

The BBC's trading activities

A consultation on Ofcom's proposed requirements

Consultation

Publication date: 29 March 2017

Closing Date for Responses: 24 May 2017

About this document

The role of the BBC is to produce high quality and distinctive programmes and services which educate, inform and entertain.

As a large, publicly-funded organisation, the BBC inevitably has an impact on competition in the wider media market. It may have a positive effect by stimulating demand or encouraging sector wide innovation. However, in fulfilling its objectives, the BBC may also harm the ability of others to compete effectively.

Under the Charter and Agreement, the core, non-commercial, BBC is allowed to carry out some specific types of commercial activity which arise as a by-product of providing public services.

This document is a consultation on the requirements we intend to place on the BBC to ensure that its trading activities do not harm fair and effective competition.

Contents

Section		Page
1	Introduction	1
2	Legal Framework	3
3	Trading activities requirements	4
Annex		Page
1	Responding to this consultation	10
2	Ofcom's consultation principles	12

Section 1

Introduction

- 1.1 The BBC's role is to act in the public interest and serve all audiences with content which informs, educates and entertains. To do so, it provides impartial news and information, together with high-quality and distinctive output and services. In resetting the BBC's Mission and Public Purposes¹, the Government has confirmed the valuable contribution the BBC makes to the UK and to people's lives. The Government also made clear that it expects the BBC to do more in certain areas in order to justify its unique funding arrangements and privileged status.
- 1.2 As a large publicly-funded organisation, the BBC inevitably has an impact on competition in the wider media market. It may have a positive effect by increasing choice, stimulating demand or encouraging sector wide innovation for example. But in fulfilling its objectives, the BBC may also harm the ability of others to compete effectively.
- 1.3 The BBC is required to carry out its commercial activities through its commercial subsidiaries,² with the exception of "trading activities", which are carried out by, and are ancillary to, the BBC Public Service.³
- 1.4 Under the agreement between the Secretary of State for Culture, Media and Sport, and the BBC (the "**Agreement**"),⁴ the BBC's trading activities are characterised as commercial in nature, but are not to be treated as "commercial activities". In practice, they are not expressly designed to make a profit, but may do so incidentally.
- 1.5 Trading activities encompass transactions between the BBC Public Service and: (i) its commercial subsidiaries; (ii) third parties; and (iii) the general public through direct provision of goods and services e.g. sale of tickets to BBC Public Service events.⁵ Other examples of trading activities include the leasing out of spare studio capacity or licensing the rights to BBC-produced DVDs. A full list of the types of trading activities, as set out in clause 31(2) of the Agreement, is provided at paragraph 3.2.
- 1.6 There is a risk that, without appropriate safeguards, the BBC's public funding could be used in a way which distorts competition in the UK, in the course of carrying out its trading activities.
- 1.7 Competition concerns could arise from the BBC:
 - i) granting its subsidiaries an unfair competitive advantage;

¹ Articles 5 and 6 of the Royal Charter for the continuance of the British Broadcasting Corporation (the "**Charter**"):

https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/577829/57964_CM_93_65_Charter_Accessible.pdf.

² See Section 1 of our guidance on the BBC's commercial activities:

https://www.ofcom.org.uk/__data/assets/pdf_file/0025/99412/bbc-commerical.pdf.

³ We use "BBC Public Service" to mean the public services arm of the BBC Corporation.

⁴https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/584329/57965_Cm_93

⁶⁶ Print 1 .pdf
5 Our proposed requirements do not include any free ancillary services provided by the BBC Public Service such as helplines or information pamphlets.

- ii) unfairly discriminating against or between third parties (either by setting different prices or granting preferential access to services); or
- iii) offering goods and services at below market norms.
- 1.8 Under the Charter and the Agreement, Ofcom must set out how it will regulate the trading activities and the procedures to be followed (including such requirements as Ofcom consider appropriate to protect fair and effective competition).

Consultation

- 1.9 We are consulting on draft requirements that we propose to place on the BBC to ensure that its trading activities do not harm fair and effective competition. Our draft requirements are set out in Section 3 of this document.
- 1.10 We welcome any views and comments which respondents may have on the issues raised in this document, or any other issues related to the regulation of the BBC's trading activities. This consultation closes on 24 May 2017.
- 1.11 Following our review of responses, we plan to issue a statement of requirements and guidance in July 2017.

