



PSB NETWORK PLATFORM RE-TRANSMISSION AND ACCESS CHARGES IN THE UK

THE CASE FOR CHANGE

JUNE 2011

SUMMARY

Free to air networks across the world have obtained direct access to audiences through allocated analogue terrestrial (and more recently largely through digital terrestrial) frequencies and transmitter networks. But across the globe a significant proportion of TV households now receive their main free to air network TV channels through cable or direct broadcast satellite systems (and most recently through telecom/internet based delivery systems). These systems tend to be primarily focused on delivering pay TV services but have in the process become some household's default method of reception for all TV services. Free to air networks have to agree access terms to these additional TV delivery systems – these arrangements are most often referred to as “re-transmission” terms.¹

O&O analysis shows the UK has the least generous TV re-transmission terms for free to air networks when compared with a wide range of comparable developed world markets - including the USA. In all developed markets reviewed apart from the UK, platforms make some kind of contribution to broadcasters and/or content providers in return for re-transmission.

Platforms make three types of contribution in return for leading free to air network re-transmission:

- (i) copyright fees paid to broadcasters, producers and authors (based on copyright law that prevents retransmission without terms being agreed between broadcaster and delivery system);
- (ii) meeting any incremental transmission costs associated with making the channel available to consumers using the platform; and/or,
- (iii) providing privileged terms of platform/set top box access (at worst accepting a “must carry” obligation for no fee, and, in some cases (most notably the USA), making a payment to the channels for re-distribution).

In all developed markets apart from the UK, regulations demand at least one of these contributions from platforms, and in some cases all three. These arrangements are made in recognition of the considerable value to platforms of not being excluded from the carriage of the leading network channels in the market and the contribution the leading networks make to new content investment.

¹ The general term “re-transmission” in this context refers to both the onward carriage of the signal to the TV household and viewer access to the appropriate signal through the set top box. With Digital satellite systems it tends to refer primarily to viewer set top box based access as in many countries (although not all) the channels arrange their own uplinking and satellite transmission capacity.



In addition, in countries where the main free to air networks also have specific Public Service Broadcasting (PSB) obligations – such as specific programming requirements and, perhaps most importantly, a universality obligation – transmission fees are also paid in recognition of the cost of these obligations to those broadcasters.

Furthermore, regulatory intervention to help set the terms of re-transmission is based on the recognition that normal commercial negotiations between leading networks and third party platforms are unlikely to lead to an optimal outcome (something accepted even in the USA).

By contrast, in the UK where all the main free to air network services have PSB requirements, including universality obligations, there exists only limited copyright protection, significant access fees are paid by the main free to air networks to platforms for re-transmission and the broadcasters have to meet their own satellite retransmission costs.

More specifically, while all the main free to air (PSB) networks in the UK are given a “must offer” obligation across all distribution systems, the BSkyB satellite platforms has no “must carry” obligation and the free to air networks enjoy no copyright protection when being retransmitted by UK cable systems.²

While there is regulatory intervention to help set retransmission terms via the BSkyB platform, the regime³ adopted explicitly allows BSkyB to charge the PSB networks a significant contribution to the platforms set top box and marketing costs based on the revenue generated by the PSB networks from BSkyB homes (about 37 per cent of all UK TV homes by the end of 2010), while taking no account of the value the free to air networks bring to the platform or the public benefit they generate.

The UK arrangements represent a diversion of funds from service and content investment towards the financing of platforms. Comparing the UK arrangements to those in the US, for example, £72m to £96m a year is being diverted from content/channels to platforms in the UK.⁴

The next few years are likely to see a growth in the proportion of homes utilising satellite and cable systems as their default reception method for all TV channels and a proliferation of new TV delivery platforms utilising internet and mobile based distribution systems as well as new satellite delivery platforms. If the current UK regime is not changed, an increasing level of resources is likely to be diverted from content/channels in the UK to platforms when contrasted with the more generous arrangements for broadcasters in other parts of the world.

The UK needs to reform its system so that it is more in line with measures taken across the developed world. This report has considered five potential changes:

² The cable TV systems are specifically exempted from copyright obligations in this respect by Section 73 of the Copyright, Designs and Patent Act of 1988.

³ The terms are regulated under the Television Platform Service (TPS) access regime administered by Ofcom within the EC Access directive that demands Fair, Reasonable and Non Discriminatory (FRND) terms of access for all users of a television platform offering access to third party services.

