

## Section 3

# Digital Content

### 3.1 The Economics of Digital Content

Digital technology has significantly reduced the cost of producing, distributing, storing and manipulating content. Today anyone can be their own publisher, journalist, programme maker or international e-merchant. It also enables content to be replicated instantly at virtually no cost.

These technology changes bring convenience and enable personalised media consumption. They create opportunities for new formats and more interactive services. They also enable the online environment to be a highly effective price discovery mechanism, improving the efficiency of the market and shortening the supply chain for individuals and businesses alike.

The UK's inherent creative strengths have given us a global advantage in the creation and production of compelling and innovative content, not just in traditional broadcasting, but in advertising, online content, mobile content, music and programme production. These have given this country a cultural significance around the world out of proportion to our relative size.

The audiovisual content production sector in the UK accounts for annual production activity of between £5.5 to £6bn, and exports (according to ONS data) of around £2.3bn.

UK content production is in turn an important part of the overall creative industries sector that in total accounts for more than 6 per cent of UK gross value added, which as a sector is equivalent in scale to the financial services industry. Radio and TV, along with software, computer games and electronic publishing account for around half of this total.

The OECD estimates that the UK cultural sector is relatively more important (at just under 6 per cent of GDP) than its equivalent sectors in the US, Canada, France and Australia. Unesco estimates indicate that the UK is the world's biggest exporter of "cultural goods", surpassing even the US.



In 2008, the Government published a strategy for developing “Creative Britain”, which argued that the creative industries must move from the margins to the mainstream of economic policy.

Until 2008, the sector was growing, driven by rising revenues, new consumer demand, and competition for audiences. In online and mobile in particular, growth in content spend has been rising rapidly from a small base. The UK games industry continues to make a significant financial, creative and cultural contribution to the UK, but is facing particular challenges.

Much of the sector’s size and growth has been based on revenues in television. Internationally, the UK television content sector is the largest in Europe and the largest relative to GDP in the world, and in export of TV show formats, the UK is by far the largest single source. Overseas sales of UK programmes and formats grew by 23% in 2007, with overseas revenues of UK distributors and producers totalling £663m, producing a net contribution to content creation, after distribution costs and commissions, of around £380m.

This overall growth trend stalled in 2008, however, as the sector has begun to face significant revenue pressures. Predictions for the short term signal a decline in the total value of UK television content production, but with continued increases in new media activity. In the longer term, there are significant structural and competitive challenges, which will change the shape of the sector and its prospects in its home market.

These structural challenges arise from the transition to digital economics and, with that, the dwindling of the advertising pound and the retail margin for physical copies that, in the past, funded substantial parts of both our traditional media and new media.

Since 2002, e-commerce has grown from £19billion to nearly £163 billion a year. Internet advertising has grown with it. Britain has the highest proportion of internet advertising of any developed economy: at 15% of all advertising it already dwarfs the revenue of radio advertising and is on course to overtake press and TV before long. British consumers have a huge appetite for new digital services, with high levels of take-up of new networks and devices. This in turn creates a market environment which unlocks new commercial possibilities and encourages innovation in new content, services and applications.

These changes are challenging the economics of intermediaries of all kinds and more traditional types of content companies – publishers, the music industry, the newspaper industry and broadcasters – in particular.

There are four commercial challenges that need to be addressed to preserve a healthy content market in the digital age.

Firstly, if digital distribution and copying costs are lower so too are digital revenues from the product or the advertising impact; often, in current business models, an order of magnitude lower. New business models need to evolve for that environment. The role for regulation or intervention is not to prevent the emergence of new business



models or to preserve old and unsustainable ones. It is to contribute constructively to the transition.

Secondly, the rapid growth in the number of digital outlets has hugely increased the volume of advertising inventory available. This trend will only increase: unless there is a paid-for product or service for the consumer to own, (e.g. paid-for content or application downloads) internet content is perceived to be 'free' - i.e. if monetised, it is through advertising. This increase in the volume of advertising impacts has a commensurate impact on their price (and hence on the margins of advertiser-funded businesses).

Thirdly, there is the challenge of access to content and the ability to innovate across the increasing range of distribution platforms and digital devices. Convergence has allowed development of bundled packages offering consumers a mix of content and services. Development of business models built around such bundling depends to a large degree on wholesale access to important content to deepen the range of bundles addressing individual consumer preferences.

