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# The implications of Government proposals for Licence Fee contestability

A paper for the BBC Trust

**PERSPECTIVE**

Part of the Ingenious Consulting Network

## Introduction: Providing PSB to Digital Britain

### The context and scope of the Digital Britain report

The government's Digital Britain report sets out to "enable Britain to be a global centre for the creative industries in the digital age, delivering an ever wider range of quality content, including public service content, within a clear and fair legal framework"<sup>1</sup>. The report rightly recognises both the importance of PSB output to the take-up of digital technology – that "public service data and content play an increasingly important role in the digital economy"<sup>2</sup>; and the opportunities offered to PSB by the development of that technology – that digital change will have "a significant bearing on the public service content that, as a society, we both want and can get"<sup>3</sup>.

To make good on this ambition, the report recommends significant changes to the remit and governance arrangements of the publicly owned broadcasters. For Channel 4, the report recommends a realignment of its remit, which it believes is too "television-centric", towards one that would encourage a shift in the balance of its activities over time to a wider range of digital activities and partnerships. The report recognises that television advertising funding will be needed to support the scale and reach of Channel 4's activity, but suggests that the channel should have greater freedom to maximise its commercial revenue in television to support a wider range of 'non-linear' public service initiatives.

The report recognises the central role the BBC plays in the delivery of high-quality public service content, but again it seeks an evolution of the BBC's role. Recognising the initiatives already taken by the BBC to promote wider partnerships in the delivery of public service content, the report goes further by suggesting that a portion of the licence fee should in future be reserved to ensure the plural supply of "essential public content". The report proposes that the level at which this portion is set should be roughly equivalent to the amount currently collected for the Digital Switchover Help Scheme and Digital UK's marketing budget, which are both funded out of the current licence fee settlement and which taken together amount to about 3.5% of the total licence fee. The government proposes that this element should be sustained beyond 2012, when the current schemes end, and that this Contained Contestable Element (CCE) of the Licence Fee should be retained at that level (i.e. the monetary amount equivalent to 3.5% of the licence fee) independent of the level of any future licence fee settlement.

The first call on this funding is support for Independently Funded Local News Consortia (IFNCs) – the government's preferred option for addressing the possible shortfall in the provision of local and regional news brought about by the structural changes in the television, radio and print markets, and exacerbated by the cyclical problems faced by all advertiser funded businesses. But the government is also explicit that the Contained Contestable Element is designed to address shortfalls beyond regional news, and could be used to fund other types of essential public content in future.

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<sup>1</sup> The Digital Britain Final Report, p1

<sup>2</sup> The Digital Britain Final Report, p24

<sup>3</sup> Ibid, p135

Perspective was commissioned by the BBC Trust to assess the proposals put forward in relation to the CCE. To do this, we have sought to answer three main questions:

- How strong are the arguments for using this source of funding for IFNCs – both in themselves, and in relation to the wider policy debate about their scale, scope and remit?
- How well argued is the case for using the CCE to support other types of public service content?
- What are the potential implications for the Licence Fee system and the governance of the BBC if contestable funding is introduced as a continued and maintained element of the Licence Fee?

In assessing the case put forward in the Digital Britain report, we have been mindful of the wider potential benefits that digital change could bring about. Among these, for example, are:

- As Ofcom has previously established, truly local TV could become possible through DTT;
- Broadcast-standard audiovisual (as well as audio) content can now be made for an increasingly low cost, and can be widely distributed online;
- Innovations such as Canvas could provide ways of linking these two, furthering the success of existing online platforms such as the iPlayer in narrowing the distinction between TV and the PC, bringing online content ‘into the living room’.

Our emerging conclusions suggest that there are significant challenges that the introduction of a Contained Contestable Element will need to confront and overcome. In particular, it will need to ensure that it does not impose rigidity in a system that has profited from the flexibility inherent in being able to match resources to priorities within a single organisation, and which has given content creators significant freedom to innovate within, and beyond, genres.

We are struck that the consultation paper published by government in July focuses narrowly on the arguments for sustaining local and regional news: our conclusion is that using the licence fee to achieve this goal engages a much wider set of both constitutional and organisational issues, which we begin to identify in this report and which we believe will need fuller analysis.

### **Scoping the debate about the provision of public service content**

In response to increasing audience fragmentation driven by the availability of new services and new platforms, the government will always want to judge the appropriate balance between two broad approaches to the provision of public service content:

- Guaranteeing a plurality of suppliers of public service content to ensure that it is available as widely as possible and in forms that are likely to attract all viewers;
- And guaranteeing the scale, impact and reach of the existing public service intervention, both broadcast and online, which is best achieved through strengthening the remit, and

ensuring the resource, of a converged and coordinated supplier of public service content, with stable, multi-year funding.

The probable effect of taking a portion of the licence fee and using it to sustain additional providers to the BBC – rather than simply using the public intervention to guarantee the supply of a particular type of essential content – will be to reduce, over time if not straight away, the scale of funding currently available to the BBC to fund its current activities. Put simply, by locking plurality as a concept into the licence fee, the range of services it funds is likely to diminish unless the level of the licence fee is increased.

Against this background, the consultation must fully assess the ways in which this intervention might strengthen the overall provision of public service content, and avoid the potential danger of weakening the ability of the BBC to continue to provide and innovate across all genres.

Although it could be argued that any such change in policy does not necessarily mean a change to the way the BBC itself is structured or governed, it is nevertheless clear that the creation of a separate fund to commission public service content paid for by the TV Licence Fee would have profound implications for the way in which public service objectives are set, and how funding is allocated at the highest level to meet those goals.

We do not in this report question the value of plurality itself: we accept that it has in the past delivered, and continues still to deliver, significant benefits to audiences both as citizens and as recipients of high quality content. Our starting point, however, is that the government's proposals are to use its funding intervention to achieve plurality, rather than – as is typical with public funding – to act as a guarantee of supply of certain types of essential content. It is the arguments for, and consequences of, this policy proposal that we examine in the following report.

