

## BBC Charter Review

### Licence Fee Seminar

#### Session 2: Industry Wide Issues: Cost Pressures and Efficiency

**Lord Burns:** Welcome back, could I remind you about your blackberries. I realise that on this day of all days, this is going to be a terrible problem for the news junkies amongst us. I do keep getting the odd bulletin if anybody wants to know what's going on. Would you like to know? I'll tell you what the headlines are. It says, and this I have to say comes from the Sky News, we're still checking it though, so there are people who have raised questions about its reliability but, the Home Secretary, Charles Clarke, has been sacked in the major cabinet reshuffle, he's returned to the back benches. Jack Straw has lost his position as Foreign Secretary. Someone said he's going to become Leader of the House. Deputy Prime Minister John Prescott has been spared the cull, although I think some of his responsibilities are being removed. He's going to remain as Deputy Leader. Geff Hoon becomes Secretary of State for Europe, and the Foreign Office will be Margaret Beckett, so we have one Minister for the continent and one for the rest of the world, and that's all this story says.

**Audience Q:** John Reid at the Home Office.

**Lord Burns:** John Reid at Home Office. Isn't it wonderful, I mean, Jenny here ...

**Audience Q:** Which I got from the BBC News Service.

**Lord Burns:** Are there any communications facilities in DCMS? OK. I had another request. Someone wanted to know where they would be able to see the webcast. I don't know if the plan is to go home from here and watch it all again, but it is on [www.bbccharterreview.org.uk/seminars](http://www.bbccharterreview.org.uk/seminars) and I think you'll find your way there. Welcome to the new panel. If you just quickly introduce yourselves.

**Mark Beilby:** I'm Mark Beilby, I'm Managing Director in Capital Markets Division of Dresdner Kleinwort, investment bank, and I have responsibility for the analysis of the media industry and media companies from the perspective of the public markets.

**Bill Robinson:** I'm Bill Robinson, I'm an economist at PWC. I've done a lot of work over the years in media issues, including on the forecast of advertising revenue, so glowingly praised by Mark Oliver.

**John Cresswell:** I'm John Cresswell, I'm the Finance Director of ITV.

**Anne Bulford:** I'm Anne Bulford, I'm the Finance Director from Channel 4.

**Phil Riley:** I'm Phil Riley, I'm the Chief Executive of Chrysalis Radio.

**John McVay:** John McVay, Chief Executive of PACT, the producers' trade association.

**James Strachan:** James Strachan, broadcasting expert in the sense of being an avid consumer but I think here as a value-for-money man, having just stood down as Chairman of the Audit Commission.

**Lord Burns:** Thank you very much. Margaret, can I ask you to introduce the second session.

**Margaret Exley:** Well, I think we started to get into this in the previous session, that this part of the day is really focusing on the whole area of efficiency and the impact on the wider market and the wider broadcasting sector, and I'm going to start by trying to identify what I think are three issues that I'd like us to take a deep dive into. The first one is this whole question of market impact and the impact of the licence fee settlement on the wider picture. As we started to say in the last session, the interesting thing about this wider picture is that the past is not a good predictor of the future, that is to say, and I'm sure colleagues on the panel will pick up this point, this is a really, really interesting time to be making decisions about licence fee, because over the next few years, there are clearly going to be some quite big structural changes in the industry, the convergence telephony, broadband television, are going to create new opportunities for new paid services and new ways of securing revenue, so we can almost predict that whatever we say today, in five years' time, certainly ten years' time, will be fairly dramatically out of date. So in that context, one of the submissions to describe this is like an elephant jumping into the swimming pool, you know, the BBC displaces so much water in whatever it does that it has all kinds of unintended consequences for the rest of the sector, so this is a chance for us to say what are those, what should the government take care of as it thinks about those issues, and really what's our best bet in terms of the shape and nature of that picture going forward. A second area is this term 'efficiency' and it's used in lots of different ways. I want to suggest that for the purpose of this debate, we define efficiency as the ratio of inputs to outputs, that simply put, this is whether or not the BBC could do more for less, whether more always has to mean more resources, and more importantly in an organisation which is not subject to market pressures, what is it that can be done in the new governance arrangements to ensure that the pressures for cost efficiency remain year by year through the period, not just the last few years before charter renewal. So I think that's an important area. The BBC has said it thinks 2.5% year on year is a reasonable goal, others have said it ought to be nearer to 3.3%. Let's try and just get behind those numbers and look at what are the arguments for and against. And I think the final area is this, for me, this term super-inflation, which I think we could usefully shed some light on in this room. On the one hand there seems to have been in the mid-90's a very clear case for the BBC to be funded to keep up with the game. The question is now, is it ahead of the game, is it creating the inflation that it says it is subject to, and as experts in the field really, what do you know about this, that is to say clearly programming is expensive and quality programming is particularly expensive. The question is, is the rate of increase increasing every year? Is that

something that is recognised in the industry or not? Or on the other hand is it fair to say that this is a feature of the market that has to be managed as with other costs, and that other costs are reducing, particularly technological costs, so I think that third area of super-inflation, is it a real concept, and just how can we tease out the elements that bear on that. So, Chairman, those are my thoughts about how we might structure the conversation.

**Lord Burns:** Thank you very much. Who would like to kick us off? John?

**John Creswell:** Shall we just try and talk a little about super-inflation.

**Audience Q:** Speak up please.

**John Creswell:** Sorry. I'm using the microphone as best I can. Someone's turned it on, thank you. Super-inflation, I think the level of super-inflation set out here would allow Mark to become Roman Abramovich really. You may look like him a little but you've kind of let the BBC become a Chelsea, and that super-inflation is a concept seemingly designed by the BBC to be delivered by the BBC. As a commercial broadcaster, you know, continually we're in a competitive market obviously, and I can't quite understand where the super-inflation is. What is it that's driving the super-inflation? It's not going to be ITV which is the BBC's main competitor for talent and rights that's going to be able to drive and look to drive super-inflation to that degree. If it's £1.4 billion across seven years, that's £200 million. Now, Mark made the argument that partly that's not only just paying more for what you have at the moment, but it's a genre mix. Well, you know, even if you said, 'Right, I'll take a repeat out of BBC peak time and put an hour of costume drama in it at a million pounds an hour, and did one an hour a week,' that's 50 million, so I just, you know, in terms of super-inflation, it's not something that we would recognise, and I've found in terms of all the documentation I've read, no real justification for it. I just don't quite understand what exactly it's designed to pay for.

**Phil Riley:** Chairman, I would just like to say, from the commercial radio section, I don't think we recognise super-inflation either. I mean, the commercial radio sector, it isn't a warm Jacuzzi or a cold bath, it feels like we've been in the shower and somebody's turned the water off and we've still got soap in our eyes, but super-inflation, I think the difference between radio and television is, I think there probably is a genuine talent market in television, because you're talking about performers operating from one network to another. That's much less the case in radio and certainly from the figures that we've seen bandied about in the press of late, clearly the BBC has a significant roster of talent that it's paying significant sums to. The commercial sector, each individual company might only one or two stars that would venture into that same league table, so that there is no doubt, in radio at least, the BBC is setting the market for talent, and if the BBC has decided it needs to pay super-inflation to that talent, the commercial sector is just going to be dragged along behind it, which is not a situation that we want to get into, and I was particularly pleased to hear Mark Thompson say that radio has been

fixed at RPI zero for the past few years, and if we could have a commitment that that would be the same going forward, it will be a start.

