

## **Public Consultation on the BBC's Fair Trading Guidelines – An Explanatory Note**

### **Foreword**

The BBC's [Royal Charter and Agreement](#) place specific obligations on the BBC Trust (the "Trust") and the BBC Executive (the "BBC") in respect of Fair Trading. These obligations are detailed in the Trust's Statement of Policy on Fair Trading, Statement of Policy on Competitive Impact and in its code on Cross and Digital TV Promotion (collectively "[the Fair Trading Policies](#)").

The BBC has implemented the Trust's Fair Trading Policies through its Fair Trading Guidelines ("the Guidelines") which are published alongside this document. The primary purpose of the Guidelines is to provide simple, clear and practical guidance to BBC staff on how these principles should be applied in practice. The Guidelines also aid transparency to external stakeholders and provide a basis for holding the BBC to account.

The BBC has implemented a comprehensive framework of Fair Trading systems and controls that enables it to monitor and assess compliance with the Trust's Fair Trading Policies. The BBC has a central Fair Trading department comprising of advisory and compliance functions. It maintains a set of Fair Trading procedures conforming to the International Organization for Standardization ISO 9001:2000 (the standard for quality management systems) and manages an extensive Fair Trading training programme for all relevant staff. Further details can be found in the Guidelines.

The Guidelines have been in place in various forms for over ten years. The previous version of the Guidelines was approved by both the BBC and the Trust and came into effect on 1 July 2007. At the time of their approval the BBC committed to review the Guidelines one year later and to consult with key stakeholders on its proposals for change.

The BBC's Fair Trading department published a consultation document, including draft, revised Guidelines on [bbc.co.uk](http://bbc.co.uk) on 24 October 2008. Key external stakeholders were also contacted directly and invited to respond to the consultation. The BBC sought feedback on the effectiveness of the Guidelines in implementing the Trust's Fair Trading Policies. The consultation did not cover the scope and content of the Trust's Fair Trading policies; the Trust intends to consult on these in 2010.

The consultation document also provided an overview of the content of the Guidelines and highlighted some of the key changes. The BBC welcomed comments on any aspect of the proposed changes to the Guidelines and to help focus the debate sought responses to a number of key questions (see Annex I to this document).

The consultation closed on 16 January 2009.

The BBC was pleased with the quality of response received from third parties and considers that this has made an important contribution to the revised Guidelines. The purpose of this Explanatory Note is to explain how the BBC responded to the main issues raised in the public consultation. The new Guidelines were approved by both the BBC Executive and the Trust prior to publication.

**Balbir Binning**

**Controller Fair Trading & BBC Compliance Officer**

## Points arising from the public consultation

The BBC received four, substantive written responses to the consultation. All four parties requested that their responses remained anonymous. In addition, Ofcom and the European Commission confirmed in writing that they would not be responding to the consultation.

In the following sections, we provide a brief explanation of the key provisions of each Chapter of the Guidelines and our view on the main points which arose during the public consultation. It is not intended to be a comprehensive assessment of every point made during the public consultation.

### **The Competitive Impact Principle (Chapter I of the Guidelines)**

The Trust's Fair Trading Policies require the BBC "whilst always ensuring the fulfilment of its Public Purposes and taking into account its other obligations in the Charter and the Agreement, to endeavour to minimise its negative competitive impacts on the wider market." This is known as the Competitive Impact Principle (hereafter the "CIP"). The application of the CIP extends beyond the requirements of Competition Law – guidance to BBC staff on the requirements of UK and EU Competition Law (including State Aid law) is set out in Annex I of the Guidelines. The CIP applies only to the BBC's Public Service Activities.

This Chapter of the Guidelines received the most comments from third parties.

A respondent stated that the CIP was unduly weak and ineffective as a means of minimising the negative competitive impact of the BBC's activities. The BBC noted the point raised by the respondent but believes this is an issue more appropriately addressed in the Trust's review of its Fair Trading Policies in 2010.

A respondent also suggested a series of changes to how the BBC interprets and applies the CIP. For example, respondents requested that the Chapter is clarified to state that the CIP applies not just to new activities but also to the BBC's ongoing activities. A respondent also asked the BBC to qualify its statement that the application of the CIP does not require the BBC to eradicate all potential negative impacts and to amend our definition of what constitutes a competitive impact. In these and other instances, we have made appropriate clarifications to the Guidelines.