⁴ This represents the potential difference between the £16.5m payment from channels to the Sky DSAT system with the £55m to £80m income to channels if copyright payments, transmission costs and carriage fees were paid to networks as they are in the USA (at the same per household level as applies in the USA).

- (i) the adoption of a US style “re-transmission consent” regime for the UK;
- (ii) removing the “must offer” condition from the PSB networks to the satellite platform and allowing the PSB networks to negotiate terms collectively;
- (iii) a mandated “must carry” regime on all significant TV platforms for no fee;
- (iv) a mandated “must carry” for no fee regime combined with a removal of any “must offer obligations; and,
- (v) a re-configured TPS access regime for BSkyB (where the PSB channels value to the platform is taken into account and/or only incremental carriage costs charged to the PSB networks).

Of the five changes proposed, a mandated “must carry” regime on all significant TV platforms with no fee paid by channels is likely to provide the most simple solution, lead to some increased investment in programming by PSB channels but not lead to any increased pay TV prices for consumers.

A further move to a combined “must carry for no fee” plus “no must offer” regime, or even a US style “retransmission consent” regime, while it might prove more complex to implement would be likely to result in more monies being invested in programming and a relatively small increases in pay TV prices to consumers – probably less than 20 pence per month.

Even if such a change to the re-transmission regime were difficult to achieve in practice there are strong arguments for, at the very least, amending the way the TPS regime is applied to PSB networks in the UK.

INTRODUCTION

The BBC has commissioned Oliver & Ohlbaum Associates (O&O):

- to review TV network re-transmission arrangements across a range of developed TV markets;
- to assess the UK's arrangements in this global context;
- to review the likely implications of continuing with the UK arrangements in a multi-platform, multi-device web 2.0 age;
- to assess the rationale for intervention in general, and then for changing the approach in the UK; and,
- to review the potential impact on consumers of any change.

Section A of the report looks at (1) why there is a need for the re-transmission of free to air networks, (2) the policy/regulatory issues it raises, (3) the ways in which the issue has been approached across the developed world, and (4) the rationales for regulatory intervention- rather than leaving terms to normal commercial negotiation.

Section B then reviews the UK arrangements in this global context. In particular, (1) it reviews the UK's current pattern of TV reception; (2) the UK's current re-transmission arrangements (3) the specific details of the TPS regime that applies to the BSkyB satellite platform (4) the financial consequences of these arrangements when compared with typical arrangements across the globe, and (5) the potential justifications for the differences between the UK regime and other developed markets.

Section C then reviews likely UK platform developments over the next 5 to 10 years and the financial consequences if the UK regime is not changed.

Section D then considers alternative interventions that could be adopted in the UK market in terms of simplicity and fairness, and the likely consequences for consumers.

In summarising the national arrangements for re-transmission across the globe the report recognises that these are often quite complex, can be subject to interpretation, have in some cases changed over time and in many cases are not fully transparent. The O&O report attempts to obtain the most up to date and comprehensive information on such arrangements across the globe. However, its main focus is to draw some general conclusions on the overall balance of benefits and costs between platforms and free to air network broadcasters across several markets rather than to provide a precise account of each regime.

A. CONTEXT

TV households now receive their TV signals through a variety of distribution systems. The traditional method of direct terrestrial UHF transmission (initially analogue and now largely digital) to TV households has been increasingly substituted by cable and direct satellite dish reception which has become the default means of reception of all TV services (including the main free to air networks) in a growing number of TV homes across the world. While many such homes can often still receive a terrestrial signal if they choose to do so, some cannot.

Even where homes can still receive the terrestrial signal, they have often disconnected their UHF aerial and/or use the satellite or cable service EPG (electronic programme guide) as their interface with all TV channels. For all practical purposes, main free to air networks now have to seek retransmission via cable and satellite to ensure they reach all TV households. For purely commercial free to air networks the need to reach all households is driven by advertisers, who reward high reach networks with higher prices. For PSB networks this economic need is often reinforced by a specific universality requirement of their broadcast licence.

The need for retransmission via alternatives to the traditional UHF terrestrial system then raises three issues: (1) is the retransmission of the signal protected by copyright (and if so what should the copyright fee be)?; (2) should the free to air networks have any right to prominence on third party delivery system EPGs?; and, (3) how should terms of retransmission (and set top box access) be set (by free negotiation or through regulatory intervention)?

All developed countries have decided to set the terms of retransmission (and access) via cable and satellite systems through some form of regulatory intervention, recognising that a purely commercial negotiation between leading free to air networks and platform providers is unlikely to lead to an optimal outcome. While the non UK developed markets studied for this review differ in the type and scale of intervention adopted, all of them offer the main free to air networks some form of privileged access to third party TV delivery systems and provide copyright protection of the network signal.