**Lord Burns:** Bill.

**Bill Robinson:** I first encountered this concept of, I think we used to call it 'the price of talent', in the early 90's, and there is no doubt in my mind that it was a very important phenomenon then, and the simple way of explaining this is there is a wonderful stylised fact which is that the amount that Julia Roberts gets paid for a film, Julia Roberts, my favourite film star, the amount that she gets paid for a film is twice what another famous film star of an earlier era, Marilyn Monroe, got paid, and the reason for that is that there is twice as much money available to pay her because of the success of video sales. What's that got to do with this? A great deal because as Mark said, the BBC's share of total revenues, although it's going up in real terms, its share is falling and this has been the case really every since the cosy duopoly of the 80's between ITV and BBC, was challenged by the incursion of Sky. We talked a lot about the digital revolution, but really that earlier distribution revolution whereby we had more players coming into this market, the repercussions of that were that you had a great deal more revenue and effectively many more hours to fill and people of course then started to bid for, there was the same amount of talent. Next question, I'm an economist and one of the things economists tend to believe is that supply responds to demand, so if you drive up the price by spending more, don't people enter the market, and that's where the Julia Roberts thing comes in. Yes, if you're talking about making programmes and as it were more people can decide to become programme-makers over time, they get trained and you get an increase in volume, but if you're talking about really special talent, actually there are only going to be a few Julia Roberts in the world and everyone wants them, and so the price gets a bit up. So there are these two sorts, if you like, of super-inflation, one of which I think is temporary and one of which has an enduring effect, but there is a second. In my conversation, after his kind remarks, with Mark, we were talking about something else which is that there are adjustment processes which go on for, you know, a very long time, and people think they're a trend, but they do come to an end, and I think this is the really interesting question about super-inflation. I have no doubt whatever that it was a very, very real phenomenon in the early 90's, and essentially if you wanted the BBC to be able to stay in the market and have, you know, an array of good talent, it had to be given the money to compete for this rising cost of talent. But is that still true 13 years later? I mean, has the market actually adapted in the sense that the supply has been called forth, we have a much bigger industry, are those same forces still at work? Well, yes a bit they are still at work, for the reason that Mark gave which is that it is still the case that there more money, as it were, coming into this industry than is coming into the BBC, so it is always at some risk of being outbid, and that is to the extent to which I think there is still a bit of super-inflation, but you know, how big that it is, I don't know, and that it's much smaller than it was in the early 90's seems to me absolutely certain.

**Lord Burns:** Isn't it the case, Bill, that I mean, for a long time people came to the view that service industries were going to have a higher inflation rate than other forms of industries because their wages were rising, earnings were rising, but somehow or other it was argued they didn't have the same potential for efficiency gains that you saw in manufacturing, and isn't that one of the things that we now see that has changed very dramatically, because service industries do, by one means or another manage these days to achieve quite substantial increases in productivity, and after all, nowadays in broadcasting, it seems to me that much of the costs have been subject to technological improvement and change which has meant that it's much cheaper to do a great deal of this, and fortunately, you know, I mean, the Julia Robertses of this world may earn a great deal of money and we see it in lots of other industries where the people at the top end get very large returns relative to the average, but you know, the BBC doesn't employ very many Julia Roberts, and you know, the vast majority of the costs, you know, well, there's a lot of costs that aren't wage costs and there are a lot of the costs that are I would have thought subject to quite considerable potential improvements in productivity and we have been seeing this happening, so I just put it to you, I mean, this sounds to me a rather old-fashioned kind of concept. This whole thing is steeped in the past and we have to move on and recognise that service industries are capable of generating efficiencies and the notion of super-inflation in this world is, you know, is a bit of yesterday's language, Mark.

**Mark Thompson:** You feel that would be the right moment for you to come in here perhaps. Yes. Well, let me say a few things and perhaps we'll suggest that Zarin can basically then correct me as to the facts. Well, I suppose the first thing I want to say is, I feel that the way Margaret's phrased it, you know, trying to look at efficiencies at the most essential macro level of inputs and outputs feels right, and it's quite important to put the super-inflation argument in context, which is that every enterprise, when you're looking at net productivity gains, has to look at productivity gains after you've considered those cost lines which go up rather than down. Super-inflation is a way of talking about some of the cost lines which we believe will have to go up, you know, because of external factors. The BBC is not suggesting that super-inflation needs to be funded, as it were, by a higher licence increase. What we're saying is when you look at the BBC's plans, absolutely you can ask the BBC to make net productivity gains over this period, you must do that, but everyone has to recognise that those gains have to be net of some of the costs that go up. How is the BBC doing in terms of the way it pays people to work for it? I mean, you know, the licence fee basically goes to people to make great content, we give it to the public, that's the economic engine which delivers the content. The overall wage story, the story of remuneration for BBC staff at large is of an average of I think of about 2% real growth in earnings per year over the present charter period. The media sector of the whole we believe at 2.7% over that period and some segments get well above 2.7%, so the overall macro story on pay at the BBC is that it has run at a lower rate than the media sector as a whole. However, we absolutely do believe, and it's not just a kind of theoretical belief about the future, it is our practical experience right now that for some categories of talent, key talent, rates are running very differently, and we are currently, I'm not going to talk about

individual cases right now, in cases both on television and have very recently in radio where very straightforwardly what's happening is other broadcasters are coming in and are offering people who are currently working for us far, far, far higher rates than they're currently getting. Now, generally what we try and do is we, the BBC can offer artists, producers, programme-makers, an amazingly wide creative range of work, and there are great reasons for coming and working for us and we try and emphasise those. We are frequently right now in a position where we are trying to hang on to key artists for example, not offering them what the market is currently offering them, but trying to persuade them that they should continue to work for us because of the creative range we offer, even though they will get less than the market will offer. This is still absolutely alive and indeed I would say, right, now in the short run, we're actually seeing quite an intense, one of one's distinguished colleagues in one of the other public service broadcasters, not Charles Allen, it must be said, has taken to describing himself as the Roman Abramovich of British TV, and we are seeing quite acute short-run pressures right now, and what we're trying to do at the BBC is, honestly is not, far from adding fuel to that, we're trying to, where we can, as we do generally with the way we pay people, we want the best people, we want to deliver the best talent we can to the public, but to hold our costs below the market far from actually adding to inflationary pressures. But Zarin, do you want to just talk broadly about how we see super-inflation in the mix of the way we think about the overall BBC economy?

**Zarin Patel:** Can I start by clarifying the numbers first of all. Cumulative numbers always sound huge, don't they. This bid allows for about £37 million per annum of costs rising above inflation. How does that break down? About 50% in straightforward staff costs, about 25% in independent productions, and the other 25% format, talent and rights and copyright, so that's how the £37 million per annum breaks down. Mark's kind of taken you through the data for staff inflation. There's a very good submission on the website from Oxira who are an independent consultancy, who've looked at all the kind of drivers and benchmarked them, so it's worth reading that. But when it comes to financial management of super-inflation, we start from the position that says, how low do we need to go to be able to get that talent, not how high do we need to go, so we set a cap on what we're prepared to pay above inflation, in the first instance. Having decided that, there is a fundamental presumption that they should be financially neutral, so if you're going to pay people more, you're going to have to make them more efficient, either have fewer of them or do the same for less, so that financially neutral cap really incentivises you not to, because the more you pay, the harder you're going to have to work at finding the economies to pay for it, so I think that's a natural inbuilt control. You asked an interesting question about when does it ever come to an end? In the last settlement, sports rights super-inflation was a big component of the bid. This time, nothing at all because we believe it has come to an end. Oliver and Ohlbaum and Mediatique and Ofcom, I think I've done a number of studies to see what super-inflation in the indi sector is, and it kind of averages 3-5%, and I don't believe the BBC is feeding that entirely on its own.

**Mark Thompson:** And moreover there's been a change of, if you like, a public policy in relation to independent production, which is something I

support, by the way, which sees a transfer of value intended towards the independent sector, that inevitably has an inflationary consequence in terms of delivering cost per hour from the independent sector.

**Lord Burns:** Tim.

**Tim Gardam:** Two points, I mean, clearly the growth of digital platforms has unlocked a value insofar as a piece of content can be seen across a lot of platforms, and where the BBC doesn't hold all rights in that of content, it seems to be driving the value of that content, and I'd be interested to hear from John McVay about how far he agrees with the submission in these figures that the increase in the percentage of independent productions on the BBC is going to further drive up the BBC's costs. But the second point I'd quite like to factor into this is if in addition to the figure we set aside for super-inflation the BBC injects a further £1.6 billion into high quality content, how can the BBC be sure that won't in turn fuel super-inflation?