A respondent stated that the primary consideration when applying the CIP should be to identify the negative competitive impacts on the wider market. It stated that the first step – the assessment of public value – was unnecessary and a materially different assessment from whether the BBC is fulfilling its 'Public Purposes'. The BBC agrees that a key part of the CIP is the consideration of the potential negative competitive impacts and how these can be minimised (whilst always ensuring the fulfilment of its Public Purposes and taking account of its other Charter and Agreement obligations). It also agrees that the Guidelines would benefit from an explicit and direct reference to an activity meeting the BBC's Public Purposes. However it does not believe that the first step is unnecessary. The BBC believes it is important that the process for the application of the CIP should include a

consideration of how the activity fulfils the BBC's Public Purposes. The Guidelines have been updated accordingly.

A respondent argued that the BBC had incorrectly interpreted the Trust's requirements for applying the CIP. It stated that there is a material distinction between the statement in the Trust's Fair Trading Policies which requires consideration of "impacts on consumer welfare, consistent with competition law principle" and the statement in the Guidelines which refers to the protection of "the interests of consumers". The BBC believes that, when read in full, the Guidelines make clear that the "primary objective of the CIP is to protect the interests of consumers, which is generally considered to coincide with the aim of protecting competition in the market". The BBC believes that this combined emphasis on protecting consumer interest and ensuring that competition is not unduly distorted is an appropriate interpretation of the Trust's Fair Trading Policies.

A respondent also stated that the illustrative examples in the Guidelines of potential sources of harm and ways of minimising negative impacts were overly-simplistic and potentially misleading. The BBC considered carefully the respondent's comments but believes that the illustrative tables provide an important and effective means of explaining the concept of the CIP to BBC staff.

A respondent requested that a row should be added to the table of illustrative examples of potential negative impacts to include the scenario whereby the BBC obtains third party content rights (such as sports commentary or talent) on an exclusive basis, in quantities which go beyond those which are necessary to fulfil the public purposes or at above-market rates. The BBC has included a new illustrative example in Table I referring to the potential impact of the BBC knowingly overpaying for programme inputs.

A respondent proposed that the CIP should be strengthened and requested new rules in the Guidelines covering specific types of BBC activity. For example, it suggested that the BBC should avoid acquiring opportunities to broadcast live performances, interviews with artists and other programming inputs in quantities beyond those necessary to fulfil its Public Purposes and/or on an 'exclusive' basis. The BBC agrees that such actions that could, in some instances, raise Fair Trading concerns. However, it believes the CIP should be applied on a case-by-case basis taking into account all relevant market characteristics, including normal business practice.

A respondent stated that the Guidelines should require the BBC to seek external assistance in assessing the likely competitive impact of areas of BBC activity which are particularly likely to raise competition concerns. It suggested that the Trust may be better placed than the BBC to make qualitative judgements about the BBC's competitive impact. It added that external consultants or Ofcom are also likely to be helpful sources of information and analysis. The BBC believes that within the context of its Charter and Agreement obligations that specify the functions of the Trust and Executive the implementation of the CIP is an activity that is more appropriate to be undertaken by the BBC Executive. The functional and operational separation between these three parties would be compromised in such a scenario. It would not

be possible, for example, for the Trust to hear a complaint regarding a particular Fair Trading issue that it had advised on previously. In a similar vein, a respondent stated that the BBC should undertake a consultation in advance, with businesses that might suffer harm from its actions. As required by the Trust's Fair Trading Policies the BBC adopts a proportionate approach to the CIP assessment taking into account the size and scale of the activity concerned and the particular circumstances. The level of analysis and supporting evidence that is required will vary depending on the context.

A respondent also requested that the distinction between the application of a Public Value Test and the CIP should be clarified. We have made appropriate clarifications to the Guidelines to address this.

A respondent stated there was too much ambiguity with the language used in the Guidelines (e.g. what constitutes a "distinctive" service?). The BBC notes those concerns and has updated the Guidelines accordingly, providing examples of how distinctiveness could be assessed in the online world.

### **The 4 Commercial Criteria (Chapter 2 of the Guidelines)**

This Chapter of the Guidelines provides examples of what constitutes a Commercial Service, a Commercial Trading Activity and other key categories of activity. All Commercial Services and Commercial Trading Activities must comply with four basic requirements, known as the 4 Commercial Criteria ("4CC"). They must:

- fit with the BBC's Public Purposes;
- exhibit commercial efficiency;
- not jeopardise the good reputation of the BBC or the value of the BBC brand; and
- comply with the Fair Trading Guidelines and in particular avoid distorting the market.

The Guidelines provide guidance on how the 4CC are implemented.

There were very few points made by respondents about the 4CC. One respondent noted that the guidance on the application of the 4CC – including the test for market distortion – was adequate (subject to certain points made elsewhere in its response).