Some national regulatory regimes make explicit arrangements for copyright fees to be paid to channels and content owners. In a few markets (such as France), the third party satellite platform also pays for the main networks' satellite re-transmission costs.

1. The Need for Re-Transmission of TV Signals

TV broadcasting began in earnest in the developed world after World War II. A small number of free to air broadcasters were given access to scarce terrestrial UHF frequencies and transmitter networks were built to use these frequencies to bring the TV services to the vast majority of the population. However, countries differed in how important they ranked channel reach versus channel choice.

Some countries reused available frequencies to ensure a small number of channels reached well over 90 per cent of the population – building masts in remote areas and filling in transmission black spots in major urban areas - while other countries used the frequencies to bring a larger average number of services to major urban areas, but left a significant proportion of the population with no signal or a very poor signal.

The lack of good quality reception in parts of a national market led to the development of cable relay systems from the 1950s onwards - especially to serve urban transmission black spots or to bring good quality reception in new build apartment blocks where set top aerials were insufficient to get a reliable signal. So while in some countries cable relay was bringing TV services to about 5 per cent of the population (as in the UK in the 1960s) in other countries such as the USA , cable relay was necessary for about 20 per cent of the population.

In continental Europe, cable relay systems were also used to receive overspill free to air channels from a neighbouring country, especially if the domestic market had a restricted choice of only heavily public service channels (as in Germany, Belgium and Holland). A weak terrestrial signal, a high level of new build apartment blocks after the war, plus carriage of overspill networks helped cable relay grow to more than 50 per cent of households across parts of continental Europe.

The advent of relatively low cost satellite TV transmission from the 1970s onwards helped these cable relay systems expand their choice of channels leading to higher build out and take up of cable. In the USA this included the first satellite delivered premium pay channel –HBO – and the so called local superstation – where Ted Turner retransmitted his local Atlanta based station across the US through cable. This not only helped cable build and take up grow to over 50 per cent of households but also allowed the cable operators to start charging consumers relatively high prices for access.

The advent of higher powered direct to home satellite broadcasting in the late 1980s meant consumers had a third choice for TV reception, the satellite dish. These systems initially carried a large number of free to air services, but soon developed as pay TV operators as they encrypted their signals so that only homes with the relevant authorised set top box could receive the services. Finally, the advent of digital terrestrial, cable and satellite transmission has enabled each system to increase the number of channels available and has led to the development of the electronic programme guide (EPG) as the main effective means by which viewers choose the channels and programmes they watch (as the prospects of having to continually scroll up and down 200 plus channels to see what is on, becomes impractical).

While today's cable and satellite TV systems (and to a lesser extent digital terrestrial systems) carry a large number of encrypted pay TV services, they also still relay the main free to air networks in each country ensuring they can be received no matter what one's choice of TV system. Given the pattern of TV reception that has built up all free to air networks need some kind of retransmission on cable and satellite systems, over and above their direct access to terrestrial frequencies and transmitters (now largely digital), in order effectively to reach 90 per cent plus of the population.

However, in some countries, the need for retransmission is due to their not being a decent terrestrial signal available to 20 per cent or more of the population, in others a decent signal is available but households have disconnected their terrestrial aerial having used alternatives for so long, while in others terrestrial reception is available from the aerial to the TV set, but they just tend to use a cable or satellite set top box and its related EPG as their default system of choice (usually because it is the means for obtaining the pay TV services they want or because it offers enhancements such as High Definition or Digital Video Recorder functionality).

But whatever the reason for different household reception choices, if a free to air network wishes to reach over 90 per cent of the national population (either because this high reach helps raise their

advertising rates and their income, or because they have been given a mandated universality obligation in return for their access to terrestrial frequencies), they have to arrange for retransmission on cable and satellite.

In practical terms to effect retransmission the cable systems usually simply take the local terrestrial transmitter signal and re-transmit in the relevant area. But for satellite retransmission, a free to air network needs to secure transponder capacity on the relevant satellite (one located in the correct part of the sky to be received by the relevant satellite systems household dishes). Unfortunately, if the free to air network has local/regional versions of its channel, it has to get satellite capacity for each of these local versions to be transmitted from the relevant satellite.