In this context, we note that the government has itself decided against any of the measures put forward as potential funding options for future provision of public service content. Ofcom's analysis in its most recent PSB review<sup>4</sup> suggested a number of ways in which government could choose to fund future public service content.

- Privileged access to broadcasting spectrum could be reassigned at the end of the current licences, to ensure the value of this public asset is being maximised.
- BBC partnerships could be developed with the other public service broadcasters, to help address the commercial pressures the latter face. The opportunity of cost efficiencies and synergies through deeper partnerships or combinations should be looked into.
- Direct government funding, as is already used for public service broadcasting in the BBC World Service and S4C, could be extended further.
- Funds could be raised through a new industry levy, as used in some other countries.

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<sup>4</sup> Ofcom's Second Public Service Broadcasting Review: Putting Viewers First, 21 January 2009

We note that the Government has specifically excluded the possibility of funding from the Exchequer<sup>5</sup>, but there is no explicit discussion of the merits of any other possible source of funding – including, for instance, the option the Government has of replicating the way foregone spectrum revenues have supported public service content, by using the payments made by service providers for use of valuable digital spectrum to fund the future provision of public service content.

### **The structure of this report**

The analysis that follows falls into three sections:

- In the first section we assess the arguments around the need to use the Licence Fee to guarantee the plural provision of local, regional and national news;
- In the second section, we assess the arguments around the implications of using a CCE to fund other genres of at-risk PSB content; and
- In the final section, we consider the wider implications in relation to administration and governance that will need to be addressed in the current consultation.

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<sup>5</sup> Digital Britain Final Report, p142

## Ensuring support for local, regional and national news

In this first section, we assess the strength of the case made by the government for using the licence fee to fund local, regional and national news from independent and commercial providers.

The Digital Britain report describes how the development of digital communications and platforms has brought challenges for some commercially funded broadcasters. It states that these challenges include: the dwindling of advertising revenues accruing to, among others, PSB broadcasters; and the implications of this for the continuing provision of some PSB content, particularly of regional news. The report assesses these developments against a policy goal that it is “important for civic society and democracy for people to have a range of sources of accurate and trustworthy news at all levels, local, regional and in the Nations as well as UK-wide and international news that is guaranteed, beyond market provision”<sup>6</sup>.

The Government has therefore concluded that plurality in the guaranteed supply of local, regional and national television news is an overall priority for continued intervention to deliver public service content. While the report does not fully address matters such as the inconsistency between stated viewer demand for local television news that Ofcom found in its research for its recent Public Service Broadcasting Review<sup>7</sup> and actual viewing figures for this programming<sup>8</sup>, there is nonetheless a case to be made for plurality in local news, as there is in national news. This case advocates plurality as a democratic safeguard (rather than to ensure volume of content), and although there may be something to be said for the growing contribution to plurality from local sources on other media such as the internet, it is nonetheless reasonable to contend that a healthy democratic system will be strengthened by the guaranteed provision of local news on a scale to compete with the BBC, bound by the same rules of accuracy and impartiality, and that this might not be delivered by the market alone. At the same time, a further issue not addressed in the Digital Britain report is what exactly people regard as ‘local’ news: for example, is it literally news ‘from a local area’, or more ‘regional’ news? And how do these opinions differ across Wales, Scotland and Northern Ireland?

This policy consideration also played its part in the decision by the Trust, supported by the market analysis carried out by Ofcom, that further Licence-Fee-funded BBC local video services risked stifling the planned investment by local newspaper groups in their digital developments, while failing to serve the target audience fully.<sup>9</sup>

Following the publication of the Digital Britain Interim Report earlier this year, the OFT and Ofcom were charged with investigating whether the way that merger investigations were carried out was still appropriate and relevant to today’s local media market:

*ACTION 14 To inform whether any change to the merger regime is yet desirable or necessary in relation to the local and regional media sector, the Government will invite the OFT,*

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<sup>6</sup> The Digital Britain Final Report, p141

<sup>7</sup> Ofcom’s Second Public Service Broadcasting Review: Putting Viewers First, 21 January 2009

<sup>8</sup> For example, see the research annexes to New News, Future News, June 26 2007

<sup>9</sup> See BBC Trust, Local Video: Public Value Test Final Conclusions, November 2008

*together with Ofcom and other interested parties, to undertake an exploratory review across the local and regional media sector and make appropriate recommendations.*<sup>10</sup>

The OFT looked into whether the existing UK merger regime was still appropriate, given the wholesale changes in, amongst other things, local and regional advertising markets that had come about in recent years, with the move of a substantial amount of classified advertising to online. In its report<sup>11</sup>, which focussed on UK local and regional newspapers, the OFT made the following points:

- The OFT recognises that the UK local media industry is facing long-term structural changes (due mainly to the sharp downturn in advertising).
- However, the UK's merger regime remains evidence-based and any investigation will therefore, by definition, seek to find the economic reality in the relevant markets underlying the proposed merger situation. Increased competition from the internet would therefore be reflected in the market definition stage of any such investigation.
- The OFT also pointed out that the current regime already recognises 'failing firm' arguments in choosing the correct counterfactual in its investigations, as well as consumer benefits gained through a merger.
- The OFT therefore concluded that there were no changes needed to the UK's media merger regime. The report also gave examples of the types of evidence it would regard as useful in its future media merger investigations.

The OFT were therefore confident that the merger regime would not stop any local media mergers on the basis of previous assessments of local advertising markets.

Ofcom, as requested in the Digital Britain interim report, is currently undertaking a review of the UK's cross-media ownership rules, as part of its statutory duty to review periodically the operation of the UK media ownership rules. The review<sup>12</sup> is taking the form of a consultation, in which Ofcom makes the following proposals:

- Liberalising the existing local and national radio ownership rules, in the hope of improving station viability;
- Liberalising the local cross media ownership rules, to allow local media to respond better to market pressures;
- Retaining the rules on: national cross media ownership; television and radio licences ownership; the appointed news provider rule; and the media public interest test allowing the Secretary of State to intervene in media mergers on public interest grounds.
- Ofcom also recognised the need to review the ownership rules regularly in the light of market developments and plurality of outlets.