Fourth, the very ease with which digital content can be distributed and copied also dramatically increases the scope for unlicensed and illegal copying and distribution. At the same time, new technological forms of piracy are being manifested at an increasing pace. Counter-piracy measures and effective rights enforcement are an important element, but only one element and insufficient on their own: new methods of legitimate access, based on new business models and incentive structures will be crucial.

This is placing pressures on professional content, whether in programme-making or in journalism and newsgathering, with significant implications for the future health and growth of the sector. While some traditional audio-visual content is under threat, new media content is in its relative infancy as a possible new generator of economic wealth.

Faced with these challenges and, in particular, the dwindling of the advertising pound in its historic role as underpinning finance for much content creation, the UK needs to consider whether there are other funding streams or mechanisms that would substitute in whole or in part. Several of these, including regulatory assets, industry or equipment levies and contestable funding for content production that meets public purposes, are deployed in varying degrees in other markets.

## **ACTION 10**

**In the final report we will examine measures needed to address the challenges for digital content in more detail, including opportunities for providing further support to foster UK creative ambition and alternative funding mechanisms to advertising revenues.**

In the remaining parts of this section we address some of the most immediate issues which have an impact on digital content and outline ways forward.



## 3.2 Investment in Content: Rights and Distribution

The core ethos, and success, of the internet to date lies in its ability to stimulate shared ideas and content. It also promotes participation, pro-activity and creativity. But there is a tension between providing reasonable rewards for creativity, which have historically required a measure of protection for the creator's rights, and the freedom to allow that content to be used to permit further innovation and creativity. In the new digital world, the ability to share content legally, becomes ever more important and necessary. Traditional mechanisms to identify rights-holders and acquire legal consent to share often need radical updating to meet the near-instant demands of this new world. There is a clear and unambiguous distinction between the legal and illegal sharing of content which we must urgently address. But, we need to do so in a way that recognises that when there is very widespread behaviour and social acceptability of such behaviour that is at odds with the rules, then the rules, the business models that the rules have underpinned and the behaviour itself may all need to change.

Across both old and new media, if we have an ambition to be the leading international destination for creative businesses, we need to combine an environment where opportunities abound for rights holders and digital distributors to develop exciting new ways to package and sell the content that people want. It must have a digital content protection framework in which such international businesses can have confidence. This will be increasingly vital in a Digital Britain where everyone has access to video capable broadband and many have access to much higher bandwidths. We must make sure that together we address the threats. But at the same time we must not lose sight of the fact that a truly broadband Britain promises huge opportunities for digital content producers.

### The Intellectual Property Office (IPO)

The Intellectual Property Office has launched a debate on the future of copyright building on the recommendations of the Gowers Review, which we will consider as part of our final report. This work aims to build a long term vision for copyright, considering what changes may be required domestically, at EU level and internationally. Although the IPO's work is not limited to digital issues, most of the key issues are highly relevant to the digital environment.

Copyright is vital for our content and communications industries. It is the framework through which people can protect their creations and seek reward. Our aim, in the rapidly changing digital world is a framework that is effective and enforceable, both nationally and across borders. But it must be one which also allows for innovation in platforms, devices and applications that make use of content and that respond to consumers' desire to access content in the time and manner they want, allowing them to use it how they want, and at a price they are willing to pay.

Already the UK has achieved a world-first in this regard: the Memorandum of Understanding between the Internet Service Providers (ISPs) and rights holders to



tackle unlawful file-sharing by consumers – it has shown that these two groups with very different agendas can engage in an intelligent conversation about how to secure action in respect of legal offerings, education and enforcement. We need to ensure that all the work, and the increased understanding it has engendered, is not wasted. Quite apart from the specific work on unlawful file-sharing we need to make sure that there continues to be a space where different interests can come together and talk. If that helps develop new legitimate offerings (being careful to avoid any possibility of anything anti-competitive being discussed) then that is something that Government should be willing to facilitate. It's clearly for industry to do the commercial deals – but Government should smooth the path where it can.

Of course much of the digital content sector still depends on non-digital and long-established business models for the bulk of its revenue, and we should not pretend that adapting to a digital environment will be easy or simple. But there can be little doubt about where the future lies, as an increasing range of content becomes digitised, for example e-books becoming part of the mainstream. What worked in the physical world will often not work online, and rights holders must find new partners, and new ways of creating value from their Intellectual Property.