2. The Policy/Regulatory Issues Raised

There are three main policy/regulatory issues raised by the need for free to air networks to secure retransmission. First, does this retransmission imply the re-use of copyright material by the delivery system, and if so, does that mean some kind of mandated/arbitrated copyright charge should be made to the delivery system.

Second, should the free to air networks have any rights to a specific slot on the third party delivery system EPGs (and if so, how should that be regulated).

Thirdly, who should be charging who for retransmission – (1) the delivery system charging the free to air network for use of its system to reach viewers it otherwise might not reach, or (2) the channel charging the delivery system for the benefits conferred on the delivery system from having access to the channel. More broadly, what obligations should there be on the delivery system to distribute the free to air networks and/or the networks to make their services available to each delivery system.

The issue of EPG prominence is not covered by this review although it is clearly related to carriage issues. How various countries in the developed world deal with the issues of copyright and access fees/arrangements will be covered in more detail below. But first, we set out below the generic arguments for regulatory intervention in the setting of access fees between the platform and the free to air network.

3. The Rationale For Regulatory Intervention of Access Fees

A Simple Model of Carriage Negotiation

The setting of re-transmission charges (both the size and direction of payments) in a purely commercial market would be with reference to (1) the incremental value to the individual broadcasters of the incremental reach from a given platform, and (2) the loss of value to the given platform from non-carriage of the individual channel.

In a fragmented TV market, with many network channels and many platforms - all with quite small incremental household penetration but with universal and overlapping technical availability - the two factors above are likely to be quite small.

An individual platform owner would know that an individual channel would suffer some small loss of revenue without carriage (from the loss of viewing on that platform from viewers who chose not to

switch to another platform just because the channel was absent). Similarly, an individual channel owner would know that the loss of its free to air channel would only cause a small amount of harm to a specific platform (from those viewers who chose to switch platforms just because of the absence of its channel).

The small amounts of transferred value in each case and the countervailing leverage of each party would be likely to lead to a zero or near zero charge between a free to air channel and platform.

Complicating Factor One – Universality Requirements

The first factor to complicate the simple model of carriage fee setting above is the universality requirements on the free to air networks – both explicit and implicit. Publicly funded free to air networks around the world are expected to be available to all households. This expectation is often linked to the licence fee funding that applies to many which makes a charge on every TV owning household.

In some markets, this explicit universality requirement is also extended to leading advertising funded free to air networks in return for their access to still scarce digital terrestrial frequencies and their regulated prominence on EPGs. And even where an explicit universality requirement does not apply, the business model of leading free to air advertising funded networks tends to demand a 90 per cent plus market reach, making the loss of access to any significant platform disproportionately damaging to the channel's economics.

The effective universality requirement means that free to air networks do not have the freedom to withhold their channels from a platform when negotiating access fees, this gives any platform engaging in commercial carriage negotiations an opportunity to extract a large proportion of any economic rents that flow to the channel from access to the platform in a free negotiation.

Over and above this imbalance of bargaining leverage, universality requirements often come from an implicit assumption that making a service available to the whole population confers some extra public value from both the shared experience and the levels of investment in indigenous programming required of free to air networks. It is possible that universality requirements on broadcasters can give a delivery system the opportunity to benefit not just from all the incremental revenue value of carriage but also from the extra public value derived. In short, the investment in content made by the free to air networks is only worthwhile if available to all (hence the universality requirement), but in order to obtain this universality a platform can demand a fee from the broadcasters that actually diverts funds from programming investment (and hence investment in public value).

Complicating Factor Two – Dominant Platforms

The second complication factor comes where a dominant platform operator exists. This is less about the total market share of all TV homes covered by a specific platform than the ease of substitution away from this platform by consumers. Where there is only weak substitution between TV platforms, either due to technical limitations or because unique services and functionality make it unlikely consumers will switch platforms, a given platform is unlikely to see its households migrate to an alternative provider if it were to lose access to one or more free to air networks.

In this case the potential loss to the free to air network from loss of carriage (especially if the platform also has a significant share of all TV homes) is far greater than the potential loss to the platform from not having access to the channel. This gives the platform the opportunity to extract all the economic rents from the channel provider.

Complicating Factor Three – Dominant Channels

A third complicating factor for the simple model of carriage access fees is the existence of dominant channels. In these circumstances, the platform faces a large loss of households if it fails to secure a given network, while the network only faces a small loss of audience if the platform refuses to carry the channel. In such circumstances, the channel has the opportunity to extract all the economic rents accruing to the platform from its carriage of the channel.

