

## 9. The scope and regulation of commercial services

### What people think

- There is widespread support for the idea that the BBC should make money on behalf of the licence fee payer out of assets paid for by the licence fee payer – 90% of people surveyed agree that ‘the BBC should raise as much money as it can from selling its programmes and other products’.
- But concerns are raised in a number of areas, including:
  - Whether or not the BBC’s commercial activities should be more closely aligned to its publicly funded services
  - Fairness and transparency
  - How the money should be used – whether it should just be spent on better programmes (50% of participants), only used to reduce the licence fee (30%) or both (20%)
  - Whether or not the current arrangements deliver the best value for money

#### Our policy

The BBC should be encouraged, as it is now, to generate as much income as it can through commercial activity, including the sale of programme rights. Since licence fee money is not at stake, and in the light of the more transparent governance arrangements that we will introduce, the Secretary of State’s approval should no longer be required for the launch of new commercial businesses or the sale of existing ones.

However, each commercial activity must be tested to make sure it adds sufficient value and is in some way related to core purposes.

Commercial services should also be kept entirely separate from publicly-funded activity – there should be no cross-subsidy of the former by the latter, no on-air trailing of commercial services, and fair trading commitments must be rigorously and transparently regulated.

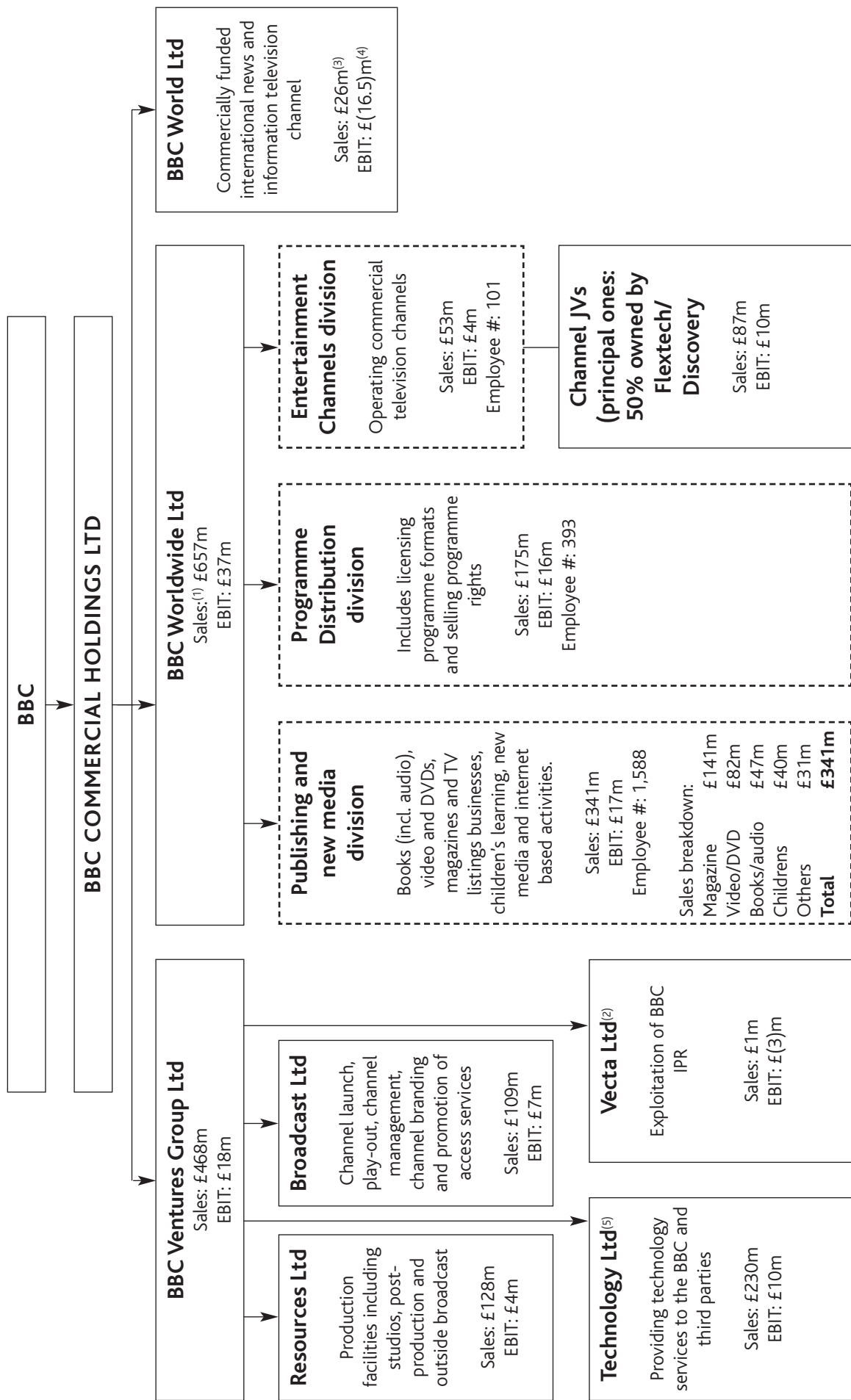
### The BBC’s existing commercial services