We need to support rights holders as they adapt their way of thinking and working. This is not to support business models that will become increasingly obsolete, and nor do we want to try and pick *the* new business model – in any case there will almost certainly be many competing ones. But we should look at the environment within which they operate, and for rights holders that means the sea of unlawful activity within which they have to swim.

As well as the Government support for rights holders we need to acknowledge the issues which their customers are raising. Businesses need to understand the best ways of responding to the changing demands and behaviour of potential customers, winning their trust and securing income. Winning the trust of customers will be vital to the success of the sector as it finds a way to seize the opportunities the internet has to offer.

An effective enforcement framework must address both criminal and civil law infringements. In terms of criminal enforcement the Government is already taking a leading role, one that is recognised internationally. Since the launch of the National IP Crime Strategy in 2004 we have continued to increase our capability to rise to the challenges of criminal piracy. The Intellectual Property Office sits at the core of this initiative, leading a co-ordinated response to improve awareness and expertise on IP crime issues within our enforcement agencies and facilitating the sharing of best practice and intelligence. The Creative Britain Report published in February 2008 heralded the creation of a new National Centre for IP Crime to help drive further improvements – which will be up and running later this year. The benefits of this co-ordinated approach are recognised internationally.

More directly, funding has been provided to help trading standards officers tackle IP crime at the local level. In 2008 this funding was over £7million with similar funding for 2009 and 2010. This work is delivering real results.



But it is not only criminal scale copying that poses a threat to our digital future. The copying and sharing of content online has become a commonplace activity for many consumers. Where such activity is unlawful, the tackling of such infringement raises clear challenges, both in terms of the scale of such activity and in the kinds of responses that may be appropriate in respect of individual consumers. We must rise to this challenge and consider what role there is for government in helping industry to address civil infringement in the online world.

The copying of content without permission by consumers is not new – it's been an unwanted companion of creative goods for as long as there have been means of copying material without paying. In the analogue world, though, it is a manageable problem, both in the control of such copies and in terms of consumer demand: there is usually a detectable deterioration of quality – video tapes were never as good as the original, and taping music from vinyl or the radio was a poor substitute. The digital world changes all that: copies are near-perfect and can be shared widely with the online community. Entirely legitimate technologies such as file-sharing can be abused such that millions of people can access material, unlawfully but for free.

This has led to a fundamental change in consumer expectations, particularly among the young. There is now a growing expectation that content can be found and shared for free. There is a corresponding resistance to paying for content, or accepting that an inability to pay means an inability to access the content. The collective impact of small scale individual infringement is considered to be significant while recourse for such infringement is delivered through individual civil court actions which can be costly and time consuming for the rights holder and which are perceived as disproportionate by consumers. This has affected different sectors to different extents; music is most exposed. Film, games, broadcasters and the publishing industry are also increasingly being affected. Indeed, it is a phenomenon all the digital content sectors will have to face sooner or later.

It is clearly in the interests of rights holders to produce the creative products that people actively want to buy in the way they want to buy them, and to ensure people are educated about how digital products can be used and why there may be limitations, we also need to work together to find ways to prevent such infringement and to enable action to be taken against those who insist on infringing copyright. If, we expect the whole value chain to benefit from new ways legitimate content can be accessed and consumed then it is reasonable to expect the whole value chain to work together to tackle unlawful activity.

What will help to deter copyright infringement online by consumers in both the short and longer term is a combination of things. A strong message is needed about the importance of respecting copyright as a necessary part of creating new high quality content. There must be a more intelligent and nuanced appeal to what consumers value – the on-going availability of compelling content.



This needs to be backed up by a substantially higher chance of repeat infringers getting caught. The University of Hertfordshire<sup>2</sup> research into attitudes towards music and copyright by young people showed that only 10% of those surveyed are currently deterred from file-sharing by a fear of being caught. The current approach to civil enforcement is not working as well as it needs to. This may be due to a lack of resource – although many rights holders assign significant sums to tackling copyright infringement. The issue may be one of spending more but it may also be one of working smarter. While there is little if any evidence that the remedies against infringement are themselves outdated, the processes by which those remedies can be reached are the product of the analogue age. They need up-dating to be workable in a digital world; and to enable new business models to get enough financial air to breathe and survive.