The Implications of these Complications

A lack of substitution between platforms when channel line ups change or a lack of substitution between channels when a channel refuses to allow access to a platform can lead to the need to intervene in the carriage market to ensure a fair price of access is set between platform and channel. The existence of universality obligations on free to air networks in recognition of the public value they create implies that intervention needs to be with reference not just to a fair commercial price but the overall impact on public value of a given set of access charges and terms.

4. Approaches Across the Developed TV Markets

O&O has reviewed the re-transmission arrangements across nine developed TV markets in addition to the UK market (See Appendix 1). It has reviewed the approach to copyright and access fees/arrangements in each of these markets. During its review O&O also noted that in several markets satellite platforms pay for the transponder capacity needed to make satellite retransmission of free to air networks possible. Appendix 1 summarises the arrangements in the UK, USA, France, Spain, Germany, Netherlands, Sweden, Canada, Australia and South Korea. Set out below is a brief summary of findings. Figure 1 summarises the results conceptually and shows that the UK's arrangements are the least generous to free to air broadcasters.

Copyright Protection and Fees

Across much of continental Europe and the USA re-transmission of leading free to air networks is protected by copyright (i.e. they need the channel's permission to re-transmit) and is accompanied by an obligation on platforms to pay a copyright fee which is then shared between the broadcasters, producers and authors of TV works/programmes. While in Europe this tends to apply mainly to cable re-transmission (raising about €90m a year), in the USA it applies to both cable and satellite re-transmission.

Figure 1 – Generosity of access / retransmission regimes to free-to-air network broadcasters

	COPYRIGHT FEES PAID TO BROADCASTER / PRODUCER	CARRIAGE / ACCESS TERMS FAVOUR FTA BROADCASTERS OVER PLATFORMS	EXTRA TRANSMISSION COST PAID BY PLATFORMS
UK			
US			
GERMANY			
FRANCE			
SPAIN			
SWEDEN			
NETHERLANDS			
CANADA			
AUSTRALIA			
SOUTH KOREA			

Carriage/Access Payments

Most of the developed world imposes a “must carry” obligation on leading delivery platforms to carry PSB channels and all leading free to air network services. Such “must carry” obligations are often accompanied by “must offer” obligations on the leading channels, with no fee payment either way (either from platform to channel or channel to platform) for access. These arrangements tend to apply to cable and satellite retransmission.

In the USA, however, there is no “must offer” obligation, instead leading free to air networks (or to be more precise the local affiliate station to a leading network) can opt to withhold their services from re-transmission unless a fee is paid (referred to as the “retransmission consent”). This gives broadcasters significant leverage over platforms, even dominant platforms such as local cable systems, as they are given both a generous fall-back position (i.e. demand “must carry” with no access fee and extra transmission costs paid by the platform where necessary) and the ability to choose to negotiate a fee from the platform as an alternative. (See more on the US system in sub-section 5 below).

Incremental Transmission Costs

In most markets PSB and leading free to air networks have direct access to their own terrestrial transmission system (which will be entirely digital in the UK by 2013). While cable re-transmission usually does not lead to any incremental transmission costs (the cable systems simply pick up the over-the-air terrestrial signal and relay it to consumers), satellite re-transmission often requires extra payments for relevant transponder capacity.

In several markets surveyed the satellite platform owner picks up these extra transmission costs for PSB channels (most notably Canalsatellite in France).

5. The USA Market in More Detail

The structure of the US channel and platform markets changes the positions of platform and channel compared to the simple market model outlined above. In short, the platforms have less to lose from non-carriage of a network affiliate than the channels have to lose from being blacked out from a platform.

In the US the terrestrial signal is not really universal. About 20 per cent of US homes receive a weak or no signal from their local network affiliate over the air, they rely on cable and/or satellite retransmission. In addition, the long history of cable in the US means that many households or apartments have no connected terrestrial aerial.

This means that if a network affiliate station disappears from the local cable system, some households will find it impossible to pick up the channel by alternate means (they do not have access to a sufficiently strong terrestrial signal nor a satellite dish connection) while others will actually switch to the rival pay TV platform – either Dish TV or Direct TV . However, the likelihood that a home will switch from cable to DSAT (even if they could), or vice versa, just because one of the local network affiliate station is missing is small.

In a free market, without effective universal terrestrial free to air reception, the leverage would go to the platform provider. Of course, if all the local network affiliates in the USA could negotiate as one entity, this might provide countervailing market power to the platforms – many viewers really would move to DSAT if all the local network affiliates were not available on cable.⁵ However, some viewers would simply not be able to get DSAT reception (causing a public outcry) while the competition authorities would probably prevent collective bargaining by all the network affiliates together (and even if they did not, it would be in the interests of one of the networks to do a deal if the others did not, undermining any collective bargain position).