**James Strachan:** I'd like to come back to efficiencies for money, and almost invoke the spirit of Oscar Wilde by pointing out that clearly the BBC were not just looking at price and trying to force down price, so there was a danger in constantly talking about inputs/outputs, where we all know very well that the outputs are very difficult to measure. If I look from my experience in other parts of publicly funded activities, you end up not with some magic metric but you end up with a tripartite of on the one hand you can look at the way an organisation is run, the way management talk about it, the way they are either obviously driven to extract maximum value for money or not is one area, and that's a judgmental thing and people who do that for a living can walk into an organisation and feel it very, very quickly. The second is much more specific, which is not ever good in a discussion like this which is the litmus test deep down in the organisation where you actually take an independent production company, you cost out bits of the supply chain and you compare it. The third bit which I think is the beautiful luxury of this debate is asking those who use and pay for these activities what they think, and I said beauty in the wake of the local government elections, because if you look at for example in local government a group of people who a) do not at any one point in their life use the services in necessarily a very direct way compared to 96% in this case, but b) are almost unanimous in their antipathy, both for the quality of the service, you could argue they will always do that, but paying the level of council tax that there is to pay, so you know, it's 3 billion in the context of a massive amount of money funded by the tax payer, and I would argue in a way when I look at the mounds of documents that have emerged from this, in one sense it's a model of doing it but it's time to move on. Balance, balance, balance is the secret of getting value for money right, and we're talking about a balance between, the BBC does want to aspire to a degree of gold-plating, I would say, in terms of all the areas that have been mentioned in training people, impacting the market, being in the forefront of public service broadcasting, but at the same time the public wants to believe somebody is extracting value for money in that process, and that's why I think the debate needs to move on to how would the Trust operate? Would the Trust actually live up to its name in generating a sufficient degree of trust, that once this amount of money has

been agreed, it's actually through time, otherwise you have a sense of 'Phew, right,' and you go off and run with it. And my very last point would be, I find it difficult against everything I've heard, and this is just an outsider's view, to understand actually why the licence fee should go up, if you extract switchover and spectrum more than the 1.5% before, and I think if you extract, it's about 1.8%, it's hard to hear just listening to everybody's arguments, it's hard to argue that it should go up to a greater degree, not withstanding Mark's sometimes persuasive arguments.

**John McVay:** Thanks very much. We have several points. One I wanted to come back to a little bit about super-inflation or what I'd call super-talent, I'm sure the economists here could work out some sort of formula where the more risk-averse a broadcaster becomes, the richer the talent becomes, 'cos I think that is a problem in the market, that you're dealing with a limited number of super-talent which all the broadcasters want, which producers want to deliver to the broadcasters. You know, I'm sure ITV will fight hard to keep Ant and Dec, so I think there are real issues on that, and I think that's just part of the cycles of the market. I think actually what it shows is that maybe the broadcasters should be more risk positive and look to be developing the next generation of talent in a more positive way rather than always looking at a very limited range of talent. I think that's good for everyone in the market. The agents amongst us might not like it, but I think that's one of the issues to look at, so I think it's always been a fact of creative industries that there is limited talent and the positive we are, the more money they make. In terms of Tim's point about the costs of if the WOCC is a success and this does mean more programming going out to the independent sector, it's really hard to know is it apples and pears, like for like. I think one of the big things I do welcome from the previous session was the BBC saying it's really keen to try and benchmark its cost per hour for its in-house production. This is a revelation because actually to arrive at some idea of what the real cost per hour for in-house would be fantastic, and I think that's, you know, if you're looking at inputs and outputs, the key to that is what are the measurements that are transparent and open. Again this goes back to the role of the Trust. I think one of the things which we and indeed some of you although probably don't want to admit here, have fought for many years is for the BBC to have to go through a market impact assessment, to have to go through value for money tests, and to actually have proper service licencees for its channels. I think that's all, if we're keeping with this sort of aquatic analogy, hey, that's the baby in the bathwater that I think we should actually embrace. I've got three kids so I'm allowed to do that. So, you know, I think there's a number of issues about how the BBC does justify its efficiency and I think, you know, when I contract a plumber, a painter or decorator, a car mechanic, I'm looking for three things. I'm looking for them to be efficient, I'm looking for them to be effective, and critically for them to deliver quality, and the price for that quality is something that I'll vary depending on what I get for it, and I think that if you take aside the point about all the other things the BBC maybe has to do, as a producer's organisation looking at the programming spend for the BBC, it's ultimately the licence fee payer will not care about all the digital switchover and everything else. They'll care about on the digital services, do they still get quality programming? They won't really care whether that's

delivered by the BBC or delivered by Granada for the BBC or delivered by an independent producer for the BBC. That's a critical test and I think, you know, we do need to have a strong licence fee funded BBC in order to deliver that, and I think that's good for everyone, but I go back to where I started about the risk-averse, I think it's important that the BBC becomes more risk-positive.

**Anne Bulford:** I mean, at Channel 4 we think it's important to have a well-funded BBC and we support the principle of a licence fee which allows the BBC to make a proper contribution and deal with digital switchover, and thrive in the digital world, but the scale of the bid is such that it's absolutely essential that there's maximum transparency around that, and there are just a few points that I wanted to make around that whole issue of transparency. First of all I think it's essential that there's, whether ring-fencing is quite the right word, I'm not sure, but that funds that are allocated for digital switchover need absolutely to be held for that. It's important that the numbers are properly tested and you know, all estimates won't be perfect, so there's clearly more work to be done on that, but at the end of the day, those funds have to be clearly for that and they mustn't leak into other things. I think we also welcome all the comment and discussion that there's been around transparency on new services and the importance of the public value test and the importance of the market impact assessments which we look forward to seeing. From our perspectives, it's very important that those market impact assessments in particular take account of the whole plurality of public service broadcasting, and that they very much look at the impact of BBC activities on Channel 4 and others working in that same space, and it comes back to this question of what should the BBC do, how much should the BBC do, what are the priorities, and to what extent does the BBC step back from things which are already being provided in the market. The final point I wanted to make is absolutely around the whole area of efficiency targets and super-inflation. Lots of things come through from the Pannell Kerr Forster Report that this absolute need for clarity around what's in the target and what's out of the target and how the numbers are presented so that it's all clear to people seems to us to be essential, and I think our worry, my worry around the question of super-inflation is that if there's a disproportionate settlement for the BBC and it becomes a self-fulfilling prophesy, of course there is competition in the market for scarce talent, that doesn't necessarily mean that overall programme budgets, relationships with independents, relationships with talent have to add up to a particular increase which reflects that top line for those scarce talents, the bet ideas that increasingly all the broadcasters are interested in. If the BBC has that funding set aside, then that super-inflation will take place, and it seems to us that it's part of normal commercial business that you have to manage those tensions and pressures around those things, and I think, you know, I guess we'll come on to talk about market conditions going forward. You know, we're at a very interesting time. We're seeing pressures on traditional forms of advertising market. None of us knows how new services are going to develop, how new sources of income are going to develop, but I don't think many people are predicting significant continuing increase in those markets which will enable the sorts of rates of super-inflation to simply be

paid for without any other steps being taken to manage, mix and churn, and to bring on new talent and diverse talent, and to balance those books.

**Tim Gardam:** Can I just ask a question to that, which is how far will the BBC's own flexibility not to succumb to super-inflation be affected if a rival publicly owned public service broadcaster abandons or lessens its traditional commitment of finding new talent, and to start bidding against the BBC and upping the price in terms of competing for talent?

**Mark Thompson:** Are you asking me or Anne?

**Tim Gardam:** No, I was asking Anne actually, I was asking Channel 4. If Channel 4 starts to move into the market and bid up the price of talent, won't that have an effect on the BBC's ability to suppress its own super-inflation?

**Anne Bulford:** I think Channel 4's always been in the market for talent, I don't think there's any change there.

**Tim Gardam:** What, taking an established channel on top of the BBC.

**Anne Bulford:** I mean, what Channel 4 is is a commercially funded public sector broadcaster and it's looking for the best ideas and the right talent to make the schedule work as a whole. There's no dilution to Channel 4's commitment to bringing on new talent and to developing new independent talent as well as on-screen talent and to working in the regions and changing that. We have to manage our overall programme budgets within constraints, and in many ways bringing an established talent on to the market on to the channel from wherever increases that requirement to develop new talent and bring it through. It doesn't reduce that in any way. I think that we all have that great responsibility.

**Tim Gardam:** So you don't see a risk that Channel 4 will further fuel that super-inflation?

**Anne Bulford:** I think Channel 4 is under the same commercial pressures as our colleagues at ITV and Channel 5. It's a competitive market. As that competition increases, there will be increasing competition for those few, to use Bill's analogy, Julia Roberts, and that doesn't mean that giving the BBC the money to do that and not to have to manage it would be a good thing.