Perhaps most importantly the availability of legal content in the forms that consumers want is crucial. In the short and long term, the rights holders must find the innovations that once again enable them and their customers to respect each other's point of view. These are businesses where the customers and content creators alike have been used to paying for and rewarding emotional commitment, enjoyment and admiration. This has been an historic strength and one that businesses need successfully to innovate to recover.

## ACTION 11

**By the time the final Digital Britain report is published the Government will have explored with interested parties the potential for a Rights Agency to bring industry together to agree how to provide incentives for legal use of copyright material; work together to prevent unlawful use by consumers which infringes civil copyright law; and enable technical copyright-support solutions that work for both consumers and content creators. The Government also welcomes other suggestions on how these objectives should be achieved.**

Such an approach would need rights-holders and distributors of all digital material (e.g. music, film, television and radio, software, computer games, e-books) to work together to develop ways of making this kind of piracy more difficult to do and easier to trace and prevent. This could involve working with authorities in other countries to act against damaging sources of infringing material. It could also include the exploration of new technical approaches to the content itself or its transmission, including common standards.

This body could carry on the work started by the Memorandum of Understanding on unlawful file-sharing. It should provide the forum within which all elements in the value chain – content creators, initial aggregators (e.g. studios or broadcasters), theatrical distributors (e.g. cinema chains), networks, ISPs and other parts of the chain – could come together. Within the boundaries of competition law, this could lead to the development of models that provide incentives for all for legitimate downloading and use, a framework of common responsibility to discourage and prevent illicit use,

<sup>2</sup> 42% of those surveyed admitted to uploading. Of the 68% who did not, only 15% said this was because of the fear of being caught. [www.ukmusic.org/cms/uploads/files/UoH%20Reseach%202008.pdf](http://www.ukmusic.org/cms/uploads/files/UoH%20Reseach%202008.pdf)



and to support and legitimise technical solutions that can achieve both. Developing new business models is primarily for industry to do, not for Government or any new body. But working together on enforcement and education mean there needs to be clear advantages to all sides – a win/win/win for rights holders, intermediaries and consumers. Rights holders and intermediaries should each reap the economic benefits of delivering a better service to consumers.

### Possible technical solutions

Automated Content Access Protocol is one example of a technical solution. Digital Rights Management (DRM), properly applied, also has a role (i.e. where it allows users to access content on any device that they own, rather than being device limited – which is the paradigm that the film industry has encouraged and one that, in music, Apple's iTunes has now embraced, in a welcome recent co-operation between rights-owners and a device/ distributor). Both can work when they are technical-enabling solutions that match market trends and go with the grain of the market and legitimate consumer demand. But they have yet to command the assent, let alone active support, of all the necessary players along the internet value-chain.

It may be that such an independent, objective body may be better able to surmount the mutual tension between rights-holders, publishers, search engines and other content aggregators, the ISPs and the underlying communications network operators and instead broker technical solutions that can command widespread adoption and support. We also recognise that, while industry co-operation should be at the core of this, such a 'Rights Agency' may need to have the power to act to ensure that enforcement measures are effective and proportionate.

If the UK can develop such a working forum, we will have an advantage over most other countries.

### ACTION 12

**Before the full Digital Britain Report is published we will explore with both distributors and rights-holders their willingness to fund, through a modest and proportionate contribution, such a new approach to civil enforcement of copyright within the legal frameworks applying to electronic commerce, copyright, data protection and privacy to facilitate and co-ordinate an industry response to this challenge. It will be important to ensure that this approach covers the need for innovative legitimate services to meet consumer demand, and education and information activity to educate consumers in fair and appropriate uses of copyrighted material as well as enforcement and prevention work.**

The Government also recognises that there is a more specific problem that needs addressing on unlawful file-sharing, where we have been clear in the *Creative Britain* paper and elsewhere that we would legislate if necessary.

The consultation on how we might tackle this issue closed at the end of October. We have today published a Response to that consultation which can be found on the



BERR website, which sets out our analysis of the responses and how we intend to proceed. None of the options highlighted in the consultation attracted widespread support. Rather there was a marked polarisation of views between the rights holder community, consumers and the ISPs over what action should be taken.

A number of key issues were identified by respondents including copyright protection, protections afforded under eCommerce legislation and the impact on the wider economy. Consumers (individuals and consumer organisations) in particular highlighted concerns over data protection and privacy. The role of technology was addressed by most respondents but there were conflicting views as to whether it could offer all or part of any solution. For almost all the options, questions were raised as to their legality under the existing legal frameworks and again, views varied.