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<sup>10</sup> Digital Britain: The Interim Report, January 2009, p47

<sup>11</sup> OFT, Review of the local and regional media merger regime: Final report, June 2009

<sup>12</sup> Ofcom, Media Ownership Rules Review: Consultation, 31 July 2009

There is a substantial amount of activity taking place at an official level to suggest that the policy landscape itself in which the discussion of local news media exists is far from fixed. We list a few of these and their implications below:

Intervention	Details	Comments
<p><b>a. Ofcom’s Review of Media Ownership Rules was asked by Government to focus specifically on local cross-media ownership between radio, newspapers and television.</b></p>	<p>Relaxing the rules governing cross-media ownership is intended to allow local media to achieve cost efficiencies and to move towards multi-platform delivery of local news and information, with the ability to offer cross-platform advertising.</p>	<ul style="list-style-type: none"> <li>• Relaxing cross-media ownership rules could have an important impact on the viability of local media.</li> <li>• The Government has not waited to observe the effects on local media viability of any mergers that may result from this, before proposing further measures.</li> </ul>
<p><b>b. Ofcom are currently also consulting on the implications of Digital Britain for localness regulation in radio.</b></p>	<p>The proposals are: to allow programming sharing for regional stations to create new national DAB stations; to allow local stations to co-locate, share programming and reduce local quotas to save costs; and support the development of community radio to create a new tier of ultra-local stations in the long run.</p>	<ul style="list-style-type: none"> <li>• Reducing local commitments to a core around local news may paradoxically strengthen local news provision on radio.</li> <li>• Again, the Government has not waited to observe the effects of these measures on the viability of local media before proposing other measures.</li> </ul>
<p><b>c. The OFT conducted a review across UK local and regional media, on the request of the Government.</b></p>	<p>This review was intended to look at whether any change to the merger regime was necessary to reflect changes in the context and circumstances of the UK local media, for example in advertising markets. The OFT found the existing competition regime wholly appropriate for addressing media advertising markets.</p>	<ul style="list-style-type: none"> <li>• The Government is looking at the current state of local media as a basis for changing cross-media ownership rules, but is not waiting to observe the outcome and effects of any new merger activity before recommending other measures.</li> </ul>
<p><b>d. Trial public funding for an Independently Financed News Consortium (IFNC) model of supplying plurality in local, regional and national news.</b></p>	<p>IFNCs are proposed as groups of interested parties joining to “provide a more ambitious cross-media proposition and enhanced localness compared with current commercial television regional news”. These trials would be made with a view to testing the possibilities for commercial funding.</p>	<ul style="list-style-type: none"> <li>• The Government predicates the funding of these trials on the outcome of the consultation on post-trial contestable funding for local news.</li> <li>• The shape and duration of the trials proposed by the Government are still unclear.</li> </ul>
<p><b>e. In early 2009, Ofcom awarded the first two of around 80 possible lots of interleaved DTT</b></p>	<p>The first award was made to Channel M Television, in the Manchester area, and the second to Cube Interactive in the Cardiff</p>	<ul style="list-style-type: none"> <li>• The Government does not acknowledge these awards and their possible effects in its assessment of the need for</li> </ul>

<p><b>spectrum for local broadcasting.</b></p>	<p>area.</p>	<p>local news plurality.</p> <ul style="list-style-type: none"> <li>• The Government has at the same time proposed that pilot news consortia (IFNCs) be undertaken in the home nations.</li> </ul>
<p><b>f. In discussing possible pilot schemes for IFNCs, the Digital Britain report notes that “S4C have already done work to develop a related initiative”.</b></p>	<p>In late 2008, ITV Wales and S4C announced launched ITV Local Cymru, a Welsh-language web portal for news, current affairs, features and archive content, to provide “Welsh-language news and current affairs plurality” on a converged communications platform.</p>	<ul style="list-style-type: none"> <li>• While the Government acknowledges the introduction of the ITV / S4C service, it does not seem to take its presence or the effects of this into account in its proposals for trials in local media services.</li> </ul>
<p><b>g. The Scottish Broadcasting Commission was established by the Scottish government to review the state of television production and broadcasting in Scotland.</b></p>	<p>The Commission recommended the setting up of a new public Scottish television network. This was intended to address issues of plurality in Scotland that the Commission saw as highlighted in Ofcom’s second PSB review.</p>	<ul style="list-style-type: none"> <li>• The Digital Britain report makes no reference to the Scottish Broadcasting Commission report or its recommendations.</li> <li>• At the same time, one of the IFNC trials is proposed for Scotland.</li> </ul>
<p><b>h. The Digital Britain report invited the Audit Commission to undertake an inquiry into local authorities taking paid advertising to support their information sheets</b></p>	<p>The Audit Commission’s role does not extend to examining the impacts of specific local authority practices on commercial bodies. The scope of the study was therefore limited to studying the value-for-money of council spending on communications.</p>	<ul style="list-style-type: none"> <li>• Although this report would still offer some insight into the possible effects on local media funding of local authority advertising revenues, the Government did not wait for its completion before advocating other measures.</li> </ul>

The Government has not commented at any length in its report on most of these reports and reviews, much less explicitly considered them in its reasoning. The only clear reference in the Government’s final report is its acceptance that the relaxation of the merger regime will allow existing local media organisations to merge, including across platforms, in order to become more sustainable entities, able to operate on a continuing basis. This would “allow for greater economies of scale and a sustainable local voice alongside that of the BBC”,<sup>13</sup> through the consolidation of resources, reduced overheads and cross-promotion between media. This idea has been widely discussed in the industry, and the emerging consensus seems to be that, along with broader market definitions in merger investigations, these measures could help local media considerably to restructure for the future.