**Lord Burns:** Mark.

**Mark Beilby:** What bothers me, but this is less to do with the cost of talent but in terms of the bench-marking is that it seems to me that in all of this and even in some of the PKF Report, there's a static benchmark as far as the other broadcasters are concerned, Channel 4, ITV, and yet the world for them is changing so quickly, and their future is so uncertain, so to refer to something that was brought up in the last session, you know, advertising is x. I don't think anybody's got any idea over the next ten years, over the duration of this particular licence fee, how advertising is going to evolve. I'd love, for my

own personal purpose, to hear John or Anne's view of that but the word product placement hasn't come up in this at all, and it seems to me that what's wrong in terms of the dialectic of the discussion is that you've got a fixed number coming in for the commercial sector, and you've got a kind of postulation of what the BBC needs to protect its position in this changing environment, which it seems to me, like James, as an observer of this, is to the detriment of the commercial broadcasters, and I'd just like, you know, perhaps Mark's or some of the commercial broadcasters' response to that.

**Lord Burns:** Could we just spend a few minutes on this issue of the shape of the markets, to what extent anyone is prepared to chance their arm on this, you know, what is going to be happening to commercial sector revenues over this licence fee period, but in terms of subscription, pay per view or advertising revenue, because we hear lots of scare stories about how easy it is going to be for people to miss out adverts etc when they watch their PVR's.

**Phil Riley:** Can I just say from a radio perspective, we've just had a year of – 5% growth, so clearly the market is forcing efficiencies on the commercial sector pretty dramatically, and I do think it's highly uncertain what the future for advertising is, particularly given the relentless growth of On-line, which grew at around 70% in the last year and shows no sign of slowing down, and in fact the rest of the advertising sector is effectively being crowded by that, and when you hear the Chief Executive of Google saying, 'Isn't it remarkable, we're taking all this money and people only spend 6% of their time online in surge.' Think of the other 94% we've got to go. I mean, I think really genuinely it is taking great risks with the future of the commercial sector to assume that there will be a nice continuous growth over the next 6 or 7 years in broadcast ad revenue both for TV and radio, and that that will somehow allow us to compete on a level playing field with the BBC. That simply isn't the case, and we certainly don't base our budgets going forward on those sort of comfortable assumptions. I think it's a really tough world out there.

**Lord Burns:** John?

**John Creswell:** Well, I mean, certainly it's a tough world. I was just agreeing with Phil that it's certainly a tough advertising market, you know, there's a certain softness in June which is already out there, so the first six months of this year will probably see a nought, slightly no growth in total TV, so you know, looking forward, you know, the Zenith Report is out in another couple of weeks, they normally give a 5-year forecast. You know, I think last time they were at 3.3% going forward. But I think it's the size of the market and you come back to the inputs and outputs that someone spoke about before. ITV currently spends about 65% of its revenue on originated content. If you look at the competition we have in all the digital channels, there's not a high percentage spent on original content. Therefore, you know, we're absolutely in favour of a strongly-funded BBC but in order for their major competitors to be able to compete with that, there has to be, you know, some kind of level playing-field, as Anne said, in terms of our ability to seek our own internal efficiencies to keep as much value as we can on the screen. So I think, you know, there is a market impact. Subscription revenues we heard before, only

3% I think it was, the figure given that subscription revenue, is spent on originated content. What that means is that advertising currently funds most of the originated content in this market outside of the BBC. You have to look at it in that context.

**John McVay:** Just a couple of points. One, you know, we're basically got an oligarchy facing competition. The winds of change are blowing through broadcasting. I for one, and I think, you know, I take on board ITV's point about funds content and that gives my members a living, but I'm actually proud of the commercial sites in the UK. It's shown itself to be responsive to most challenges that's come along and continue to be responsive. Indeed we're right in the middle of negotiations around new media rights, and what's clear from that, going back to Mark's comment from ITN earlier on, it's not just the BBC who want to be on both sides of the frontier, I can tell you that. All the broadcasters want to be there and that's quite right, you know, they should be there, they are looking to develop their content, to develop the propositions, and the creative commercial responses, what we should absolutely expect from the sector, so I think, you know, I take on board that that is a scary future but it's scary for everyone. I mean, the BBC probably is outside of that but that's scary for producers and it's scary for broadcasters, but I do think that we do have a great commercial sector in the UK and you know, as a producer I may not say this, but I'm actually proud of what commercial broadcasters do.

**Lord Burns:** The third topic Margaret raised was the whole question of efficiencies and what is it that is reasonable to deliver in this industry. Before I throw the discussion to the floor, do any of the panel who are involved in broadcasting or others have any views about, you know, what the mains source of efficiencies are likely to be over the period going ahead, what kind of numbers can one reasonably expect this industry to be able to achieve?

**Mark Thompson:** I'm very struck by some of James's remarks because I mean, firstly just to go half a pace back, clearly there are enormous uncertainties in the developing market. We're seeing, I mean, over the next two years we're going to see a large number of new entrants into pay audio-visual content, big new entrants. I think we'll see in some of the sports rights processes happening this year, you'll see some interesting pressures there from new content entrants. The competitor set, if you like, which the BBC faces, has changed enormously in the last ten years, probably will change more in the next five or ten years, and in its very disruptive phase of media, some traditional media organisations probably won't make it, and you know, that's what it's going to be like, so I think it is going to be a very unstable place. When we come back and just look at this issue of inflationary pressures but also about how the BBC should think about the resource it spends to make the content it delivers to its audiences, I think in a way, you know, I want to go back to James and say, I mean, the way we try and look at this issue and of our performance is around a combination of a delivery of reach to audiences, quality, impact and value. We try and hold those things together. If you try and take one and pay no attention for example to what audiences think about quality, you fail. We're committed to delivering significant and continual net

efficiencies, net productivity and efficiency gains on like-for-like output year on year on year, and for those gains to be fully auditable, to be audited by the NAO and published every year, so that in answer to Tim's question, how can we be sure that the £1.6 billion, that's about £700,000 a day that the BBC's asking for for new quality content, for example new originations for Cbeebies, that that's not going to lead to inflationary pressure. It's because the unit cost of that content, the cost per hour of that content, year on year we are committed to delivering real savings year on year and for all of that to be published. One last point, so that's the way we think about efficiency, which is what do we need, what inputs do we need to deliver not just the lowest possible cost per hour, but cost per hour of high quality content which actually delivers what our audiences want. I'm not quite sure when he uses the word 'gold-plating' but, you know, there's no question, audiences have particular expectations from the BBC which we have to meet as well as thinking hard about the best possible use of the licence fee. The only other point, James, I want to make and I'm afraid this is a day of statistics, but it's worth saying that the RPI plus 1.8% you talked about does not include the so-called industry costs of digital switchover, but it does include, if you like, 0.7% for the BBC's own very substantial costs of digital terrestrial switchover, so if you like, like for like, RPI is plus 1.1%, which is actually a lower rate than the current settlement for like for like services, and even that includes, as you know, proposals for a number of new digital services.

**James Strachan:** Can I come back on that? It's interesting, if you look at how economic regulation has worked in relation to all the industries that were privatised. It started RPI minus x, because basically you were saying, 'This was inefficient, I want to extract.' More recently it's moved to RPI minus x + q, quality, so the debate really becomes on the one hand, if I were looking at this, I would go over to the people who would say that, wouldn't they, and ask them where are the areas in the minus x you think could be greater, and you only have to look at ITN's very good, as I say, ATP's very good, Channel 4, and you can pick out some bits and let's not go through them all, but I mean, Manchester could be cheaper or, etc. and quite quickly you've got a feel for that. The q is the heart of it because the q is 1.6 billion, it's massive, and the q, the quality is a political decision ultimately, and it's also a decision that has to take huge account of the fact that it is remarkable that there were a large number of people out there who would pay an even greater licence fee. Don't for goodness sake use that as an excuse to gold-plate it plus, but always keep that firmly in mind, it's a lovely thing to have.