Commercial activities requirements and guidance

- 1.12 Ofcom has published final requirements and guidance relating to the BBC's commercial activities.⁶ That document focuses on the BBC's relationship with its commercial subsidiaries with an aim to ensuring that the commercial activities do not receive an unfair competitive advantage or distort the market due to their relationship with the BBC Public Service. For the reasons set out below, the requirements set out in this trading activities consultation are based on the requirements set out in the commercial activities statement.
- 1.13 Our commercial activities statement lists a number of areas for further evidence gathering work and engagement with the BBC. In relation to trading activities, we also expect to engage in further work following the publication of our statement. Some of these are also relevant to trading activities, and we will consider the impact of that work on the requirements proposed here as appropriate.

Purpose of this document

- 1.14 The proposals in this document are intended to form part of the BBC's Operating Framework, and as such include obligations which are binding on the BBC.
- 1.15 This document sets out the requirements that we propose to impose on the BBC to ensure that its trading activities do not harm fair and effective competition in the UK.
- 1.16 Where we have discretion to impose requirements or to determine the form of the requirement, we have assessed the need for such a requirement, in line with our statutory duties.

⁶ See: https://www.ofcom.org.uk/ data/assets/pdf file/0025/99412/bbc-commerical.pdf

Section 2

Legal Framework

2.1 Ofcom sets out these requirements and procedures based on the legal framework contained within the Communications Act 2003 ("the **Act**"), the Charter, and the Agreement. This section summarises that framework.

The Communications Act

- 2.2 Ofcom is a statutory corporation created by the Office of Communications Act 2002. Our power to regulate the BBC is derived from the Act, which sets out that for the purposes of the carrying out regulation of the BBC we will have such powers and duties as may be conferred by or under the Charter and Agreement. Our general duties under section 3 of the Act therefore apply to the exercise of our functions in relation to the BBC.
- 2.3 Section 198 of the Act sets out that it shall be a function of Ofcom, to the extent that provision for them to do so is contained in the Charter and Agreement, to regulate the provision of the BBC's services and the carrying on by the BBC of other activities for purposes connected with the provision of those services.

Royal Charter for the BBC

- 2.4 Article 46(2) of the Charter (Principal functions of Ofcom) requires Ofcom to prepare and publish an Operating Framework which must contain the provisions Ofcom consider appropriate to secure the effective regulation of the activities of the BBC, including the trading activities.
- 2.5 Article 46(5) of the Charter requires Ofcom to set requirements in the Operating Framework to protect fair and effective competition in the United Kingdom in relation to (i) the effect on fair and effective competition of trading activities; and (ii) agreements with, and conduct affecting, third parties in relation to trading activities.

Agreement between the Secretary of State and the BBC

- 2.6 Under clause 31(1) of the Agreement, the BBC is permitted to carry out trading activities.
- 2.7 Under clause 31(2) of the Agreement, "trading activities" means activities which are commercial in nature but are not to be treated as commercial activities. We outline what these encompass at paragraph 3.2.
- 2.8 In carrying out the trading activities, the BBC must comply with the requirements, in the Operating Framework, to protect fair and effective competition.⁷
- 2.9 Clause 32 of the Agreement states that the Operating Framework must set out how we will regulate the BBC's trading activities and the procedures to be followed (including such requirements we consider appropriate to protect fair and effective competition).

⁷ Clause 31(3) of the Agreement.