Anticipating the likely outcome of this consolidation, the report also recommends that “existing television news providers, newspaper groups or other newsgathering agencies” should be

<sup>13</sup> The Digital Britain Final Report, p155

encouraged to combine to form Independently Financed News Consortia (IFNCs) to provide sustainable local news services, both commercially and to replace the ITV services on Channel 3 licensees. Again, there have already been discussions of this idea in the industry, with the same purpose of finding a sustainable model for local media in the converged future – including the possibility of using public money, at least in the short term, to enable the necessary structural changes to take place.

However, before any assessment of the impact of the likely restructuring of the local news industry following on from these changes, the report states that the IFNC model of supplying plurality in local, regional and national news should receive funding for trials, with a view to testing, among other things, the possibilities for commercial funding. At the same time as it proposes these trials, however, the Government also states in its report that it will also create a “Contained Contestable Element of the Licence Fee used by or channelled through other organisations, primarily for news”,<sup>14</sup> to be instituted after digital switchover is finalised. This would be an amount, taken directly from the TV Licence Fee and equivalent to the 3.5% that is currently used for the Digital Help scheme and Digital UK’s marketing and communications budget, but fixed independently of the future Licence Fee proceeds, to be maintained as a contestable element for non-BBC organisations.

While it is clear that the Government has decided, in its Digital Britain report, that the IFNC model is the right one, it is clear that other models exist and need to be tested – models which do not call for long terms and sustained public funding. The Government has not taken account of the significant amount of work already being undertaken in this area, and in deciding at this stage to opt for the publicly-funded IFNC model it is effectively either pre-judging or ignoring their outcomes.

In this context, it is worth noting the recent conclusions of the independent report commissioned by the Conservative Party from Roger Parry<sup>15</sup>, on the possibility of a national network of commercially viable local television stations. This paper put forward the following ideas, on which it sought industry opinion:

- Digital switchover will release broadcasting spectrum that will allow for the creation of “several hundred” local TV stations across the UK. Ofcom analysis has already identified 81 locations throughout the UK that might possess the right qualities for local television to be economically viable.
- The report proposes that 80 “Local Media Companies” (LMCs) could be founded, each typically covering a city or a group of towns, and each combining print, online, television and radio – although chiefly based around local television, which would have Freeview carriage.
- These LMCs would be self-sustaining, with income streams from classified, display and broadcast advertising, and content sales to other media organisations – possibly including the making of local and regional news for the Channel 3 regional licensees. Costs would be kept low through the use of the latest digital production technology, and through drawing

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<sup>14</sup> The Digital Britain Final Report, p155

<sup>15</sup> Executive Chairman of Media Square plc; former Chairman of Johnston Press and CEO of Clear Channel International.

on community volunteers and industry trainees, which would also benefit the local communities.

- Plurality in local news and media would be enhanced – especially when considering the possible counterfactual of the total collapse and disappearance of local media in some areas; and the local media industry – particularly newspapers – would be able to make the transition into the digital age.

While this paper was published after the Digital Britain final report, it nonetheless suggests that other possible solutions should be assessed before deciding that public funding, whether from the Television Licence fee or from some other source, is required.

Other research into new business models for local online news and information services has suggested that there may already be very real potential for such services to develop and flourish. For example, the City University of New York's Graduate School of Journalism has conducted studies into the existing and potential delivery of information services by and for communities, with the market responding to meet the demand for local information and news, in their ongoing 'New Business Models for News Project'.<sup>16</sup> This has concluded that "a sustainable and once-again profitable future with the prospect of expanding and improving journalism by taking it deeper into our communities with increased relevance, engagement, accountability and efficiency" is possible, and that there are several possible models that such an 'ecosystem' of local information providers might take. This research suggests that such ecosystems are already established to an extent, for example, with hyper-local bloggers having audiences of about 50,000 people, making up to \$200,000 a year in advertising revenues. The research concludes that "these are sustainable businesses and we believe they are critical elements of the future of local news – a future no longer controlled by a single newspaper but instead by an ecosystem made up of many players with varying motives, means and models, working collaboratively in networks."

Comments in the Digital Britain report on the concern that there may be "large parts of the UK will be left without professionally verified sources of information" are perhaps underestimating the ability of local services to develop into marketable commercial services (not to mention overestimating the extent to which professional local media in the UK actually currently provide independent, original and fully verified stories). The conclusion that publicly funded plurality is needed to address the decline in the local newspaper industry could be said to ignore the substantial possibility for the 'organic' development of new local, and above all profitable, news and information services online.

### **Key challenges**

Regardless of the justification for the continued provision of plural sources of local and regional news, there are five key challenges arising from this proposed solution to the problems facing local, regional and National news, which need to be addressed in the consultation and the Government's response:

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<sup>16</sup> See <http://newsinnovation.com>

- **Timing and relationship to other initiatives:** The proposal to implement plurality through both a relaxation of the media ownership rules (which the industry has widely called for) and a guaranteed portion of the TV Licence Fee on a permanent basis (which it has not), ahead of any actual trials to demonstrate that the approach is the right one and that the results will serve the public service need, has to be justified more thoroughly. In this context, it seems premature to opt for the future ring-fencing of funding for local news from the Licence Fee, ahead of the results of Ofcom's assessment of options for securing local services in future.<sup>17</sup>
- **Impact on commercial funding and efficient use of public money:** If the pilot IFNCs are to test commercial funding possibilities, the specific guarantee of public funding, potentially at a level sufficient to fully fund the entire service, means that it will be essential to devise ways to guarantee that the public funding is being fully and efficiently used, and is not allowing commercial providers to profit from publicly funded activity (for example, by setting a capped rate of return).
- **Demonstrating Public Value:** The recent exercise carried out by the BBC Trust into the public value of a new publicly funded local news service, delivered by broadband, concluded that an investment of £60m of Television Licence Fee funding was unjustified on the grounds that it would fail to meet the needs of the likely target audience, while Ofcom had also concluded that the level of public funding would have a chilling effect on commercial investment. The Government needs to demonstrate how its proposals address both of these concerns, which were the result of intensive analysis and consultation across the industry;
- **Guaranteeing the benefits of plurality:** A more thorough assessment should be made of the way in which the benefits of plurality of news provision (diversity of voice and opinion) are to be secured when the funding is all from the same Licence Fee source and the content rules requiring impartial treatment of news are applied to news providers (i.e. local newspaper groups) who have been accustomed to the freedom of adopting strong editorial and campaigning approaches to local news;
- **Achieving a proper balance of priorities:** Hypothecating a fixed element of the licence fee to fund one specific type of public service content may limit the flexibility of both the BBC and the Government to address future priorities. We address in more detail in later sections of this report the governance implications of being able to address the balance of priorities for the licence fee as a whole: in relation to local news, we simply note that a requirement to supply an additional range of local news may not only take funding that might potentially be better employed in future, while at the same time locking the BBC into equal provision. Because of the protected nature of spending on local news, this could have a disproportionate effect on the BBC's ability to fund other kinds of programmes. While the idea of local news plurality may be a reasonable one, it does not automatically follow that this should be implemented through public funding – including from the TV Licence Fee – without substantially more analysis of all the funding possibilities and, more importantly, the repercussions of these.