**Mark Thompson:** I suppose what I want to say, James, is the BBC I think shouldn't and I think is not arguing that the public should pay more as it were for the existing BBC1, an existing service. We should be trying to deliver, you know, that body of content for less each year. If, however, the public, and they do, and the government and they have, tell us they would like us to reduce the numbers of repeats on BBC1 and enrich BBC1 with new content, that's q, that's q. Now, what I'm saying is, as you bring that content in, if you bring in more expensive, if you bring more *Planet Earths*, more *Bleak Houses* into the BBC1 schedule, it requires a greater input of resource, but we're saying, within that investment as well, we believe that investment should be

subject to the same downward pressures on productivity, so that although, you know, you get more on that channel, you know, more on other BBC services, you know, the actual unit cost of what you're doing, there should still be downward pressure and it should be transparent and it should be, you know, it should be audited and everyone, licence payers, government, the industry should be able to see exactly how well or badly we're doing on this parameter.

**Margaret Exley:** But can I just come back on a question then, because I think we're getting to the heart of the issue here. As I understood it, you said that some of the rights questions were going to go away, sports for example, and that we're seeing, aren't we, a move into pay per view and subscription and less on advertising, so this whole notion of the market hotting up in terms of war for talent may actually not be the picture we're seeing, so on the one hand that speaks to input costs. In terms of output, clearly there are demands for quality and clearly there's a very good and compelling vision in the White Paper about what's required, and it is a demanding picture. On the other hand, the quality is clearly established and recognised and celebrated, as we've said, so I think the question for me that's outstanding is, so what's the argument for the increase then in terms of input costs, if the quality is good, if the market is not as hot as it was, if there is this shift in the market as we've seen, if there is a potential for cost reduction as you've said, then what's the argument?

**Mark Thompson:** Well, I mean, firstly one particular point to make is that although clearly in terms of, as it were, consumer markets, the subscription content market and the advertising funded content market and indeed the licence fee funded market are all separate. In the factor market for rights and content, these markets cross over each other. The comedian who would rather as it were make money from a pod-cast or from an appearance on a pay TV channel is no longer available to work for a free-to-air channel, so in the factor markets, you're still seeing extensive crossover, and indeed I would say specifically one of the things you will see over the next year or so, we're beginning to see it already, is new pay content competitors arriving and competing as it were in the rights factor market with existing players, but I think what we're saying, I think all we're saying is that one of the pressures the BBC will face in this period is certain kinds of rising cost. You can argue about the quantum, that's what this debate is perhaps partly all about. The BBC is recognising that it has to absorb those. We're saying that our ability to achieve productivity gains has to be seen in the context of some of these pressures on us. The reason that we need a licence fee which goes up in real terms is not because we need, as it were, a lot more money to produce what we're currently doing. It's because we're being asked to do a great many other things as well, we're being asked to improve the quality of what we're currently doing across all of our services. There's no suggestion in the White Paper or anywhere else of a BBC service, a fundamental service that the public don't want or which will be terminated. There are also infrastructural costs, so the reason that you need an RPI plus settlement is not fundamentally about super-inflation, it's about the new demands that are being made on the BBC. All we're saying is our ability to fully fund that ambition is to some extent constrained by issues like super-inflation, but taking it together, in terms of, as it were, the core propositions from the BBC, the BBC is saying it

can nonetheless pay for around 70% of that through becoming more productive in various ways.

**Lord Burns:** Thanks very much. I'd now like to throw it open. I think we may actually have a couple of microphones, someone down here.

**Audience Q:** Andrew Yates from the Education Recording Agency. The debate is about, a lot of it today is about the way that the BBC can grow and provide new and additional services, and that the licence fee settlement will accommodate that. On the contrary, other areas of business are constantly looking at evolving and changing the services that they provide, cutting back in some areas and providing new substitution services. My question relates to the effect on the market-place that the BBC will have if they're constantly adding new services that are perceived as being free to the consumer. How will that effect us educating the broader consumers to accept a new commercial world where increasingly they will pay subscriptions for the services that they want to choose to get, so that they really get innovation and choice from the consumer prospective.

**Audience Q:** I just want to address the issue of super-inflation. Football's a very good analogy and we might find out this afternoon whether there's a bit more super-inflation in football. But what changed in football wasn't just the new revenue streams. It was a change in the market structure, in particular the Bosman ruling on players and the ending of contracts which were a bit like slave contracts. Football moved into the 20<sup>th</sup> century. So it's actually both new revenue streams and market structural changes, and I think it had a lot on new possible revenue streams, but I just want to give a list of candidate things that could possibly cause super-inflation in the future. I take note of you on whether they will. Firstly a move from what I would call differentiated competition among major networks, the more head-on competition. To put it plainly, is Channel 4 going directly for ITV's audience where usually it didn't. That could cause super-inflation, to take a view. Beyond that a general shift in programme priorities is the appetite of ITV 2, E4 and Channel 5 acquisitions going to have an effect on the acquisitions market, whereas previously you had a kind of networks had original programmes and paid TV had acquisitions. Thirdly, risk aversion. John McVay, you mentioned this. People are more risk-averse, they pay for the talent to give them the guaranteed hit or the format that works. The person who owns the format that works has bargain leverage. Next a change in the structure of supply of Indies. Indies have been found not to have much bargaining leverage, that's why Ofcom and others intervene, but if all the interventions are successful, in five or ten years' time they might have some more, in which case that would have an effect. And lastly the globalisation and convergence of talent. Ricky Gervais is actually well-known in America now, and is asked to go on American chat shows as well as UK. One of the penalties we pay for the success of the UK TV and film talent industry is actually we are in a global market, not just the global TV market. There are a lot of British TV actors who are now doing films, and it won't be long before the MSN's of this world, or indeed the subscription radio companies are after that key talent to drive

their businesses. So, that's just a list of possible candidates, I take a view on what the effect will be.

**Lord Burns:** OK. I'll just have one observation if I may of my own there. I think we always have to distinguish in these things is between what is happening to the distribution within industry and what is happening to the average within an industry, because what we're seeing in all sorts of walks of life is the distribution as being stretched out, and the people who are at the very top are receiving what some people think of as disproportionate but a quite large remuneration, but nevertheless the average is kept in check because everyone else is being squeezed because there is only a certain amount of resources to go round, and if however you decide that every time you see the remuneration to the people at the top going up, you think that there has to be an increase in the amount of resources that go into that market, you are inevitably also going to push up the average because you're taking away the pressures, to put downward pressure on some of the costs elsewhere, and you know, I mean, this is a classic issue about inflation. And you know, I can well see, and you know, be quite persuaded as is happening in all kinds of markets, that the distribution is being pulled out. I remain cautious as to whether that means that you've therefore got to assume that the average also rises at that same pace, and that surely must have something to do with the amount of resources that is being pushed into that market. Now, that's my bit. I would like to, at the back.

**Audience Q:** Thank you. Robert Beveridge, Voice of the Listener & Viewer of Napier University, Edinburgh. Anne Bulford asked for transparency in relation to funds allocated to the BBC for digital switchover. I agree. However, you went on to express a concern that there should be no leakage of these funds into the rest of the BBC. The problem is actually, and the danger is precisely the opposite. The BBC is required to drive and largely fund digital switchover, and the overall cost for this is by no means clear at the moment, and not only that, but the BBC I understand may well be to ask or require to help to fund currently profitable Channel 4's transition to digital switchover, so the main problem that I see at the moment is that we do need transparency in order to ensure that the BBC does not subsidise digital switchover government policy and Channel 4.

**Lord Burns:** Any other contributions at this stage?

**Audience Q:** I'd like to ask a question, sir. I'd like to ask a question of Mark Thompson, and first of all, can I say thank you to everybody who's talked about ring-fencing because that was one of my major concerns, and I think if that ring-fencing is absolute, and thank you for nodding to that, Mark, then I think it takes it out of this question and answer please. We heard a lot about market uncertainties, but there is one certainty about the advertising market, is that it all comes out of the same pocket, and speaking on behalf of everybody else, it's mine, which means it's limited, and in a market which is becoming more diverse, thanks to the ring-fenced initiative of providing more channels and so on, my question to you, Mark, is how can you justify getting a larger proportion of my RPI-linked pocket than you are getting at the moment

simply on the basis of being the BBC, because that's what it means. It means that they will get less if you get more. It's my pocket, RPI-linked.