Section 3

Trading activities requirements

- 3.1 This section sets out the requirements we propose to impose on the BBC to address potential competition concerns arising from the trading activities. The objective of these requirements is to ensure that the BBC's trading activities do not harm fair and effective competition. We also provide guidance on interpreting these requirements.
- 3.2 Clause 31(2) of the Agreement states that trading activities comprise the following: 8
 - a) the selling of assets or of excess capacity in the BBC's resources held for use by the UK Public Services (including any capacity on a television multiplex service that is under the BBC's control) (e.g. studio space)
 - b) the provision of facilities and services which are ancillary to the provision of the UK Public Services and in respect of which any charge is imposed primarily for recovering the costs or expenses of the provision, even if other factors (for example, rounding the charge for convenience) make a profit likely; (e.g. tickets to PS events)
 - c) licensing or otherwise disposing of rights in anything created for the purposes of the UK Public Services or the World Service⁹; (e.g. licensing of rights to publish the DVD of a BBC-produced programme)
 - d) sub-licensing or otherwise disposing of rights which are not required for the promotion of the Public Purposes and which are acquired incidentally by the BBC as part of a larger package of rights which, as a whole, was acquired only because the package included rights which were required for the promotion of the Public Purposes; (e.g. sub-licensing of sports rights)
 - e) trading or other activity between the BBC and the BBC's commercial arm, or between different parts of the BBC's organisation; (e.g. provision of shared services/group functions such as finance or HR)
 - f) securing up-front investment from third parties in BBC content (e.g. provision of co-production funds in exchange for secondary distribution rights)
- 3.3 Below we set out the competition concerns that may arise when the BBC Public Service is offering goods and services i) to its own commercial subsidiaries and ii) to third parties.

Potential competition concerns

3.4 Competition typically produces benefits for society. Where a supplier offers a more attractive service or a better price than its rivals, it is likely to win customers and can attract new customers to the market. This in turn creates an incentive for all firms to innovate and invest in producing better services and to keep prices in line with their costs.

⁸ Examples given in bold are added by Ofcom and are not part of the text of the Agreement.

⁹ The World Service is a non-commercial service primarily targeted at audiences outside the UK. Matters relating to the World Service are not included as part of Ofcom's remit.

- 3.5 The unique position of the BBC as a publicly funded broadcaster enables it to create and acquire assets which can form important inputs into other services. The way that the BBC makes these assets available to the wider market has the potential to have an impact on competition in relevant markets. There is a concern that the BBC Public Service may use licence fee funded assets in a way which might harm fair and effective competition.
- 3.6 The BBC Public Service uses the licence fee to fund a range of services, including content which may also have value in secondary/overseas markets. While trading activities are not expressly designed to make a profit, the BBC Public Service can generate income, in order to supplement the licence fee funded assets, by selling them to BBC commercial subsidiaries and other third parties.
- 3.7 In addition, the BBC Public Service may, in the interests of commercial efficiency, choose to provide other goods and services to the commercial subsidiaries and other third parties. For example, the BBC may wish to provide an external producer with access to facilities and staff to support programme making for an appropriate charge.

Trading with commercial subsidiaries

- 3.8 Where the BBC is trading with its own commercial arm, there is a risk that the relationship between the BBC Public Service and its commercial subsidiaries could give the subsidiaries an unfair competitive advantage. This could occur, for example, if the subsidiaries paid less than the market rate for access to BBC Public Service assets or enjoyed preferential access to those assets.
- 3.9 If the BBC commercial subsidiaries receive an unfair competitive advantage, competitors may be less able to attract customers, and may be unable to expand or forced to exit the market entirely. This may lead to less innovation and investment, and ultimately worse outcomes for UK consumers in terms of their access to quality services.

Trading with third parties

- 3.10 Concerns may also arise where the BBC Public Service is offering goods and services to the wider market.
- 3.11 Competition concerns will vary depending on the nature and scope of the trading activity in question. However, they are likely to stem from one of the following concerns:
 - **Discriminatory pricing/access:** when it supplies products or services to others, the BBC may do so in a discriminatory manner. This could include charging different prices to different third parties for the same service, granting preferential access or refusing to supply to certain third parties. Trading in this way may put certain parties at a competitive disadvantage.
 - Pricing below market norms: there is a risk that the BBC Public Service offers
 goods and services at below market price, due to cost advantages that it may
 enjoy as a large publicly funded body, which could make it difficult for suppliers of
 similar services to compete. This could occur, for example, where the BBC offers
 access to licence fee funded assets with spare capacity, such as studio space,

- based on short run incremental costs, which may be below typical unit costs faced by independent suppliers.¹⁰
- 3.12 The risk of adverse effects from this type of behaviour will depend on the nature of the activity in question. When deciding whether to open an investigation, we will consider whether the BBC's trading activities are likely to lead to a market distortion and would only intervene if a material effect on competition can be identified. As part of our analysis, we will therefore assess the nature of competition, and the specific risks and possible impacts associated with the BBC's activities.