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<sup>17</sup> See Ofcom's Media Ownership Rules Review Consultation, 31 July 2009

It is also important, in this context, to note the significant differences between the proposed method of securing local, regional and national news and the process for awarding current contracts to deliver national and international news to ITV, Channel 4 and Five – which has been cited as a comparator by Ofcom<sup>18</sup>. The contracts placed by commercial broadcasters, including Channel 4, with their news suppliers differ in two key respects:

- They do not involve public money – and therefore are subject to less oversight and scrutiny than will be the case with IFNCs, especially if public money is being used to support a part of the host’s business that reflects only a fraction of their overall activity (as could be the case with large newspaper groups);
- They have always been placed with a provider for whom the provision of impartial television news is the primary focus of their business – so there is less tension between the potentially conflicting editorial styles of opinionated or campaigning local news for print and on-line being generated in the same news room and by the same team as those responsible for broadcast.

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<sup>18</sup> See, for example, Ofcom’s Second PSB Review Final Statement: Putting Viewers First, para 9.25, p 90

## Contestable funding for wider PSB content

The Digital Britain report rightly observes that, prior to the recent expansion of audiovisual platforms, channels, and content, there was a surplus from the revenues accruing from limited TV advertising, which generally allowed for the funding of non-BBC PSB content, such as drama, investigative journalism and documentaries. It contrasts this with the current situation for broadcasters, in which advertising revenues have been dispersed, along with viewing, across the much greater range of platforms, channels and other media now available to consumers.

The report maintains that, while the commercial revenues may no longer be sufficient to support it, there is nonetheless “a clear case for continued strong intervention to deliver public service content”,<sup>19</sup> and that this should include the delivery of plurality in some genres beyond news. In terms of which genres, the report is not specific. It mentions “material for older children including online content, and hard factual and documentary”, and also refers to Ofcom having previously identified “high-end drama and original comedy and satire and more generally, content that falls under the banner of innovative”<sup>20</sup>.

As cited above, the Government proposes in the Digital Britain report that non-BBC plurality in local and regional news should be ensured through public money, with post-switchover funding being taken from the TV Licence Fee. However, while this Contained Contestable Element of the Licence Fee is intended firstly to address a potential shortfall in news (that is, “used by or channelled through other organisations, primarily for news”<sup>21</sup>), elsewhere in the report the Government states that the CCE should “support public service content, particularly in local, regional and Nations news.”<sup>22</sup> While the idea of contestable funding is introduced for the specific purpose of democratic plurality in news, it seems that this purpose changes during the course of the report itself, with the Government moving towards a more general public service content fund.<sup>23</sup>

In its section on “Public Funding for competitive provision of essential public content”<sup>24</sup>, the report talks of “gaps in market provision” for some types of PSB content, and states that “plurality in the ownership, commissioning, editorial and production of public service” is essential. It also states that plurality in news is “important for civic society and democracy” and that “this may be also true of children’s content”. The actual public policy goals behind the desired plurality of provision for news and other content may or may not be the same – whether democratic or quality-based – but this is not made clear.

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<sup>19</sup> The Digital Britain Final Report, p137

<sup>20</sup> Ibid, p137

<sup>21</sup> Ibid, p143

<sup>22</sup> Ibid, p142

<sup>23</sup> Interestingly, DCMS’s consultation paper on the future of local news provision, states that the purpose of the CCE would be “primarily to top-up fund independent, alternative providers of news (the IFNCs)”, but that it “could also potentially be used to sustain other essential public service content priorities ... if the independent provision of Nations, local and regional news should require less than the contestable sum set aside”. DCMS, Sustainable independent and impartial news; in the Nations, locally and in the regions, June 2009

<sup>24</sup> The Digital Britain Final Report, p141

There are three important observations to be made about this approach.

First, the government does not appear to have made its own analysis of the case put forward by Ofcom for the need for plurality in genres outside news. There is no reference to quantitative or financial data, to industry or consumer surveys, or to actual output figures. There is no further development on which PSB genres are seen to be in danger of under-supply, whether this is expected to be an ongoing or transitory situation, or whether consumer demand for these might eventually result in their market provision beyond the BBC's own output.

Second, and more urgent, given the nature of the Government's proposal, there needs to be greater clarity about the underlying rationale for plurality of supply. Ofcom helpfully identified the three possible benefits of plurality of supply in the first phase of their most recent PSB Review as:

- diversity of voice;
- competition for quality ; and
- enhanced reach and impact.<sup>25</sup>

These benefits were identified in a context where the Licence Fee was not anticipated to be the funding source for achieving these benefits – although Ofcom had clearly envisaged public intervention as necessary to achieve these outcomes.