**Lord Burns:** Are there any other points?

**Mark Thompon:** Shall we begin with the pocket perhaps? I'm not going to presume to talk about your pocket but household income typically grows not in line with inflation but in relation to the growth of the whole economy, GDP growth, and over this last 6, 7-year settlement, what's happened is the licence fee's gone up by 1½ per cent above inflation. In fact the economy's grown faster than that, and as a result, the licence fee as a proportion of disposable income has declined and it's declined not just for average households but for the lower income households too. For the poorest 10% as a burden in terms of household income, the licence fee's gone down. If the BBC was to be successful, I mean, there's some components target we're not quite clear on, but our analysis taking reasonable Treasury-based assumptions about future GDP growth was were the BBC to get the kind of settlement it's talking about now, the licence fee would certainly grow in real terms, but it would continue, would continue to decline as a burden, as a proportion of disposable household income, not just for average households but also for the lowest 10%. So, you know, I understand the headline numbers are only going at real terms. As a burden it should continue to decline. Just to say, I do believe that the industry costs of digital switchover, the, you know, marketing costs of digital UK, any other industry costs and indeed the sum of money eventually agreed to support so-called targeted help for disadvantaged groups in DDT should be ring-fenced. I mean, that cuts both ways though. That's partly because I think we also need to make sure we protect the licence fee that goes to BBC services. I think we'll find it very, very hard, I mean, I think we'd all have to go into witness protection programme, if it became clear that there was a transfer of value out of the Radio 4 programme budget for example to pay for digital infrastructure, so I think ring-fencing is quite important and transparency is important for both reasons. One final quick point from me. You will see and you already have seen reprioritisation, in other words, you know, should the BBC look at ways of moving its existing resources around rather than just always asking for more money? You should. Look at acquisitions in television. The television, BBC television, is far less reliant on acquisitions than it used to be. I mean, a generation ago, it's an extraordinary switch out of acquisition. There have been a number of big recent occasions, *The Simpsons* is an example, where the BBC didn't lose *The Simpsons* in an auction. There came a point where the BBC decided it could no longer justify competing for it. Elsewhere on the BBC you've seen the shutting of a dozen of the World Service's radio stations to pay for a new Arabic television service. You will see the BBC trying to move money around to deliver its public purposes more effectively, but what I'd say to you again, this rings out a ...? all of the research that's been done, DTMS's consultation, Ofcom's work, our own work with our licence payers is the public for the most part passionately value the services we currently provide, and we can't simply willy-nilly either shut down or massively reduce the budgets of existing BBC services without profoundly disappointing the public. So we should do what we can with progressive, continuous efficiencies. That job's never done, it's

building the Forth road bridge, we'll never find an end to looking for productivity, and where we can, we should also look for where we can place our bets with the licence fee more effectively, but if you want the scale of ambition captured in the White Paper, those two things alone will not achieve it.

**Audience Q:** Can I just make two points as quickly as I can.

**Lord Burns:** Very quickly.

**Audience Q:** First of all, I believe cross-licensing should be cost related because it should work two ways, so I really can't find it in my heart to give you a lot of credit on that one, and secondly, yes, if you maintain the burden, then that makes sense provided you're maintaining your market share in a game which has more players, and I'm not sure as a licence payer that I agree with that objective. I'm not sure about that, I would need time to think.

**Lord Burns:** Thank you.

**Phil Riley:** Chairman, I just wanted to just try and question whether there was an inexorable linkage between increasing quality and increasing cost. I'm not actually sure there is, and particularly picking radio, I just think Radio 2 which is the particular bugbear of the commercial sector, as everybody knows, if you think in the last six or seven years, *Drive Time*, we've gone from John Dunn to Chris Evans, there's certainly been an increase in cost but I'd question whether there's been an increase in quality.

**Lord Burns:** Getting too personal here. Tim?

**Tim Gardam:** I'd just like to pursue this point about the cost of quality and Mark's answer to one point very clearly, which is about reprioritisation, but clearly the justification of the figure of £1.6 billion is going to be the most sensitive part I think of what we've been talking about, but given your presentation, the BBC's presentation says, you know, *'Investment in new British programmes will be coming under pressure. Though there is self-help for the commercial broadcasters, they will have less money to invest.'* I understand that the licence payer wants more high-quality programming, but are you saying there will be an increased differential between the quality of programming the BBC is doing and that being done by anybody else, and for that to take place, there has to be further investment because if the amount of money going into programming is going to lessen from what we used to call, you know, the public service commercial broadcasters, I think it's difficult for the BBC to be convincing that they need that money to maintain that level or that differential of quality.

**Mark Thompson:** If I can just respond to that. I mean, perhaps we should leave detail of the debate about quality content to the session on the future proposal, we'll have it out now if you'd rather, but I suppose what I want to say is this.

**Lord Burns:** I think, as Tim says, in a sense this session is about in some ways is about the £1.6 billion, the next session is about some of the other ...?

**Mark Thompson:** OK, very good. Well, if you take the example of the two children channels I mentioned or you could equally take the BBC 1 peak time schedule, I want to say at a more basic level that one of the things that we've been charged with doing in the White Paper is ensuring that all of the BBC's programming meets actually rather more clearly specified public service goals of which quality is one. There is a very strong injunction on us not to pursue acquisitions or to use them too extensively in peak time. There's been in the Green Paper rather than White Paper an injunction not to indulge in too many low-cost factual format programmes. There's also both strong, from the government and also from the licence-paying public, a strong view and indeed the government have set an objective for the BBC to reduce its reliance on repeats on BBC 1. On the contrary, the BBC's asked to deliver more high-quality drama, comedy, specialist factual programmes and so forth, and we're trying to do that on BBC1. Now, if you make substitution or mixed changes on BBC1 of that kind, there is a cost, and you know, given that, you know, we heard from Steve an episode, typical episode of an original UK drama, you can argue about exactly where today's as it were floating averages but £700, £800,000 an hour. If you look at the scale of what we think we need to do with our children's channels, if you look at some of the improvements and ways we want to strengthen our journalism, the idea of spending across all of the BBC services which, you know, are used by something like 95% of the UK population every month, the idea to do all of those things, you should inject another £700,000 a day, actually I believe is not disproportionate, and let me tell you, you can relate it directly, directly to what licence payers have told us, have told Ofcom and told the DCMS they want, and I would say in terms of licence payers' priorities from the BBC, quality content comes number one and it comes ahead of some of the BBC's own aspirations, for example the move to Manchester, and I believe it comes I suspect ahead of some of the government's aspirations, for example the provision of targeted help, boxes to disadvantaged groups, so in my view quality content is critical and it's a big part of what the BBC can do.

**Lord Burns:** Is your case basically what the White Paper is saying, that things that it is asking you to do in sort of all cases are more expensive than the things that you've been asked to less of?

**Mark Thompson:** No, but can we just remind ourselves that what the BBC's saying is 70% of what it believes it needs to do, it can fund through its efficiencies. Now, depending on how high you propagate the numbers, you can say that the BBC can afford, it believes, to pay for all of its improvements in quality content through efficiencies, so it depends on exactly, you know, the overwhelming majority of the list of things the BBC believes we deliver the White Paper vision, it believes it can achieve 70% of it though efficiencies, so you know, you can argue about what the list is ...

**Lord Burns:** But the way that you were describing it earlier seemed, I mean, your basic argument is that the things that you are being asked to do more of

are going to be more expensive than the things that you are being asked to do less of.

**Mark Thompson:** Yes, because they involve mixed changes. Within a particular category, within let us say the category of costume drama, should the BBC be looking to deliver as good as or better costume drama at a lower per unit cost? Yes, we should, so should we be trying to see if we can make the programme that comes after *Bleak House*, *Little Dorrit* we think but we'll see, should we try and make that at a lower cost per hour? Yes, we should. We should try and find technology and other ways of doing that, so that's what we need to do. We need to do it with every genre, but if you start changing the genre mix so you're taking out repeats at £10,000 an hour and replacing them with....

**Lord Burns:** oh yes, I see.

**Mark Thompson:** Even the most efficiently made costume drama in the world, it's a massive increase in budget need.

**Lord Burns:** But what about some of the issues and, you know, the programmes that have been going head to head with commercial television which it is being suggested there might be?