- 9.1 The BBC is active in a number of commercial markets. The structure and range of principal activities, together with key financial data from 2003–4, is described in the organisation chart overleaf. The BBC estimates that a total of over £140 million flows back to its public services from commercial services, but the actual profits generated by these businesses amount to only £38.5 million.

### What commercial services should the BBC run in future?

- 9.2 Each commercial service should be assessed against four criteria to establish whether or not the BBC should be engaged in that activity:

**Fit with PSB purposes** – does the activity either support or relate to PSB purposes?



Notes: EBIT = Earnings Before Income Tax. (1) Includes £87m of share of JVs; (2) The BBC announced the closure of Vecta in July 2004; (3) Sales figure estimated from 2003/04 BBC Annual Report – total commercial revenue of £1,151m less sales from BBC Ventures plus BBC Worldwide (£1,125m); (4) Source: Directly quoted in the 2003/04 BBC Annual Report; figures refer to year ending 31 March 2004 and all holdings are 100% except where stated. All boxes under BBC Commercial Holdings represent limited companies except the dotted boxes under BBC Worldwide, which are operating divisions of BBC Worldwide; (5) Technology was sold to Siemens Business Services in October 2004.

**Commercial efficiency** – is BBC ownership the most effective economic exploitation of the capital involved or might a sale or licensing of the asset create better value for money for the licence fee payer?

**BBC brand protection** – is there a positive or negative implication for the BBC's brand or values?

**Market distortion** – are BBC commercial services being sold or structured in a way that might give them an unfair advantage over the competition?

- 9.3 Asking these questions helps to address the most common criticisms currently levelled at the BBC's commercial operation. First, that it is not adequately aligned to the core public service remit. Second, that there is too much cross-promotion of commercial services by public services (for example through on-air trails). Third, that the BBC's commercial businesses are not particularly profitable or efficient by industry standards, and might make more money for the licence fee payer if they were sold or licensed to other operators.
- 9.4 Since licence fee money is not at stake, the Secretary of State's approval should no longer be required for the launch of new commercial businesses or the closure of existing ones.

### The BBC's own review

- 9.5 The BBC has recently conducted an internal review of its commercial services. It concluded that the BBC should only have commercial services that exploit and/or export BBC content and the BBC brand. It also accepted that the principle behind BBC involvement with commercial activities was to maximise profits on behalf of the licence fee payer.
- 9.6 Following this review, the BBC has announced it will consider selling BBC Broadcast and BBC Resources, or transferring them into joint ventures or partnerships. It will consider the same options for some of BBC Worldwide's smaller operations, including its book publishing. Magazines will in future be focused more on brands and subjects that are connected to BBC programmes and on-air trailing of BBC magazines has been stopped. The BBC will look to grow its channel and programme sales business, and to pursue partnerships with other UK broadcasters. Its overall aim is to double the profits of BBC Worldwide over the next two years, which would mean it contributing earnings before tax of around £75 million annually to public services (although part of this growth will come from the cessation or sale of loss-making activities).

### Government response to the BBC review

#### Support services

- 9.7 We recognise the arguments behind the BBC's suggestion that BBC Broadcast and BBC Resources are candidates for sale or joint venture. The BBC's support services – its production studios and broadcast services – are reasonably efficient but do not generate large profits. If they could be sold with sufficient contractual protection to sustain the BBC's ability to put together large-scale outside broadcasts then we think sale should be considered. We think there is no strong strategic or public service reason for the BBC to retain them.