Our preferred option of co-regulation did not attract widespread support. The key problem highlighted was the lack of certainty over the nature of the obligation on ISPs and the resulting legal uncertainty this would create for all parties. There remained major concerns how consumer protection would be properly addressed, while developing the self-regulatory aspect through a code of practice raised significant questions on how to accommodate other rights holders, the smaller ISPs and consumer bodies. This was borne out by the experience of the current Memorandum of Understanding group which showed that despite the best endeavours of all concerned, reaching voluntary agreement where there is little perceived common interest between the various participants is extremely hard.

There was, however, a degree of consensus that any solution must involve the provision of new legal sources of attractive content, and that there is a need for education on the importance of copyright in the wider economy.

### **ACTION 13**

**Our response to the consultation on peer-to-peer file sharing sets out our intention to legislate, requiring ISPs to notify alleged infringers of rights (subject to reasonable levels of proof from rights- holders) that their conduct is unlawful. We also intend to require ISPs to collect anonymised information on serious repeat infringers (derived from their notification activities), to be made available to rights-holders together with personal details on receipt of a court order. We intend to consult on this approach shortly, setting out our proposals in detail.**

This should provide a good evidence base, to make it significantly easier for rights-holders to take targeted legal action against the most significant infringers. International experience of action of this sort suggests that more than two thirds of infringers change their behaviour when receiving notification. These obligations will form the central elements of a Code on unlawful file-sharing which Industry would be required to have in place, supported by backstop powers overseen by Ofcom. The Code would cover among other issues practical supporting measures, including appeals and standards of evidence. It would also cover cost-sharing.

We think the concept of a new Rights Agency and legislative action aimed specifically at addressing unlawful peer-to-peer file-sharing could be major steps forward. But this



is new and difficult territory, and we want to get it right. So we will review the impact of any new measures, and will not hesitate to examine other options if these do not prove to be effective.

### 3.3 Investment in Content: Original UK Content

The migration to the new digital world vastly increases the amount of content and applications at our disposal. Digital technology extends choice: wholly-market based operators such as BSkyB offer innovative distribution platforms, aggregating hundreds of digital channels, including their own content across programme areas such as 24-hour news and the Arts that were previously considered the exclusive preserve of public service broadcasters (PSBs). Digital technology also lowers barriers to new providers- the wide range of services now catering to ethnic minority communities and to specialist interest, the development of community services, of user-generated content whether on YouTube or on social networking sites- all testify to the liberating power of digital technology.

For cultural reasons, social reasons and, as citizens in a democracy we want at least some of that rich array of choice to be British content, including impartial British news.

The previous section shows the challenge that digital economics pose to a number of business models that have traditionally supported content creation and aggregation. The huge growth of advertising inventory has produced a parallel reduction in the value of advertising impacts and their ability to fund professional long-form content. Pricing and consumer expectations whether for adverts or subscription to the content itself are a fraction of their analogue value.

The profits that funded high levels of original UK content are diminishing. This change impacts on television and radio broadcasting, and our press among other parts of the sector.

The BBC continues to provide programming of wide range and quality, well-resourced impartial news and is innovating successfully in new forms of content for today's multi-media, multi-platform digital age. The Government is committed to a strong, fully funded BBC at the core of delivering public purposes in Britain's media.

As a nation, we have been very fortunate in having other sources of quality programming, delivering public purposes and impartial, high quality news alongside the BBC. This contrasts with many other countries, even the more developed economies, where there is often only one public service institution. All the evidence suggests that Britain's citizens value this plurality.

But the wide range of sources of news at national, regional and local level, and particularly a range of sources of widely- available impartial news is not something that we can any longer take for granted.

In television and radio, as with news, we may no longer be able to rely on the provision in the future of the wider range of public service programming from varied sources to which we have been used. The BBC will, of course, remain as the guarantor



of a significant level of public service programming and of high-quality news. The Government does not believe that the BBC as the only publicly secured provider will be sufficient.

The research in Ofcom’s recent Review of Public Service Broadcasting shows continued public demand both for competition for quality and innovation across a wide range of programming and for a publicly funded plurality of impartial news sources at regional and national levels.

This response by the public shows the continued importance the UK places upon the relationship between impartial news and an informed democratic process. This suggests that we need to be sure of a continued wide range of impartial news sources.