Requirements for trading between the BBC Public Service and BBC commercial subsidiaries

- 3.13 As explained in paragraph 3.8, where the BBC is trading with its own commercial arm, there is a risk that the BBC Public Service could provide its commercial subsidiaries with an unfair competitive advantage.
- 3.14 Our requirements and guidance on the BBC's Commercial Activities address this concern. We have put in place a range of requirements to ensure appropriate operational and financial separation between the BBC Public Service and its commercial subsidiaries. In relation to trading with the commercial subsidiaries, we require:
 - Arm's length commercial arrangements and terms;
 - · Equivalent access to goods and services by third parties;
 - Fair transfer pricing for goods and services, including content, rights and brands.¹¹

Proposed requirements for trading between the BBC Public Service and third parties

3.15 Although our regulation of the BBC's commercial activities addresses competition concerns that arise from the relationship between the BBC Public Service and its commercial subsidiaries, additional requirements are necessary to address the broader concerns identified in paragraph 3.11, where the BBC is offering services to third parties. These requirements are set out in the table below:¹²

¹⁰ We recognise that the relevant market rate will vary depending on the nature of the arrangement in question. Where occasional sales are being made on an ad hoc basis, prices that cover short run incremental costs of providing studio pace to a third-party, that would otherwise have been vacant, may be appropriate even if the contribution to fixed costs is small (so long as there is no repeated pattern of such sales). However, for longer-term contracts, or where ad hoc contracts together amount to a significant stream of ongoing business, we would expect prices to include some contribution to the fixed costs of maintaining studio space.

¹¹ See table addressing 'Supply of goods and services and transfer pricing' on page 14 of our requirements and guidance on the BBC's commercial activities at: https://www.ofcom.org.uk/ data/assets/pdf file/0025/99412/bbc-commerical.pdf.

¹² Note that the pricing requirements set out below are based on our requirements and guidance on the BBC's commercial activities.

Requirement not to unduly discriminate

Where the BBC Public Service supplies goods and services to the wider market, the BBC must not discriminate unduly against or between third parties.

Pricing requirements

The BBC must set pricing for goods and services supplied by the BBC Public Service on the basis of the following principles:

- Set market prices and terms for goods and services, where appropriate using an open market process (e.g. competitive tendering).
- Absent an open market process, set market prices and terms using verifiable, comparable information on prevailing market practices wherever possible.
- Where there are no relevant market benchmarks or evidence on market practices, adopt a cost-based approach.
- Where a cost-based approach to pricing is used, ensure the price covers:
 - All relevant direct costs involved in providing the good(s) or services;
 and
 - An appropriate contribution to the relevant overheads and capital costs incurred by the business areas together with an appropriate contribution for reinvestment in the Public Service activities.
- Base prices on the BBC's incremental costs of providing a good or service only where it can be demonstrated that incremental cost pricing conforms to market practice and not set prices below incremental cost under any circumstances.
- Ensure that any pricing methodologies and terms and conditions are reviewed regularly, and consistent approaches are applied to any similar goods and services, including agreements for use of the BBC Brand.

Requirement to maintain records of trading activities

The BBC must maintain records of its trading activities with third parties.

Requirement not to unduly discriminate

3.16 To address the concerns we have around discriminatory access and pricing, we propose that where the BBC Public Service supplies goods and services to the wider market, the BBC must not discriminate unduly against or between third parties.

Pricing requirements

3.17 We propose that the market pricing principles in our guidance on the BBC's commercial activities apply to the pricing of goods and services sold by the BBC Public Service to third parties. This should address the risk of the BBC Public Service pricing services below market norms.

