a way that allows Ofcom to publish their responses upon receipt, rather than waiting until the consultation period has ended.
- A2.4 We strongly prefer to receive responses via the online web form which incorporates the coversheet. If you are responding via email, post or fax you can download an electronic copy of this coversheet in Word or RTF format from the 'Consultations' section of our website at [www.ofcom.org.uk/consult/](http://www.ofcom.org.uk/consult/).
- A2.5 Please put any confidential parts of your response in a separate annex to your response, so that they are clearly identified. This can include information such as your personal background and experience. If you want your name, address, other contact details, or job title to remain confidential, please provide them in your coversheet only so that we don't have to edit your response.

## Cover sheet for response to this Ofcom discussion document

### BASIC DETAILS

Discussion title:

To (Ofcom contact):

Name of respondent:

Representing (self or organisation/s):

Address (if not received by email):

### CONFIDENTIALITY

What do you want Ofcom to keep confidential?

Nothing

☐

Name/contact details/job title

☐

Whole response

☐

Organisation

☐

Part of the response

☐

If there is no separate annex, which parts?

### DECLARATION

I confirm that the correspondence supplied with this cover sheet is a formal consultation response. It can be published in full on Ofcom's website, unless otherwise specified on this cover sheet, and I authorise Ofcom to make use of the information in this response to meet its legal requirements. If I have sent my response by email, Ofcom can disregard any standard e-mail text about not disclosing email contents and attachments.

Ofcom seeks to publish responses on receipt. If your response is non-confidential (in whole or in part), and you would prefer us to publish your response only once the consultation has ended, please tick here.

☐

Name

Signed (if hard copy)