More generally, the Government is clear that a range of different creative sources, commissioners and perspectives is vital for healthy levels of innovation and to ensure that we are developing the talent and voices of all diverse communities. We recognise the need to secure adequate provision of content for Northern Ireland, Scotland and Wales in the context of any new PSB model. For cultural and social reasons, we need at least one other provider of scale as well as the BBC.

We believe that we need to aim for plural public service provision which gives us:

- Sources of high quality impartial news at local, regional as well as national level, including the Nations as well as the UK as a whole.
- Large scale original British content.
- A wide range of voices and talent from across the whole United Kingdom, secured in part by ensuring the continuation and development of creative talent clusters in the regions and Nations, currently guaranteed through regional production quotas on some public service broadcasters.
- Guaranteed levels of investment in independent production to ensure the delivery of the best creative ideas and the healthy development of this vital creative sector, similarly secured through quotas.
- A range of commissioning sources for innovative original production.
- Original children’s production for all ages but especially for over 10s.
- The development of plural sources of commissioning for current affairs, international issues and serious factual programmes.

Although we can expect the market to deliver some of these types of content to some degree, it is likely that interventions will be essential to meet the expectations and requirements of UK viewers. Achieving all of this is a significant task, requiring policy decisions across a great number of areas, including balancing some competing priorities. Ofcom’s review of Public Service Broadcasting makes a number of recommendations to Government. The Government will set out its detailed reaction to these in the final Digital Britain Report. But we are clear now that the over-riding priority is for investment in UK original content at scale and, within that, high quality



impartial news, both at UK and international level and for the devolved Nations and English Regions. This priority should be open also to content not created solely with the closed broadcasting networks and traditional broadcasting business models in mind.

### **IMPARTIAL NEWS FOR THE NATIONS, REGIONS AND LOCALLY**

At a local level, the challenges for news are intense. These challenges were highlighted in the thoughtful report by the House of Lords Communications Select Committee on *'The Ownership of news'*.

Local media groups are seeking to make the transition to digital business models but argue the need to consolidate in order to have the scale and sustainability to do so. They argue too that the media merger regime does not take account of the potential for competition across boundaries between newspapers and other media. This position, they argue, will become increasingly unsustainable as we move into a fully Digital Britain. Such arguments need to be tested against current evidence.

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

More widely, many people are beginning to raise questions about the longevity of local content. It is an issue in commercial radio and the newspaper industry. It was one of the factors in the decision by the BBC Trust to reject the BBC management's proposals for new BBC local services. Yet there are also some encouraging signs of community-based ultra-local information and news services, using digital technologies for inexpensive production and distribution. Similarly, there are examples of new partnerships emerging at local level, bringing together local media businesses working with voluntary and public sectors.

In the responses to this interim Digital Britain report, we will be particularly interested in hearing collectively from the local newspaper industry and others, alongside the independent review of local audio services mentioned earlier, about what role local journalism will have in providing impartial news in the digital age.

UK-wide and international news remains relatively well provided for from a range of sources. This contrasts with the position of news at the level of the devolved Nations and the English Regions where the commercial PSBs are facing challenges.

ITV plc and the other Channel 3 licensees are currently the key providers, outside the BBC, of news for the Nations and Regions. Ofcom's work has shown that this service is highly valued by viewers and the Government sees it as central to the ITV companies' identities as public service broadcasters. Ofcom's analysis also highlights the economic pressures on the continued delivery by the Channel 3 licensees of their public service obligations.



There are three broad options to address the issue of providing audiences with regional news beyond the BBC services. These options may, together, form an evolutionary path to a sustainable future, until such time as broadband-delivered local news could become an effective substitute.

The first is the BBC's proposal to enter into news gathering and production partnerships with the ITV companies, which could potentially lead to significant efficiencies in this area; and help sustain their ability to provide well resourced and informative regional news well into the future. This would also mark the beginning of a new phase of partnerships led by the BBC acting as an enabler of the plurality and quality of public service broadcasting. The BBC has proposed a range of partnerships in content, production and distribution which are the subject of engagement with other broadcasters.

Discussions between the BBC and ITV plc are at an advanced stage. This proposal offers a promising but not yet settled route forward. The Government is encouraging the parties to conclude their discussion to provide certainty in this area.