This is why the US has the “re-transmission consent” system. A platform cannot “black out” a local affiliate (they can always insist on carriage even though they have to accept they get no fee), but a channel can withdraw from a platform (and demand a fee). This rebalances the leverage between platform and network affiliate.

⁵ Recent consumer research by Needham & Co in the USA suggested that the availability of the main network schedules through broadband would be the content most likely to get cable consumers to “cut the cord” on their cable subscription and use broadband to feed their TV instead.

B. THE CURRENT UK SYSTEM

DTT reception of the main networks is currently available to about 93 per cent of TV households via roof top aerial reception, and by 2012, following analogue switch off, this will rise to 98.5 per cent. However, technical availability is not the same as actual availability. Many households no longer connect their main TV set to a rooftop terrestrial aerial either because they actively choose to use cable or satellite as their default reception method or they live in apartment blocks which have adopted cable or satellite as their main feed system. A significant proportion of cable and satellite households (about 35 per cent) now chose to use this system to connect all the TV's in their homes.

Furthermore, even in those cable and satellite households that retain the ability to receive DTT signals to their main or extra TV sets, the main cable or satellite system EPG is their default interface with all TV channels (pay and free). This preference has probably increased since the introduction of the personal video recorder (PVR) functionality of Sky Plus and VPlus, where viewers can only access their stored programmes through the cable and satellite system EPG. DTT reception, although technically near universal, is in practice far from it.

The Freesat system developed by the BBC and ITV does offer main network reception to satellite reception households without the need for a BSkyB set top box and EPG. However, if BSkyB was to drop a PSB network channel from its system, viewers would either have to switch boxes and EPGs or go searching for the channel on the BSkyB tuner every time they wanted to watch the channel. So while Freesat does offer viewers the ability to receive network TV via satellite without needing to subscribe to BSkyB, in those households that want to continue to subscribe to BSkyB (37 per cent of all TV households in the UK) it does not offer network channel providers an effective alternative route to the viewer.

The UK does have a regulatory regime designed to help ensure the reception of the main PSB networks on all TV access systems. However, it is one that gives no copyright protection to the main PSB networks for their retransmission on cable (which removes the ability of the network owners to demand any payment), and which allows significant charges to be made to the main PSB networks for their distribution via the BSkyB satellite system.

The rationale for this regime seems to be based on (1) the belief that DTT and Freesat reception give the main networks effective alternative routes to using the BSkyB system to reach TV households, and (2) that the main PSB networks should not be allowed to extract the value they bring to distribution platforms and the public more generally, while BSkyB platforms should be allowed to extract the value they bring to the main PSB networks.

In reality, the main PSB networks do not have effective alternative routes to cable and satellite households that remain pay TV subscribers. A regulatory system that ignores the value the main PSB networks bring to distribution systems and the public more generally is not going to deliver a socially or economically optimal outcome.

1. The Market for TV Signal Reception in the UK

System Coverage

The UK analogue terrestrial signal was near universal for the BBC1, BBC 2, ITV1 and Channel 4⁶, and once digital switchover is complete by the end of 2012, the Digital Terrestrial TV (DTT) signal will be near universal for all the BBC's digital channels, ITV1, Channel 4 and Channel 5 – available via roof top aerial to 98.5 per cent of the UK population. Furthermore, those homes that cannot receive DTT⁷ will probably be able to receive Freesat (a satellite service operating from a satellite system co-located with the Sky pay retail package channels and which can be received using the same dish as for Sky services).

However, while the main network PSB broadcasters in the UK can achieve near universal technical coverage through DTT and Freesat, TV connectivity to and within UK homes means that in practice universality is far from guaranteed by DTT and Freesat reception.

TV Connectivity – The DTT Alternative

Over half of UK TV homes currently connect their main TV set to either Virgin Media (cable) or BSkyB (pay satellite system). While many of these main TV sets do have the ability to switch to DTT easily (as DTT reception is built into their digital sets) a significant proportion (about half) do not have such a facility and would have to go and buy a DTT (Freeview) set top box to do so. In addition, about one third of all BSkyB and Virgin Media homes have actually disconnected their TV set from the UHF aerial, and would therefore have to reconnect their TV set to the aerial in order to receive TV signals via DTT.⁸

Although many extra sets in BSkyB and Virgin Media main set households are currently connected to DTT ready TV sets or set top boxes (about 50 per cent), about forty per cent get their extra set connectivity through BSkyB or Virgin Media through their multi-room connectivity options. In any event, extra set connectivity to DTT would imply that in order to receive free to air networks if they were no longer available on BSkyB or Virgin Media the consumer would have to move to viewing on their secondary set.