Another respondent stated that the 4CC have not provided an adequate restriction on the BBC's commercial ambitions in the past and cannot be expected to do so in the future. The BBC believes that the 4CC – including the test for market distortion – are fit for purpose and provide an appropriate level of control over the scope and nature of the BBC's Commercial Activities. The general issue of whether the 4CC framework is an appropriate mechanism to manage the remit of the BBC's commercial activities is more appropriate to be addressed in the Trust's review of its Fair Trading Policies in 2010.

### **Separation (Chapter 3 of the Guidelines)**

The BBC has three key sources of funding – licence fee income, commercial revenues and grant-in-aid (for BBC World Service). The BBC must implement an appropriate degree of separation between these different funding sources to ensure that, inter alia, the BBC’s Commercial Activities gain no unfair advantage from the BBC’s Public Service Activities. The Guidelines provide detailed guidance on how the BBC achieves such separation. For example, they specify the BBC’s approach to setting prices for the provision of goods and services between the BBC’s Public Service Groups and its Commercial Subsidiaries.

A respondent stated that the rules on transfer pricing provided the BBC with too much flexibility, leading to the possibility of cross-subsidy between the BBC’s Public Services and its Commercial Services. For example, a respondent was concerned that the draft Guidelines stated that prices should ‘normally’ be set in line with prevailing market practice. The respondent suggested that the BBC should always seek to set prices in line with market practice. The response also suggested that the BBC should always seek out external market information to validate this policy. These three points have been addressed by clarifying the text of the Guidelines, which now emphasizes clearly the primacy of market practice (at paragraph 3.13) as ‘the key principle’ of fair transfer pricing. The wording on prices ‘normally’ being set with regard to market practice has been removed.

As regards the use of external market information the Guidelines explain (at paragraphs 3.21–3.26) the role of the Commercial Agency in practically assisting the BBC to price in line with the market context and obtaining ‘full value’ for its rights.

A respondent also raised a concern that the only absolute requirement of the Guidelines is to cover incremental costs. The revised Guidelines make clear that prices would only ever be set in relation to incremental cost if this conforms to market practice—which is consistent with the primacy of market practice as the key principle of fair transfer pricing. Even then, in exceptional cases where prices are similar to incremental costs, the prior approval of the Fair Trading department is required.

Where market practice is not verifiable, the revised Guidelines require a cost-oriented price to be set which seeks to reflect all appropriate costs, rather than solely incremental costs (paragraph 3.16). The BBC believes that this addresses the respondent’s concern that BBC commercial ventures would not bear all reasonable costs in the event that comparable information on market practice is not available, and therefore also addresses concerns in relation to potential cross-subsidy.

The BBC agrees with the respondent’s point that the ‘most simple and transparent route’ to separation is for prices to follow market practice and that a cost-based transfer price can be appropriate when evidence on market practice is unavailable. Any request to deviate from this approach would require the prior approval of the Fair Trading department. The revisions to the Guidelines are intended to make the role of these two routes (market practice and cost-based) clearer to external stakeholders.

Two respondents stated that there should be greater transparency in the pricing provisions of the Guidelines. They noted that the Guidelines fail to provide any indicative rates of return for the commercial exploitation of the BBC's public service assets relying instead on references, for example, to 'appropriate' contributions to overheads. The BBC believes that it would not be appropriate to include minimum or target returns in the Guidelines. In light of the primacy of market practice, and the alternative of cost-oriented prices, it is unnecessary (and in any case impractical) for the Guidelines to specify appropriate commercial return for every BBC commercial venture – the assessment of what constitutes an appropriate return will vary according to the nature of the goods/services being supplied and the market context.

A respondent stated that the methodology used by the BBC to establish compliance with the requirement for separation was flawed and could only be addressed by a more fundamental review of the BBC's Fair Trading framework. For example, it stated that the arrangements for sales of rights between the BBC and BBC Worldwide were not on an arm's length basis and such arrangements would not exist in the commercial world. The respondent considered that the Guidelines should be amended to re-define the role of the BBC's Commercial Activities and to insist that programme rights should be exploited on a case-by-case basis with transparent market testing. The BBC believes that the existing arrangements between BBC Worldwide and the BBC are consistent with the requirements of the Trust's Fair Trading Policies and such arrangements are not uncommon in the marketplace. We do not propose making any amendments to the Guidelines but note the Trust's ongoing review of the BBC's Commercial Activities which touches on many of the issues raised by the respondent.

### **Use of BBC brands (Chapter 4 of the Guidelines)**

BBC brands cover anything that might suggest a good or service has originated from, or is associated with, the BBC (e.g. programme brands). The Guidelines require inter alia that BBC brands must not be used to endorse the activities of the BBC's Commercial Subsidiaries or third parties. The Guidelines provide detailed guidance on how the key principles on use of BBC brands are applied in practice – for example they outline the Fair Trading considerations associated with the sponsorship of BBC Public Service events.