Ofcom has suggested that the current regional news slots in ITV's schedule could be opened to a third party, contestably-funded, news provider or indeed that the whole process, including distribution, could be made contestable. The suggestion has the advantage that it could bring in other news-providers from related media who can offset their news-gathering and production costs across a range of outlets, not just commercial television. It could also provide a clearer route to more broadband-focused delivery at some stage in future. It has the disadvantage that, if adopted wholesale now as the only approach, it may require additional public expenditure, which might be difficult to justify in current circumstances. These ideas should be developed further as a contingency against the risk that the partnership between the BBC and ITV is insufficient to meet the challenge.

In connection with the second option S4C have put forward interesting outline proposals in relation to an English-language news service for Wales. We will work with S4C and other partners to establish whether this proposal could form the basis of a pilot project in Wales.

The Government will also explore with the BBC, STV and UTV as well as other relevant possible partners how far similar pilot proposals could point a way forward for Scotland and Northern Ireland.

We will also consider the wide availability of news within the context of the development of a new and broader, commercially-based, content institution in the UK.

We also recognise the concerns raised by stakeholders, supported by Ofcom's analysis, in relation to the provision of high quality, original UK programming for children. The plural public service provision of original children's production, especially for the over 10s (a group currently underserved by the market unlike older teenagers and young adults) is an area we have identified above as being very important. We will return to this important topic in the final Digital Britain Report.



Support for UK originated content brings dual economic and social benefits. The starting point for both is to ensure a strong home market for investment in content of all types, on which we can build international success.

A strong and innovative BBC, working with the market, will be at the cornerstone of these efforts, currently with more than £3 billion public funding each year.

The BBC also has, in BBC Worldwide, an international rights-exploitation and channel operating entity with revenues of £916m and earnings of £118m. It is one of the more successful UK international media operators. It is well placed in the field of global rights exploitation upon which the strongest growth within the digital economy is based. It also has a portfolio of distribution channels in the UK and around the World which act as a shop window for those rights. Its success over the quarter century it has existed (as BBC Enterprises before becoming BBC Worldwide) has rested in large part on its proximity to the BBC licence-fee funded public services, the BBC brand around the world, and its first-look exploitation relationship of the relevant rights.

Following the BBC's own review of BBC Worldwide at the beginning of this decade, BBC Worldwide has been run as a vigorously commercial entity over recent years. Its contribution in terms of earning for the BBC and its place as a successful rights-exploiter and channel operator domestically and globally are testament to that more vigorously commercial approach. But the evidence suggests that BBC Worldwide may now be testing the limits of what can be achieved commercially within the way that it is currently structured.

Some have suggested that a greater degree of operational and financial flexibility for BBC Worldwide in the future could be better for Worldwide as a business, could be good for the licence payer by enabling it to return more to the BBC itself and could enable it to provide more for the creative system of this country as a whole. There may be a range of possible options and structures for the evolution of BBC Worldwide, That could enable it to meet public purposes while playing a larger part as a successfully commercial British Rights Company internationally. The Government will discuss this issue further with the BBC before the final report.

Changes are needed in the commercial broadcasting sector. The advertiser-funded, free-to-air broadcasters have contributed almost as much to investment in original UK content as the BBC, and more than the rest of the market put together. Recent research suggests that, in 2006, pay TV accounted for 26 per cent of TV income but only 5 per cent of spend on new TV programming – a position which is unlikely to have changed markedly since then. In contrast, around 60 per cent of advertising and publicly-funded income is translated into programme spend. The advertiser-funded broadcasters have been adversely affected both cyclically by the current significant drop in advertising revenues and structurally by the economics of digital.

These changes are putting increasing pressure on their role as investment engines for originated UK content. ITV plc has argued that it needs to be relieved of most of its licence obligations and other regulatory constraints if it is to be able to sustain significant levels of UK production. Indeed, this is the trajectory of a process which has



been underway throughout much of the last decade, as the regulation of ITV has had to adjust to changing market circumstances.

With an increasing pull towards net-based search advertising, and away from traditional broadcast ad sales, the commercial broadcasters are likely to be increasingly unable to develop their businesses to satisfy both their shareholders and our wish for them to continue to generate original UK content at scale and to meet our other public policy demands on them.