In short, while DTT based reception of the main PSB networks is currently available technically to about 93 per cent of UK homes, and will be available to 98.5 per cent of homes once analogue switch off is complete at the end of 2012, there are significant practical impediments to continued reception of a free to air network via DTT in cable and BSkyB homes should a channel be dropped from the BSkyB or Virgin Media system.

⁶ Although for C4, its coverage in Wales was replaced by S4C, which mixed in C4 programmes with its schedule of local output

⁷ The DTT service in the UK goes under the brand name of Freeview, which is the name for the reception boxes and the EPG interface.

⁸ See O&O, Battling for the Media Consumer Research, Dec 2010

TV Connectivity – the Freesat Alternative in DSAT Homes

While DTT reception of the main PSB networks may be impractical for many BSkyB homes, it might be contended that Freesat availability to the same receiver dish effectively guarantees universality to any PSB channel dropped from the BSkyB system. This might imply that BSkyB enjoys less potential leverage over PSB networks than Virgin Media. While Virgin Media is a closed TV distribution system where alternative access to the home might only come from DTT access, BSkyB is an open system where channels can gain technical access to the home by seeking transmission on a co-located satellite system – as Freesat has done.

However, in practice, should a PSB network fail to gain a carriage agreement with BSkyB and instead rely on Freesat access to the DSAT home, the consumer would either have to seek out that channel outside of the BSkyB EPG on their set top box or load the Freesat EPG on to their set top box.

As it is not possible to run two EPGs on the same set top box, the consumer is faced with one of three choices. First, having two set top boxes and switching to the Freesat box should it want to view the PSB network that has been dropped by BSkyB, or, second, buying a Freesat ready TV set and switching to the TV set EPG every time they want to watch the dropped channel, or, third, switching out of the BSkyB EPG and searching for the channel on their TV tuner every time they want to watch the channel.

Given the efforts involved, it is likely that the dropped channel would suffer a significant drop in effective universality and audience share. Conversely the harm to the platform provider of dropping just one of the PSB network providers is likely to be minimal (indeed it might even be positive if viewing share switched from the dropped PBS network to a channel owned by the platform provider).

The outcome might be different if all the PSB networks were to fail to reach agreement with BSkyB.⁹ In such circumstances one might expect the consumer to be prepared to deal with the inconvenience of switching EPGs, buying a Freesat set or seeking out the channels through the TV tuner to gain access to all the PSB networks, which still account for about half of all viewing in BSkyB homes. But such collective action is unlikely, may be deemed to be anti-competitive and is inherently unstable (it's always in the interest of one of the PSBs to opt out of the collective action and do a carriage deal with BSkyB). Such collectively would have to be mandated on all PSBs to be effective.

TV Connectivity – the OTT Alternative in Cable Homes and DSAT Households

Over the next 5 years an increasing number of TV homes are likely to be able to receive on demand TV services on their TV set via their broadband internet connection (so called Over the Top TV services (OTT) of which Youview is a prime example). It is possible, should broadband networks provide "multicast" functionality for broadcasters, that broadcasters will be able to offer their live streamed PSB network service through such a system to TV sets in homes with a broadband connection.

⁹ O&O research suggests that 38 per cent of BSkyB and Virgin Media homes would consider changing their preferred pay TV provider if all the PSB networks were only available by switching to a Freeview signal for instance.

It might be argued that such a system gives the PSB networks guaranteed access to TV sets in both BSkyB and, for the first time, Virgin Media homes, which implies that the broadcasters have sufficient leverage with both systems to come to commercial arrangements without the need for intervention.

However, the same issues will apply as do to the Freesat alternative in BSkyB homes. While it is possible to gain access to such homes using OTT distribution, consumers would still have to connect a second set top box, or buy a OTT ready TV set, or find their own way of transferring the broadband signal to the TV set in order to gain access to any channel dropped by Virgin Media or BSkyB. Such inconvenience would be bound to harm any specific PSB network that failed to gain access to the BSkyB or Virgin Media EPG.¹⁰

In addition, even with "multicast" technology, these systems might struggle to provide simultaneous live coverage of the same programme to millions of homes, exactly the key requirement of a leading free to air network in the UK.