A respondent expressed concerns that the guidance on sponsorship appeared to permit the BBC to continue to accept sponsorship for on-air Public Service events. It also expressed concern that the BBC was continuing to seek sponsorship for licence-fee funded events and also to cover these events on-air. It stated that the Guidelines should be revised, stating, inter alia, that the BBC will not accept sponsorship for any on-air BBC event. The BBC's policy towards sponsorship of Public Service events has been revised following last year's [Trust investigation into Sports Personality of the Year](#). The BBC's proposed new policy on sponsorship is subject currently to a [public consultation](#). The proposed new policy is clear that sponsorship of on-air Public Service events is permitted only in very limited circumstances. The purpose of the Fair Trading Guidelines is not to define BBC policy but to outline the Fair Trading considerations associated with BBC activities.

However, the Guidelines make clear that sponsorship must comply with the BBC's Editorial Guidelines and related guidance.

Another respondent welcomed the changes to the Guidelines following the Trust's investigation into sponsorship of Sports Personality of the Year and the clarification of the BBC's policy with regard to sponsorship. It stated that the changes accurately reflect the judgement by the Trust that the BBC's sponsorship activity is subject to the CIP. The respondent stated that its primary concern with this aspect of the Guidelines was that it stops short of prohibiting on-air references to a third party sponsor of an on-air BBC event. It believes that this omission is unwarranted and places the BBC at risk of trading unfairly. Furthermore the respondent stated that the Guidelines should outline a policy covering editorial references to third parties associated with artists (e.g. ticket agents). The BBC believes that the appropriateness or otherwise of on-air references of this nature is primarily an editorial issue to be covered by the [BBC's Editorial Guidelines](#). As noted above the BBC's proposed new policy on sponsorship is currently the subject of a separate public consultation.

A respondent stated that the guidance on use of BBC brands should be expanded with regard to its use in third party marketing materials. The BBC believes that existing guidance is sufficient in this area and that a more prescriptive approach could, for example, prevent legitimate marketing activities from taking place.

### **Other points raised**

A respondent suggested that the Guidelines should be expanded to provide greater transparency about who is responsible for implementing the Trust's Fair Trading policies for individual services. Annex I to the Guidelines explains how the BBC fulfils its Fair Trading obligations with a centralised team of advisers providing expert advice to all BBC staff including training, approvals, information and analysis. It also notes that each Group/Subsidiary Director appoints a Fair Trading Representative, typically a member of the Group Management Board with responsibility for compliance. Furthermore a network of 'Fair Trading Representatives' and 'Fair Trading Champions' exist throughout the BBC, with responsibility for promoting and supporting the Fair Trading regime. The BBC believes that Annex I provides an appropriate level of detail on its compliance structures. Adherence to Fair Trading obligations is mandatory and is the responsibility of every member of BBC staff. If there is any doubt as to how the BBC's Fair Trading obligations should be discharged, staff are required to seek expert advice from the BBC's Fair Trading department.

## **Annex I – Consultation questions**

### **General observations**

Question 1: Overall, how effective do you consider the Guidelines to be in implementing the BBC Trust’s Fair Trading Policies?

### **Competitive Impact Principle (“CIP”)**

Question 2: Do the Guidelines adequately explain how the BBC implements the CIP (i.e. how it endeavours to minimise its potential negative competitive impacts)?

Question 3: Is the distinction between a Public Value Test and the CIP clear?

### **The 4 Commercial Criteria (“4CC”)**

Question 4: Do the Guidelines adequately explain:

- (a) the distinction between those activities that are subject to the 4CC and those that are subject to the CIP?
- (b) how each of the 4CC applies to the BBC’s Commercial Services and Commercial Trading Activities?
- (c) the test for market distortion?

### **Separation/Pricing**

Question 5: Do you have any comments about the guidance provided to ensure an appropriate degree of separation between the BBC’s licence fee-funded, commercially funded and grant-in-aid-funded activities?

Question 6: Do the Guidelines provide a clear explanation of the BBC’s approach to transfer pricing and benchmarking?

### **Branding**

Question 7: Is there sufficient clarity as to:

- (a) how and when third parties may be able to use, or associate themselves with, BBC brands?
- (b) how Fair Trading applies to the sponsorship of BBC Public Service events?

### **Compliance**

Question 8: Does the description of the compliance and reporting controls which the BBC has in place adequately explain how the BBC delivers on its Fair Trading obligations?