We need to recognise that one of the key features undermining the old model is the surplus of advertising impacts. The commercial PSBs are beginning to express concern about the need for scale and efficiencies. Consolidation may become necessary. But how that consolidation occurs is a matter of public interest as well as purely a competition issue. We need to consider how any such consolidation could best meet public interests.

As regards public service obligations, this report offers possible ways forward for Regional News above, and underlines the importance of continuing with Regional production and Independent production quotas as an essential part of the social and economic benefits arising from public service broadcasting.

An important part of the UK's international success in content to date has been driven by a successful and entrepreneurial independent production sector. A new breed of independent production houses of some scale has developed in recent years. The Terms of Trade have played a contributory role, and, nearly six years on from the Communications Act 2003, both the independent sector and wider media industries have been through significant change.

### Terms of trade

Under the Framework set out by the Communications Act 2003, the Terms of Trade between broadcasters and independent production companies govern the release of programming into the UK secondary market and new media rights for independently produced programming. The Terms of Trade allow Independent Producers to exploit secondary revenues from the programmes they create once the broadcaster has shown the programme. This has fuelled growth both domestically and internationally, and encouraged innovation as producers look to maximise value.

## ACTION 15

**The existing Terms of Trade between the independent producers and broadcasters have worked well. In light of new entrants to the market, new business models and new distribution channels, it makes sense to have a forward look at how the relationship between independent producers and those who commission their ideas could evolve. This review will focus on the appropriate rights holding agreements and definitions required for a multi-platform digital future, on the overall health of the sector and on continuing to ensure that viewers, listeners and users get the best and most innovative content and programming.**



Channel 4 has been greatly valued as a successful public policy intervention, although one designed for the analogue era of a very limited number of television channels and no internet. Today, while it remains a strong brand and continues to provide distinct content, the multiplicity of different content sources available means that its place in the world has shifted. In the digital world and against the backdrop of falling advertising revenues across the medium, Channel 4 has said that it will find it increasingly difficult, in its current institutional guise, to balance its public purposes and its commercial future effectively.

Many of the public purposes for which it was created remain valuable in the digital age – innovation, diversity, original production from a wide range of independent producers. In a digital age, these purposes need to be re-invented and broadened to provide a strong source of plurality and competition to the BBC. At the heart of this new remit should be strong commitments to international and national news, current affairs, documentaries and film with the prospect of introducing programming for older children and news for the nations.

In the medium term such a role could only be discharged successfully by an institution of sufficient scale and flexibility to sustain a viable commercially funded business model:

- **Scale:** to achieve impact, reach and effectiveness in a globally competitive multi media, multi-platform market place;
- **Flexibility:** to allow it to adapt to a fast changing media environment.

## **ACTION 16**

**In the final Digital Britain Report, we will establish whether a long-term and sustainable second public service organisation providing competition for quality to the BBC can be defined and designed, drawing in part on Channel 4's assets and a re-cast remit. It would be a body with public service at its heart, but one which is able to develop flexible and innovative partnerships with the wider private and public sector. While it makes sense to begin by looking at public sector bodies- Channel 4 and BBC Worldwide- the Government is currently evaluating a range of options and organisational solutions for achieving such an outcome.**

Channel 4 would continue to be the broadcast licensee within such an entity. For the public the viewing experience would be the same or better than today, but as a sustainable part of a wider whole operating successfully across the whole range of digital devices and platforms.

There is a range of issues that needs to be addressed in achieving such partnership, including the governance and accountability arrangements required for any new structure. We will return to this in the final report.

In summary, we see the BBC as the cornerstone of our audio-visual public services. We could have a vital, second Public Service Content Company, with access to rights and global markets, encapsulating the revitalised remit for Channel 4's public purposes and with the scale necessary to be able to compete in a multi-media, multi platform world. In addition, there would be Five and ITV, focused on original UK content,



but with a continued commitment to news and in ITV's case, regional news; S4C's additional news proposal and desires in Scotland for a stronger, distinctive national voice not limited just to broadcasting. Alongside these institutional developments, there are the public purposes identified earlier, including children's programming, where plurality of output is desirable. In their recent report, Ofcom noted that contestable funding may be a possible or necessary route to secure such plurality.

The BBC partnerships are a potentially helpful step but the challenge remains to secure such plurality of output at scale and in the medium term and beyond. Other options must remain on the table, including exploring the value of any surplus in the licence fee pre or post switchover and top-slicing. It is an issue to which we will return in the final Digital Britain Report.