Now that the Government has made plain its intention to reserve part of the Licence Fee to fund other services, a more sustained and developed analysis – of which of these benefits is to be achieved, and of whether it is the most efficient way to achieve them – needs to be undertaken in relation to each or any of the types of programme funded in this way.

In particular, the relationship between sustained volume and enhanced reach and impact needs to be explored if the Government and the public are to be sure that the licence fee is being efficiently spent. The decision to fund two services from the same source of funding is likely to be more justifiable if there is very limited overlap between the audiences of the two services: if there is significant overlap, the services will need to be either delivering very different but still demonstrably public service content, or demonstrably driving up quality.

Finally, it is worth observing that the UK is unique in attempting to use public funding to address a failure of plurality rather than a failure of volume or supply. All the other examples of public funding of PSB are designed to address straightforward market failure: they do not occur in the context of an existing public provider whose remit already specifically requires it to provide the content in question.

These are complex and sophisticated arguments that deserve serious debate in the consultation process. The UK has rightly prided itself on its unique approach to providing PSB in the past: this has guaranteed high levels of investment in innovative and challenging content. The Government needs to be sure that, by spreading the public funding part of the intervention more widely, it has retained

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<sup>25</sup> Ofcom's Second PSB Review Phase 1: The Digital Opportunity pp 82 - 83

the appropriate balance between a single, well funded supplier with a wide ranging public remit, and a range of other providers with a mix of commercial and non-commercial goals.

### Key challenges

We believe that the decision to use part of the CCE in future to supply other kinds of public service content gives rise to at least two fundamental issues that need to be addressed through the current consultations process.

- **Genres:** In which genres exactly does the Government believe there is a current need for plurality? Some are mentioned, but there is no definitive set of genres stated that require intervention. Additionally, the Government needs to be clearer about the justification for requiring plurality of supply rather than simply volume of supply, particularly in cases where there is no over-riding democratic need for a diversity of voices and opinions.
- **Reach and Impact:** How can the CCE guarantee reach and impact? Furthermore, if it achieves greater reach and impact through alternative funding, what is the continued rationale for funding both services? How much of the amount equal to 3.5% of the current Licence Fee revenues, hypothecated in the report “primarily for news”, will be needed for other genres to achieve the necessary scale of contribution?

These challenges rise from the decision to allocate money for specific genres. However, it is also the case that the decision to move to a mixed structure of public funding – where the BBC is accompanied by a fund that supplies alternative content providers – has more profound implications for the structure of public service content in future. We address these in our final section. The Digital Britain report itself does not address these questions, but suggests that there will be an open consultation on the issue. We note, however, that the consultation limits itself to the issue of supporting “[s]ustainable, independent and impartial news in the Nations, locally and in the regions”. We therefore believe it is important that the questions pertaining to the wider uses to which the CCE might be put should be addressed within the same consultation framework.

## The wider debate on contestable funding and its consequences

The case for introducing a contestable element to the Licence fee fund is worthy of full and thorough debate: it is not clear that this case has been adequately made in the Digital Britain report. In addition to the specific issues raised in the foregoing sections, any such debate should address two fundamental challenges.

### **What are the potential impacts on flexibility and responsiveness represented by contestable funding mechanisms?**

One hallmark of an approach to PSB provision based around an organisation of scale and reach is the potential for flexibility in setting priorities and strategies for reaching them. There is a danger that, in adopting a genre-led approach to contestable funding, this flexibility will be at risk. The consequence of a CCE designed to achieve plurality will be to require the BBC to maintain a matching requirement to meet the specific goal of plural supply in the genres chosen for contestable funding. While this may be desirable for sound reasons of reach, impact and quality, it will nevertheless impose a significant degree of external control over the BBC's decisions about where and how best to allocate its own funding.

Beyond the potential impact on the BBC's own decision making, there are other risks that such a system would need to avoid. First, safeguards would need to be devised to ensure that incentives on the market to develop its own supply of public service content were not removed – which could become problematic if different markets or methods of payment emerged in future. Second, while it is easy to see how a structure of CCE-funded interventions could be built up to give plurality in content provision around specific genres, such interventions may 'set in stone' specific public service goals, assigning them a specific priority and a call on public funding, rather than allowing flexibility for PSB content creators to allocate resources according to the varying availability of desirable content proposals, and could have disincentives for the development of content outside or between standard content genres.

Any system of contestable funding would therefore need to replicate the advantages enjoyed by institutions which are able to adapt to changing priorities, and have more flexibility in the way they can move funds and production resources to meet emerging needs, or new platforms and services to use to meet the desired audience.

Third, a system in which shortfalls in PSB provision are 'chased' by a funding body and contractually specified for grant-receiving content producers to address over a fixed period may not have the ability to react in such a way as to ensure that the chosen service is still the best way to reach the audience. Recent experience suggests that, in the case of reaching youth audiences, the length of time for which a service is the 'must-have' way of reaching the audience is likely to get shorter, rather than longer, which means either that the commissioning body will have to deal in shorter term contracts, or that there will be a greater risk of funding going to services for relatively longer and stable contracts but which are themselves no longer particularly efficient ways of reaching the audience.

Ultimately, under a genre-specific PSB funding system, CCE interventions would tend towards 'market-failure'-style targeting, producing a system of fixed, 'pure' PSB responses to specific plurality requirements. There could be an undesirable knock-on effect on the BBC's own PSB provision – both in terms of its orientation (which would inevitably be at least partially determined by the areas in which plurality was being funded), and its nature (which would be refocused towards the same 'pure' PSB content). The resulting system of PSB provision would need to be carefully designed to ensure that it retained the potential benefits of the current system where all public funding is channelled to a single provider with clear and unambiguous public goals, and avoided becoming too rigidly structured and compartmentalised.