**Mark Thompson:** Well, if I may say so, we've had certainly in the field of television, many fewer complaints about if you like, in quotes 'excessively competitive scheduling or excessively competitive commissioning' than we've had actually for many years, but what I would say is that what audiences are responding to on BBC1 and BBC2, particularly BBC1, are programmes like *Super Volcano*. You know, they are some of the most expensive kinds of programmes that we make. *Dr. Who*, you know, we haven't had a very high cost science fiction drama in our Saturday evening schedule ever. It's a new addition, audiences are loving it, but you know, it's obviously expensive to put there. On radio, to be honest, I think it's a different debate. It's not fundamentally, in my view, and of course we can talk about, you know, fees for artists and so forth, but I would say what's happening in radio is that BBC radio has a different tradition and has different objectives than commercial radio, and you know, the inputs for, for Classic FM and for Radio 3 are fundamentally different. Radio 3 is focused on a very, very large investment in live music, we support five orchestras and many other music groups. We commission a vast amount of music. We play, more than half of all the music played on Radio 3 is either live or specially recorded. Classic FM, which I think is an outstanding success story in many ways, is a very different proposition, has a completely different cost structure, and I think that my challenge back about radio is I think that, you know, like for like, again we would hope, you know, to find good comparisons in the world of radio, but I would just say in the world of radio, it's quite hard to find like for like because there's no equivalent of Radio 4, there's no equivalent of Radio 3 and so on, and even Radio 1 and Radio 2 which I know are the most sensitive ones, I would argue, they've become more different from commercial radio in recent years as they focus more on speech, more on some built programming on

Radio 2. I think the difference in terms of distinctiveness between Radio 1 and Radio 2 has actually grown over the last five or six years. Now, what is true is they've been very successful with audiences, but again I, I don't want to make a complete apology for that.

**John Creswell:** I'm interested in a couple of points. I mean, I hear lots of Mark's arguments and I agree with a lot of them about the quality content the BBC does provide, *Bleak House* is a great example, but I come back to this transparency thing really which is, you know, a lot of good ideas but I can't quite grapple with what it is we're going to get, which is actually setting out a remit and a, if you like, in our terms a licence commitment of what we do and how and where we're going to spend our money, which then could be benchmarked against where you're going to spend it, so if you're sitting here saying on the one hand earlier you said I think the cost of the BBC 1 schedule will come down, I think that's part of one your earlier answers.

**Mark Thompson:** As it were, the existing content of BBC 1, but you then add new content in to enrich it.

**John Creswell:** OK, which is fine, so if you're saying actually you're sitting here committing that you do another 30 hours of costume drama on BBC 1 and that's going to cost, you know, take out the substitution costs and add it up, you can give that a tick, and then you say, 'OK, well, where's the rest of it going?' It's still, it's that transparency thing that I still really, really struggle with. And one other thing. Could I just ask about Manchester, 'cos in Michael's opening address he said Manchester was part of the BBC's efficiency drive, and you would think that's quite right, taking people out of the most costly centre in the UK and moving them to Manchester must be efficient, yet it's costing £400-odd million. Where's the displacement cost? There must be a saving from moving a thousand people there, you know, and there's a lot of public money going in, I'm sure you get rent-free periods and everything, and I can't, you know, again 400 million to move people to Manchester, if you want to get more commissioning out of Manchester, why don't you just say, 'We'll spend 15% of our budget in the northwest.'

**Lord Burns:** I think we're going to have to go into just a little bit more detail about, you know, where you're going to spend the money.

**Mark Thompson:** Well, there's two different things. I mean, let me focus first of all on, if you like, quality content and more broadly content spend. What's proposed, but it's worth again spelling it out because perhaps we haven't done it clearly enough, what's proposed is that each BBC service, BBC1 is a good example but it'll be true of every BBC service, will have a service licence, and the intention of the service licence, and there will be public consultation on the nature and the detail of the service licences and everyone in this room will have a chance to comment on them, will set out far more clearly than has been set out before what the key characteristics and the fundamental remit of the service is. A budget for the service will be attached to the service licence, so you can get a sense of how much of the licence fee the BBC intends to spend on each public services and you'll be able to track

and see shifts in that spend. I hope that, you know, what will happen is that in dialogue with the BBC Trust we will shift funding across services as our understanding of our public purposes develops and as audience behaviour changes, so I absolutely think these things should evolve over time, but at any one time there will be a great deal of clarity, more clarity and the services licences will be more clear and more specific than any commercial licence equivalent. People will be able to see very clearly what's intended and where the money's going to go. Now, Manchester I think is a very different part of the forest but let's go to Manchester. Manchester is a vision for doing a number of things. Creating a broadcast centre from scratch in a way which will deliver a large amount of BBC content which will also we hope become the nucleus of something very exciting for the creative industries in the Manchester area, in the North West, across the whole of north of England, which will have very significant impact in terms of inward investment and in developing these interests in this part of the world. The business of moving a very large number of employees, we're talking about the centre which is going to ultimately we believe have more than 2000 people, the transitional costs of moving a very large number of staff and of developing with partners and indeed I hope in partnership with stakeholders and I hope in partnership with ITV, it's going to be an expensive business during the course of the next Charter. Ultimately I think you're right. I think that what will happen is, doing this in the Charter that follows the present one will lead to long-run savings for the licence payer, because I believe for a whole variety of reasons, because we will be building from scratch and because, you know, as London weighting will work its way out of the system in due course, and that overall there will be some labour savings, I believe that it will be, it will deliver content at a lower cost per hour, radio, television, web and so forth, than we could do in London. So it will lead to savings, though I believe as we build it out over the period of the next 7 years, it will not lead to savings, it will require net investment. But the point of Manchester is about spreading investment of the BBC across the UK, it's about inward investment into the creative industries. I hope that it will see a great burgeoning of the independent sector across the north of England. We will minimise the costs and we are trying to minimise the costs by working with partners, and I think we have some potentially very exciting proposals developing. We expect to take, now that we have a short list of two candidates for the site and two very detailed plans, to take more detailed plans to our Board of Governors in June. The moment we can, we'll be sharing those details with the government as well so they can build, as it were, absolutely up-to-date details of the Manchester vision into the negotiation for what level of funding the BBC should get.

**Lord Burns:** But when you make the adjustment for the one-off costs of the move, you expect this to be, in quotes, 'an efficient move', it will save costs in the longer term.

**Mark Thompson:** Yes. I mean, the issue is, you know, as you can imagine, it depends on exactly where you get to with some of the elements of the move is the issue of pay-back and the issue of cash outflow in this next period.

**Phil Riley:** It is staggering that it's going to cost £200,000 per member of staff to make that move. When you think about it in those terms, it's an enormous amount of money.

**Lord Burns:** OK, microphone please.

**Audience Q:** Thank you. As one of the few organisations that's represented on the BBC's North Forum looking at the Manchester move, I think perhaps I can make a couple of comments. There are some crucial elements of this move. One is about building bridges and building communities in an area where perhaps the BBC has perhaps been weaker rather than stronger, of reaching audiences which again traditionally hasn't reached perhaps as strongly as in other places, and also that we haven't really mentioned very much today so far local and regional output, and I think it's important to say that arguments have been made by other broadcasters that this is something they need to come out of, and audiences want more of, and the BBC is the natural deliverer of that, and I think there are costs that local and regional audiences are willing to pay. There's a very good local television experiment going on in the Midlands at the moment, which is offering very exciting opportunities for local to participate and broadcast and get involved, and that sort of thing rolled out across the country and particularly in the north of the UK I think are very important things that we need to bear in mind and need to be built into the costings.

**Lord Burns:** OK. Got someone here.

**Audience Q:** Nick Toon from Channel 4. Just picking up on the point of super-inflation, just to address Mark Oliver's point about convergence and head-on competition between Channel 4 and ITV, in fact we've been conducting tracking surveys for the last five years, asking viewers to identify which channels are the more innovative, diverse, where they expect to find different content, and the gap between Channel 4 and all channels, but in particular between Channel 4 and ITV is greater today than it's ever been, so I don't know whether we have to be that worried about loss of differentiation in terms of competition. Just turning to the BBC's concerns about super-inflation, inflationary costs coming out of the indie sector, isn't one way of addressing that for the BBC to set parameters for the operation of the WOCC, that means that it does not simply increase its independent commissioning by defaulting to using the biggest, most successful talent-based London indies, but rather that it incentivises itself as an organisation to invest in the widest possible range of independent production companies from all across the UK, different sizes, different types of companies, start-up companies, etc., which would help to address that kind of talent whole issue, which is something Channel 4 does, spending 30% of its programme budget outside London but would significantly be assisted by the BBC making commitments in that areas.