- 3.18 We propose to impose the above requirements to address the risk of the BBC pricing services below market norms. We note the following by way of additional guidance on these requirements:
 - The BBC should consider whether it would be appropriate to sell goods and services through an open market process. For example, where feasible, a competitive tendering/bidding process would be the best way to identify the market price for the good or service in question.
 - Absent an open market process, in pricing the goods and services of the BBC Public Service, the BBC must use any verifiable, comparable information on prevailing market practices (including both prices and terms and conditions). In particular, we expect the BBC Public Service to use market benchmarking to value the secondary and ancillary rights of its originated content in most cases.
 - Where possible, evidence should be gathered from publicly available sources (e.g. published rate-cards¹³). It may also be appropriate to use benchmarking studies or independent experts.
 - Where the BBC adopts a cost-based approach to derive a price, the BBC must be able to justify using this approach, for example with reference to the work done to assess the availability of any relevant market benchmarks.

Requirement to maintain records of trading activities

- 3.19 The BBC must maintain records of its trading activities with third parties.
- 3.20 The BBC maintaining records of its trading activities will allow Ofcom to investigate complaints or carry out own-initiative investigations as required.
- 3.21 We expect to engage with the BBC periodically to ensure that its records are sufficient for our purposes.

Complaints and Investigations

- 3.22 This document forms part of the BBC's Operating Framework, meaning that the obligations it imposes on the BBC are "specified requirements" as defined by clause 59(a) of the Agreement. Ofcom can enforce the requirements set out in this document either by considering a complaint or by conducting an investigation (clauses 57 and 58 of the Agreement). If Ofcom is satisfied the BBC has failed to comply with any of these requirements, Ofcom may make directions or accept undertakings from the BBC (article 49(2) of the Charter).
- 3.23 The Charter and Agreement state that Ofcom must set out procedures for the handling and resolution of complaints, for conducting investigations and for the imposition of sanctions in relation to breaches of competition requirements.¹⁴ Ofcom

¹³ An example of where a rate-card may be used is for hiring a studio. We recognise that published rate-cards may not always be an accurate representation of actual prices paid for services. That is, the rate-card may only serve as a starting point for commercial negotiations over price.

¹⁴ Charter, Article 49(6); Agreement, Clause 5(4), Clause 57(1), Clause 58(2).

has consulted on draft enforcement procedures which will be finalised in due course. $^{\rm 15}$

¹⁵ See our *Procedures for enforcement of requirements in the BBC Agreement and compliance with Ofcom enforcement action* at:

https://www.ofcom.org.uk/__data/assets/pdf_file/0024/99420/bbc-agreement.pdf;
See our consultation, *Procedures for enforcement of BBC Competition requirements* at:
https://www.ofcom.org.uk/__data/assets/pdf_file/0039/96798/Procedures-for-enforcement-of-BBC-competition-requirements.pdf.

Annex 1

Responding to this consultation

How to respond

- A1.1 Of com would like to receive views and comments on the issues raised in this document, **by 5pm on 24 May 2017.**
- A1.2 We strongly prefer to receive responses via the online form at https://www.ofcom.org.uk/consultations-and-statements/category-2/bbc-trading-activities. We also provide a cover sheet http://stakeholders.ofcom.org.uk/consultations/consultation-response-coversheet/) for responses sent by email or post; please fill this in, as it helps us to maintain your confidentiality, and speeds up our work. You do not need to do this if you respond using the online form.
- A1.3 If your response is a large file, or has supporting charts, tables or other data, please email it to BBCTradingActivities@ofcom.org.uk as an attachment in Microsoft Word format, together with the cover sheet (http://stakeholders.ofcom.org.uk/consultations/consultation-response-coversheet/).
- A1.4 Responses may alternatively be posted to the address below, marked with the title of the consultation.

Alex Pascoe Ofcom Riverside House 2A Southwark Bridge Road London SE1 9HA

- A1.5 If you would like to submit your response in an alternative format (e.g. a video or audio file), please contact Alex Pascoe on 0300 123 3000.
- A1.6 We do not need a paper copy of your response as well as an electronic version. We will acknowledge receipt if your response is submitted via the online web form, but not otherwise.
- A1.7 If you want to discuss the issues and questions raised in this consultation, please contact Alex Pascoe on 0300 123 3000.