There may also be a need to define new approaches to sustaining quality. In a world where the commissioner of the product is also its immediate distributor, the alignment of incentives around quality and purpose are likely to be clear and straightforward. Contestable funding means the emergence of a third party at point of commission, as well as responsible for monitoring and assessing of the quality of the finished product. This suggests that a potentially more complex set of relationships may need to be put in place. These are by no means new or unknown in the media sector, where it is common practice for content to be co-produced by a number of different parties, each with their own editorial objectives. However, even in relatively straightforward contracts, it is likely to be the case that aligning these objectives and establishing the criteria for assessment between all three parties (the producer, the funder and the platform or distributor) is likely to be more complex in order to ensure that quality and performance criteria are properly established at the outset.

### **Key challenges**

- How can PSB be delivered in a flexible and adaptive way with the governing structure necessary for contestability imposed upon it?
- How can a genre-compartmentalised contestable system address the problems of delivering mass audiences with content proliferation, audience fragmentation and changing viewing patterns?
- How can a public funding allocation process ensure that funds reach content providers in time for them to address increasingly changeable and unpredictable audiences across constantly developing, yet often evanescent, platforms?
- How would funding PSB both for the BBC and contestable funding through the same source affect democratic plurality in the provision of genres such as news and current affairs?

### **How can effective governance be imposed simultaneously on the BBC, the Licence Fee and a contestable element?**

Under the 2006 BBC Royal Charter, the BBC Trust is both responsible for the revenue from the TV Licence Fee, and guardian of the Licence Fee payers' interest in the BBC. As custodian of the Licence Fee on behalf of viewers, the Trust requires the BBC to undertake commitments to, among other

things, the supply of PSB content in return for this funding, and assesses the Corporation's output against these commitments.

The introduction of a contestable element to the TV Licence Fee, to be distributed to other originators of PSB content, would necessitate the administration of such a fund. If the sole requirement of the CCE were to provide funding for an additional source of local and regional news, then the administrative and governance requirements could be comparatively less onerous: however, even in this case, and certainly if the fund is applied to other types of content as well (as discussed in the previous section), the demands both of administration and of governance could be significantly greater.

In relation to administration, the more complex the set of content requirements, the more sophisticated will its powers of strategic analysis, as well as commissioning expertise, need to be. In relation to governance, in addition to ways of ensuring proper accountability and transparency for how the money is being spent, there will also be a requirement to ensure that both the goals for which the money is allocated and the amount of money reserved for meeting those goals are still appropriate when set against the other uses that might be made of the funding by the BBC.

While perhaps not urgent at present, this could become a pressing issue if the overall level of the licence fee were to fall. On the one hand, the BBC with its far greater size and flexibility may be better placed to reallocate resources to meet its priorities; on the other, the content providers funded out of the CCE would have no such advantage – so that a reduction in the overall level could be disproportionately difficult for them to accommodate.

Equally, any change in the level of the overall licence fee suggests that a holistic assessment should be made of how best to allocate the funds to meet overall public service goals – but with the money split into two funds, and with one of those funds hypothecated to a particular form of output, such a review will need careful governance arrangements. This would particularly be the case if the fund were specifically designed to guarantee the continued plurality of supply of specific content: the BBC might well be compromised in its ability to maintain the range of its local services under the current proposal.

### **Key challenges**

Both the Digital Britain report and the consultation document issued by DCMS recognise that there is a complex set of issues in designing the CCE in such a way as to protect the interests of the BBC, to ensure that the level of the CCE would be contained, and to ensure effective accountability for the way the funding would be allocated. In particular, the relationship between the CCE and the BBC Trust in relation to the overall review of priorities for public funding would require careful assessment. There would undoubtedly be implications, possibly very profound, for the way in which the BBC Trust would in future be able to discharge its role, and these would need to be considered alongside the narrower deliberations over the future funding of regional news.

### **Experience from other countries**

As we have already noted, the proposal to introduce a CCE from within the TV Licence Fee differs markedly from any other public intervention in that it is specifically designed to use public money to

complement existing public provision with an alternative supplier of the same kind of content. This therefore goes beyond a simple market failure argument, where the assessment is made in relation to whether the market itself will supply, by using the funding to create two public sources of content.

There are therefore no direct comparators for the proposal put forward in the Digital Britain report from which we can draw lessons about how the challenges identified above have been addressed elsewhere. However, there are still generic challenges inherent in the creation of contestable funding mechanisms which it will be appropriate to assess in order to draw the appropriate lessons.

### **Bureaucracy / Inflexibility**

#### Canada

The Canadian Television Fund (CTF) is a PSB intervention designed to promote the production of Canadian-made content in a number of genres. It is funded both by the Department of Canadian Heritage and by statutory contributions from broadcasting distribution undertakings (BDUs) – i.e. broadcasting networks such as satellite, cable, terrestrial etc. As a condition of their licences from the broadcasting regulator (the Canadian Radio-television and Telecommunications Commission), BDUs must contribute around 5% of their broadcasting revenues to Canadian programming, of which 1.5% to 5% to be contributed to production funds. At least 80% of these contributions must be given to the CTF.

The development of the Canadian experience in contestable PSB funding is illustrative of a number of dangers inherent in this sort of arrangement. For example, the CTF has been criticised for being bureaucratic, for providing poor value for money in its funding activity (including the programmes selected for production) and for producing output that was neither commercial nor popular. While the bureaucratic nature of the CTF could to an extent be said to be intrinsic to Canada's multi-lingual society and federal political structure – for example, with the inclusion of French programming – there have nonetheless also been criticisms of ineffectiveness in the contestable funding arrangement that can't be traced to the same causes.

In late 2006, two major Canadian broadcasting companies, Shaw Communications and Quebecor Media, withheld their statutory contributions to the CTF, in protest over the CTF's efficacy, efficiency, and governance structure. Among the complaints made by these two organisations was that they were paying too much for the bureaucracy dedicated to running the fund, and that the output was unpopular and of low commercial or cultural value.

Partly as a result of these protests, the CTF was restructured and its funding resources split into two streams – one for the state contributions to fund publicly-owned broadcasters; and the other for the BDUs to fund more mainstream programming. Funding for content makers from the former stream would be awarded for measures of public service output, whereas the latter funding stream would be awarded on the basis of audience success alone. This change in turn raised complaints of duplicating bureaucracy. Where there had been a single board, there would now be one for each funding source.