**John McVay:** Could I ask that 'cos there are clearly now negotiations with the BBC about creating the WOCC. You know, I represent 850 companies from across the UK and it was one of the undertakings which the Trust will

report on is the diversity of supply within the work, and one of the key commitments the BBC gave was that there'll also be the same range and diversity of programming to be competed for within the work as there is for the independent quota. Now, those are two key principles. Without those, we would never have agreed to the WOCC, and they are really down to the Trust now when it reports to give in to us and indeed to many others that the BBC has made a commitment to that.

**Mark Thompson:** I just want to say, I mean, I think one interesting difference between the way we're thinking in the BBC today from five years ago is we want to do this in partnership with you guys and with ITV and the other broadcasters. I mean, the more we can work together outside London to create really strong critical masses and with some bigger companies as well as smaller companies outside London, it's good for all of us because it increases diversity of supply, but it's also incredibly good for the broader development of the creative industries in other centres around the UK.

**John Creswell:** I, you know, fully support that. I think that the rationale about my questioning was when ITV merged and it upped its out-of-London commitment, it pushed another £60, £70 million pounds out into the regions, you know, I think one of my concerns is there's a lot of money going into infrastructure, that the viewer or listener won't necessarily see. Was there a different way and did the BBC look at a different way and say, 'Actually what we want to get is a lot more regional production and creativity and vitality in centres of excellence.' Therefore if we take all our money coming in the top and said, 'Right, we'll dedicate to spend that in the market-place,' whether that's independents or in-house, whatever, you know, we'll just say, 'Right, we'll allocate, you know, 15 more per cent of our spend into the North West,' would you have got the same element. It's still amount of money just going on programming rather than infrastructure, and it's just that difference of emphasis.

**Mark Thompson:** Though we are trying to do that as well, a shift towards a much higher proportion of spend outside London, even if as it were the commissioning itself is still done in London, so I mean, I would say that what we're trying to do in Manchester, and there is something about physical presence and there is something about moving BBC networks and significant areas of BBC activity, but I'd say it's very much as well as looking at a better way of more broadly balancing content investment across the country.

**Lord Burns:** Mike at the front please.

**Audience Q:** I'm Emiko Terazono from *The Financial Times*. I just wanted to, more young people are spending their times on internet communities and Mark, you yourself have said, in creative futures that you wanted more user-generated content. I myself spend a day sort of surfing UT which is sort of video clips of people uploaded. I was just wondering, I mean, considering that more people will be sort of looking at non-professional content and how that would affect the cost of content in the future.

**Mark Thompson:** No licence fee at all, just let the public do it themselves, yes.

**Lord Burns:** No rights.

**Mark Thompson:** Well, I mean, I think firstly, I mean, one thing I want to say is here is another area where I think we see ourselves much more in partnership. I see us, you know, rather than trying to become flicker, I think the idea the BBC would start linking out of our sites more regularly to sites like Flickr, so you know, other people have got effective relationships with these audiences. Frankly, I think we can to some extent partner and build on that. But generally I would say that there's no evidence at all that public appetite for as it were, high quality professionally made content from the BBC's diminishing. It's rather that as it were around that, debate, recommendation, discussion, sharing are going to grow and are growing already. I mean, we know there's already a lively kind of world of illegal downloads of BBC content with recommendations and swapping of files and all the rest of it, I have to say rather charmingly some of the people who are doing this are actively, far from trying to hide, they kind of ring us up and say, 'When are you going to do your official version, we can't wait,' sort of thing, so we've got quite a friendly relationship with some of the pirates who are pirating our stuff, but appetite by the public to explore our content, to debate it, to argue about it, to blog about, all of this stuff is out there. I have to say, I don't believe generally this is going to be substitutional though, and I don't think there's much evidence in audience users. I readily accept people may spend a lot of time doing it, but in terms of expectations of what people want from the BBC, I think it's going to be one of the ways in which they enhance their experience. I mean, we've been running for 40, 50 years phone-ins at the BBC and many of our services, particularly local radio, are dominated by a kind of never-ending live conversation with and between the BBC and those audiences, and it's a rather wonderful thing. Now, I think that spirit of the phone-in and the e-mail and the text message is going to grow and develop, but I don't think that, you know, the Terry Wogan Show on Radio 2, it's the kind of programme which I know others worry about. A big part of Terry's show is about testimony, jokes, experiences, ideas, poems sadly, from members of his audience. Terry's a big part of it as well though, and you take Terry away, you haven't got that programme, so to me it's a way of broadening and enriching our output and I think it's a fantastic moment in broadcasting, but I don't think it's substitutional.

**Lord Burns:** Michael, there has been raised quite a lot of times about, you know, how the government's processes are going to work to ensure that the money is spent, is set out in the bid and you know, particularly the issue of our digital switchover, and I think one or two other areas where the question has been raised as to what assurances do we have that this money in the end will go where it is that it has been asked for, and I'm just wondering whether this was a moment that it might be useful if you were to say something about how you see the new arrangements working and how it is that you're going to keep these people up to the fire really in terms of this.

**Michael Grade:** I knew I wouldn't get through the morning unscathed. First thing I would recommend anybody who hasn't done so to read the White Paper and the draft Charter and Agreement, because laid down in there in more detail than in the BBC's history are the protections and the mandates that the Trust will be required, required to carry out in order to ensure that this difficult co-existence with our private sector peers is managed much more efficiently, effectively, transparently and accountably than ever, ever before. You know, the notion, I know this sounds silly now at this point in the debate, but the notion that the BBC will not launch a new service without consulting and the Trust will not approve a new service or a significant change to an existing service, won't give that approval until it has been through the public value test, market impact carried out by Ofcom, that is very radical in the history of the BBC and is to be welcomed and is quite right, it's a much needed piece of modernisation. Within the new framework of governance, the Trust's ability to demonstrate how the money is spent and call the management, the executive to account through the service licences which reflect the public purposes and so on, will be very clear. The service licences themselves will be out for consultation, everybody will have a view, and hopefully they'll be out for consultation within the next two or three months, they will be very effective tools. They're tools that have worked very effectively in the private sector for years, through the original ITA, the IBA, the ITC and now Ofcom, it'll be very clear. On the issue, let us take for example big chunky items in the bid, digital switchover and Manchester as two chunky items. I make no comment about Manchester because neither the governors nor the putative Trust has yet approved. We've agreed in principle it would be a good thing. We need to see whether we think it's value for money and then if we think it's value for money under the plans proposed by the management, we will then decide whether we can afford it or not, but let us assume that post the settlement and the government tells us how much we're going to get, in that bid is a sum of money for Manchester as accurately as we can forecast at this stage. If Manchester were to fall over, planning reasons, some unforeseen reasons and Manchester were to fall over, that money should not go back into the central pot of the BBC and it should be returned to the licence fee payers, there's no question about that. Similarly, although it this is an academic question, I think the capital expenditure on the digital switchover should be a very easily identifiable number within the bid. If those estimates turn out to be grossly over-inflated and we manage to achieve digital switchover and all the component parts including Channel 4, including targeted help, whatever, if there's a lot of loose change at the end of that process, that money should not stay with the BBC, that's quite clear, and that should be very transparent. On editorial issues and so on, that is a matter for the Trust, not a matter for the government to decide.

**Lord Burns:** OK, thanks very much. I think we've had a good run through these issues this morning. Does anyone have anything further?

**John McVay:** I just wanted to ask Mark if, for the licence fee payer, if you haven't delivered value for money and you end up in a witness protection programme does that mean you will get rid of the beard?

**Mark Thompson:** I don't think I'll grace that with a reply!

**Lord Burns:** Thank you all very much particularly to Mark who has had to work pretty hard for his privilege of being here this morning. This afternoon we are going to move on to technological issues including digital switchover and new media, etc and to look a little bit more into how the market impact assessments will work with regard to all of that. We are due to be back at 2pm and I will start at 2pm so if everyone can be back at 5 to 2. Thank you.