Confidentiality

- A1.8 Consultations are more effective if we publish the responses before the consultation period closes. In particular, this can help people and organisations with limited resources or familiarity with the issues to respond in a more informed way. So, in the interests of transparency and good regulatory practice, and because we believe it is important that everyone who is interested in an issue can see other respondents' views, we usually publish all responses on our website, www.ofcom.org.uk, as soon as we receive them.
- A1.9 If you think your response should be kept confidential, please specify which part(s) this applies to, and explain why. Please send any confidential sections as a

separate annex. If you want your name, address, other contact details or job title to remain confidential, please provide them only in the cover sheet, so that we don't have to edit your response.

- A1.10 If someone asks us to keep part or all of a response confidential, we will treat this request seriously and try to respect it. But sometimes we will need to publish all responses, including those that are marked as confidential, in order to meet legal obligations.
- A1.11 Please also note that copyright and all other intellectual property in responses will be assumed to be licensed to Ofcom to use. Ofcom's intellectual property rights are explained further at http://www.ofcom.org.uk/terms-of-use/.

Next steps

- A1.12 Following this consultation period, Ofcom plans to publish a statement in July 2017.
- A1.13 If you wish, you can register to receive mail updates alerting you to new Ofcom publications; for more details please see http://www.ofcom.org.uk/email-updates/.

Ofcom's consultation processes

- A1.14 Ofcom aims to make responding to a consultation as easy as possible. For more information, please see our consultation principles in Annex 2.
- A1.15 If you have any comments or suggestions on how we manage our consultations, please call our consultation helpdesk on 020 7981 3003 or email us at consult@ofcom.org.uk. We particularly welcome ideas on how Ofcom could more effectively seek the views of groups or individuals, such as small businesses and residential consumers, who are less likely to give their opinions through a formal consultation.

If you would like to discuss these issues, or Ofcom's consultation processes more generally, please contact Steve Gettings, Ofcom's consultation champion:

Steve Gettings
Ofcom
Riverside House
2a Southwark Bridge Road
London SE1 9HA

Tel: 020 7981 3601

Email steve.gettings@ofcom.org.uk

Annex 2

Ofcom's consultation principles

Ofcom has seven principles that it follows for every public written consultation:

Before the consultation

A2.1 Wherever possible, we will hold informal talks with people and organisations before announcing a big consultation, to find out whether we are thinking along the right lines. If we do not have enough time to do this, we will hold an open meeting to explain our proposals, shortly after announcing the consultation.

During the consultation

- A2.2 We will be clear about whom we are consulting, why, on what questions and for how long.
- A2.3 We will make the consultation document as short and simple as possible, with a summary of no more than two pages. We will try to make it as easy as possible for people to give us a written response. If the consultation is complicated, we may provide a short Plain English / Cymraeg Clir guide, to help smaller organisations or individuals who would not otherwise be able to spare the time to share their views.
- A2.4 We will consult for up to ten weeks, depending on the potential impact of our proposals.
- A2.5 A person within Ofcom will be in charge of making sure we follow our own guidelines and aim to reach the largest possible number of people and organisations who may be interested in the outcome of our decisions. Ofcom's Consultation Champion is the main person to contact if you have views on the way we run our consultations.
- A2.6 If we are not able to follow any of these seven principles, we will explain why.

After the consultation

A2.7 We think it is important that everyone who is interested in an issue can see other people's views, so we usually publish all the responses on our website as soon as we receive them. After the consultation we will make our decisions and publish a statement explaining what we are going to do, and why, showing how respondents' views helped to shape these decisions.

Cover sheet for response to an Ofcom consultation

BASIC DETAILS			
Consultation title:			
To (Ofcom contact):			
Name of respondent:			
Representing (self or organisation/s):			
Address (if not received by email):			
CONFIDENTIALITY			
Please tick below what part of your response you consider is confidential, giving your reasons why			
Nothing Name/contact details/job title			
Whole response Organisation			
Part of the response			
If you want part of your response, your name or your organisation not to be published, can Ofcom still publish a reference to the contents of your response (including, for any confidential parts, a general summary that does not disclose the specific information or enable you to be identified)?			
DECLARATION			
I confirm that the correspondence supplied with this cover sheet is a formal consultation response that Ofcom can publish. However, in supplying this response, I understand that Ofcom may need to publish all responses, including those which are marked as confidential, in order to meet legal obligations. 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)			