More fundamentally, the splitting of the CTF's function into 'PSB' and 'populist' streams of funding has brought criticism that this has essentially allowed the contributing broadcasting networks to 're-

capture' the funds they were required to give for public service output in the first place. While it is important that contestably funded content should have as large a reach and audience as possible, simply taking away the more onerous requirements of public service content and making audience figures the sole criterion of success for one stream of funding for CTF's commissions reduces its relevance to the original reason for the intervention.

The bureaucratic difficulty and unclear or unrealistic goals that can come about with a committee-administered fund for public service content, can lead to outcomes that depart significantly from the original intentions in setting up such funds. In the case of the CTF, this may have been due in some measure to the larger private contributors using their influence to affect the allocation of resources, but the principle remains: a contestable PSB fund brings with it pressures from influential competing broadcasters and this can build bureaucracy within the fund's administration and can even distort the original aims and objectives of the funding intervention itself.

### **Unavoidable increases in the amount of money made available to the fund**

#### Ireland

The main funding of public service broadcasting in Ireland is through a licence fee, which is used to fund Raidió Teilifís Éireann (RTÉ), the state broadcaster. However, in 2003 the Irish government introduced the 'Sound and Vision Grant Scheme' which was designed to support the production of new television and radio programmes in the areas of Irish culture, heritage and experience, and in adult literacy. The Broadcasting Funding Act of 2003 set out that the scheme would be funded by 5% of the net receipts of the television licence fee (after costs and other disbursements) to be handled by the Broadcasting Commission of Ireland (BCI) – the Irish commercial broadcasting sector regulator.<sup>26</sup> This fund is contestable and allocated in funding rounds to producers who compete to make public service programmes of the types described.

The Broadcasting Act of 2009, signed into law on 12 July, established the Broadcasting Authority of Ireland (BAI), to take over the role of the BCI (and some other functions). While the provisions of the Act covering the BAI and its activities will not come into force until a Statutory Instrument gives them effect, the Bill passed by the Irish parliament from which it originated proposed an increase in the amount to be allocated to the Sound and Vision scheme, from 5 to 7%.<sup>27</sup>

This suggests that it may be in the nature of top-sliced funding to grow over time. If the Government, in its report, is prepared to make recommendations for the contestable public funding of content in genres that it regards as under-supplied or lacking in plurality, instead of addressing the perceived shortfall through existing PSB content providers, then it is easy to imagine the idea being extended to other genres of public service content in the future. If one area of public service content is important enough to need publicly funded competition to the BBC, all other genres could be seen in the same way.

### **Impact on the attitude and behaviour of the existing public provider**

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<sup>26</sup> Broadcasting (Funding) Act 2003 <http://www.oireachtas.ie/documents/bills28/acts/2003/a4303.pdf>

<sup>27</sup> Broadcasting Bill 2008 <http://www.oireachtas.ie/viewdoc.asp?fn=/documents/bills28/bills/2008/2908/b29d08s.pdf>

### New Zealand

From a system with a single, licence-fee funded public broadcaster similar to the BBC, New Zealand moved in the late 1980s to a commercial PSB system, with the channels of the state broadcaster (TVNZ) having to sell advertising as their chief source of funds, and required to return a dividend to the state. The TV licence fee was removed from the public broadcaster's control and made a fully contestable fund, under the control of a broadcasting commission. At the same time, privately owned TV networks were allowed for the first time and advertising was liberalised. TVNZ had its public service obligations heavily reduced and the broadcasting commission (which became known as NZ On Air) distributed the licence fee funds for local content and non-commercial broadcasting.

In 1999, moves were made by government to do away with the licence fee totally. By this time, TVNZ had become highly commercialised in its outlook and output, maintaining a high audience share with its channels, but with little in the way of 'traditional' public service television in its schedules. Soon after the licence fee abolition, however, a newly elected New Zealand government arranged for funding for NZOA to come directly from public funds. Over the next few years, public service obligations were reintroduced, and in 2003 TVNZ was restructured and given a public service charter, accompanied by a small amount of direct government subsidy (although it remained mostly dependent on advertising revenues). At present, although a public broadcaster, TVNZ is essentially a commercially funded network competing for ratings with commercial broadcasters.

With the removal of its licence fee funding, the New Zealand state broadcaster became almost entirely commercially orientated. The contestable fund became the only remaining source of public service content in an otherwise commercial television economy. This commercial television economy also affected the operation of the contestable fund itself, with claims being made that NZOA invested in overly-commercial content, possibly as the result of pressure from broadcasters to make the PSB commissions in question more marketable.

### **Effect on levels and quality of PSB content**

#### New Zealand

Intense competition for audiences and advertising revenues in New Zealand also meant that content acquired from overseas – the US, UK and Australia in particular – took up increasing amounts in channels' schedules. According to one commentator, by the early 2000s New Zealand television was showing one of the lowest amounts of original content in the developed world, at 24%.<sup>28</sup> Ultimately, it would also seem that the NZOA contestable fund system was not sufficient to guarantee adequate levels of PSB programming: in 2006, the New Zealand government gave TVNZ full funding for two non-commercial digital PSB services, showing content in drama, arts, documentary and children's programming.

#### Canada

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<sup>28</sup> Tim Gardam, Financial Times, December 2003

As described above, the contestable Canadian Television Fund, paid for by government and broadcasters, has suffered from criticism of failing to produce content of sufficient quality – both culturally and in terms of audience appreciation and popularity.

In summary, experience of contestable PSB funding in other regulatory jurisdictions has shown that there are several important risks taken on in setting up this kind of arrangement. In recommending a contestable element to the Licence Fee, the Government does not recognise these risks, much less describe how their effects might be mitigated. These are serious shortcomings that must be fully debated and addressed if there is to be any consideration of contestable funding – otherwise the risk to the supply of PSB in the UK would be considerable, and very difficult to reverse.