## Publishing

- 9.8 We also accept the argument that the BBC does not need to retain its small amount of business as a book publisher. However, we have some concerns about the strategy for its magazine business. Here the BBC has real scale – it is the fourth largest publisher of magazines in the UK. However, it is not clear that magazine publishing represents good value for money for licence fee payers. Certain of its magazines clearly do extend the enjoyment of core BBC content – BBC History is an example. But the BBC operation is not commercially successful by industry standards and we would want the BBC to explain how it plans to improve its performance.
- 9.9 If the magazine business is to be retained, we welcome the decision to end on-air trailing. But we want to be sure what the BBC means when it says ‘magazines should focus more on brands and subjects connected to the BBC’s core programmes and mission.’<sup>52</sup> At present, many titles are clearly not linked to BBC programme titles (for instance *Your Hair* or *Cross Stitch Crazy*) and are thus unconnected to public purposes. One such magazine, *Eve*, has already been sold. There is scope for considering whether more sales should be undertaken, so that publishing activity is restricted to those magazines that include content with a direct link to BBC programming and not to more general titles such as BBC Good Food. If the consequent reduction in scale would be considered too harmful to the magazine operation as a whole, the BBC should consider whether a licensing arrangement with a third party might bring in more money than the £17 million of profits it currently records.

## Programme sales

- 9.10 Programme sales provide significant revenue for the BBC. In overseas markets, they are directly tied to one of the BBC’s public purposes – to export UK content, culture and values. They represent real value for money and we fully support the BBC’s ambition to grow and improve their global services. However, the BBC should ensure that it is exploiting its assets in the most effective way. We would particularly like to see plans for the improvement of the loss-making BBC World (a commercial global news channel, not related to the radio World Service) and BBC America (a commercial channel in the US that mainly broadcasts lifestyle programming). We would support any move by the BBC to form new sales partnerships with other UK broadcasters, for example with Channel 4 or ITV, that might generate economies of scale.

## Commercial channels

- 9.11 The BBC’s commercial channels, many of which sit within the BBC-Flextech joint venture UKTV (including UK Gold, UK Living and others), perform a valuable role in extending the consumption of the BBC’s rich archive of programming and leveraging the resources of the BBC to develop new channel offerings in the UK. The BBC’s review of commercial services envisages the retention of these channels and we agree with this conclusion. We would also support the strengthening of financial performance through further expansion, provided that any such move does not compromise any of the BBC’s broader core purposes.

<sup>52</sup> BBC press release, ‘Thompson unveils plans to transform the BBC’, 7.12.2004

## Profits from asset sales

- 9.12 If the BBC is going to profit from the sale of any asset, there is a question over where that profit should go. If it is returned directly to the BBC's programme budget, there may be a case for reducing the level of the licence fee accordingly. This issue should be considered further by the funding review that will help set the overall level of the licence fee.

## Regulating commercial services

- 9.13 The BBC has taken steps to reform the management board of BBC commercial services, with the appointment of non-executive directors and the publication of much more detailed accounts. We welcome these developments, which should allow a clearer assessment of the performance of each business.
- 9.14 There are two further issues to consider, to ensure the BBC's commercial services operate in the public interest:
- fair trading; and
  - transparency
- 9.15 Transparency is the easier to deal with. Licence fee payers should be able to understand exactly how money moves between commercial services and publicly-funded services, and what they get for their money. That may involve the publication of more detailed accounts.
- 9.16 Regulation is more complex. The BBC's commercial services are regulated by Ofcom and the OFT under general competition law, like any other company. They are also subject to an additional fair trading regime, with aspirations that go beyond competition law, overseen by the Board of Governors. The BBC's Fair Trading Commitment is summarised in **Annex B**.
- 9.17 The Fair Trading Commitment has proved controversial – it is expressed in fairly general terms and some have argued that the Governors have not upheld it rigorously enough. Some of its clauses replicate aspects of competition law that are anyway regulated by Ofcom, the EU or the OFT. Those that are not tend to relate to the ways in which the BBC aims to operate commercial services – providing good value for money, keeping commercial and publicly-funded services separate or limiting any damage to the BBC brand, for instance. Competitors have in some cases found it difficult to know which regulator is responsible for pursuing complaints.
- 9.18 We would welcome views on whether the Fair Trading Commitment should continue in its current form, or whether it might be simpler to separate matters of internal BBC housekeeping from those of external regulation that could be left in their entirety to Ofcom. In that arrangement, one further option would be to require Ofcom to grant its approval to the terms of whatever internal rules remained – as a form of 'ex ante' regulation.

## Further review

- 9.19 The performance of the BBC's commercial services should be kept under review by the BBC Trust. The Trust should conduct a further, formal internal review mid-way through the next Charter period, to consider the financial record of each business against the targets that are set now.