2. The Current UK Re-Transmission Regime

Must Offer Conditions Applied to All PSB Networks.

All the UK PSB networks in the UK have universality requirements (in exchange for the benefits they receive) and a specific must offer requirement within their terrestrial licences. All the PSB networks also have additionally strong incentives to secure carriage on all platforms. For the BBC, acceptance of household licence fee funding is underpinned by universal access to the services financed by that mandatory licence fee. For commercial funded PSB networks, the loss of effective access to even small proportions of the available audience can harm their unique proposition to advertisers.

Only Loose Must Carry Obligation on Cable, No Such Obligation on BSkyB

Cable systems in the UK do have a must carry obligation for PSB networks. However, because cable systems have been exempted from copyright based retransmission payment obligations, Virgin Media can effectively re-transmit the main PSB networks without being obliged to pay the PSB networks any money. There is no mechanism for the networks to deny the cable systems their signal and demand a charge for providing it. In practice, this has meant that the must carry obligations that exist have never needed to be enforced.

BSkyB has no must carry obligations in the UK. As an "open system", the regulations implicitly assume that PSB networks can go directly to DSAT households and receiver dishes without the need to go through the BSkyB set top box access system if they wish.

¹⁰ BSkyB's own evidence to the BBC Trust and Ofcom objecting to YouView actually recognises the role of the preferred EPG in determining viewing choice in households. In the case of BSkyB's evidence this was used to protest against the Youview EPG becoming the preferred access point for on demand content in TV homes, the same argument can be applied to the role of the BSkyB EPG for all linear channels in DSAT homes.

Cable Exempt from Copyright Charges, BSkyB Effectively Zero Rated

In the UK, cable systems are specifically exempted from copyright fees. While satellite is not exempted, the UK Government recognises that this fee is effectively zero at the moment as the leading copyright owners have no leverage by which to extract any value from the satellite platform.

The Specific TPS Access Regime Applied to the BSkyB Platform

While BSkyB has no must carry obligation and effectively has its copyright charges zero rated, access terms to the BSkyB platform (effectively access to their set top box through their conditional access system) for the main free to air networks are regulated. (This regime applies to all channels – pay and free, both within the Sky retail pay proposition and outside the Sky pay proposition).

BSkyB has made itself an open system, whereby channels can gain access to their viewers directly rather than having to be a part of the BSkyB retail pay package (this is in contrast to the cable systems where payment of a cable subscription to Virgin Media guarantees reception of the main PSB networks through the cable system).

As an open TV delivery system, BSkyB's terms of access are regulated pursuant to the terms of the EC Access directive (2002/19/EC) that requires that terms to all users – third party and the Sky retail package - are set in a Fair, Reasonable and Non Discriminatory (FRND) way. Within this framework Ofcom has set out its interpretation of FRND pricing and some guidelines for charging which BSkyB's charging regime complies with.¹¹

The principles of the regime have been applied to all users of the platform including free to air TV channels, and in particular the free to air PSB networks. Details of the TPS regime are highlighted below.

3. The Television Platform Services (TPS) Access Framework for the BSkyB Platform

PSB networks are charged for their Electronic Programme Guide (EPG) slots and for the regionalisation of their services (i.e. ensuring the correct regional version of the channel appears in the correct EPG slot). The level of charges that can be made for such services is based upon a calculation of the satellite systems total costs (including a reasonable return on capital investment) and then an allocation of costs to each channel that uses the platform based upon the incremental value to that channel of access to BSkyB homes (almost 9.2 million in the UK by the end of 2010).

The largest single user of the Sky platform is the Sky pay TV retail operation, and as one might expect leading channels in the Sky retail package such as Sky One are assigned among the highest carriage costs as they derive the highest incremental income from having access to the Sky platform – subscription and advertising income.

However, as the leading PSB channels have the highest audience shares in the UK and the commercially funded PSB channels enjoy the highest advertising yields per viewing hour, the PSBs also end up making a significant annual payments to BSkyB (currently totally £16.5m a year). Charges

¹¹ Ofcom has also investigated whether within the TPS market BSkyB can be deemed to have significant market power which might lead to a different type of regime, but this investigation is still on-going.

to the BBC are set with reference to the "hypothetical" advertising based value of their incremental audiences on the BSkyB platform.

O&O research suggests that the UK is the only developed market where a satellite platform is allowed to make platform access charges to the leading free to air networks.

4. The Rationale for the UK Approach

Two main arguments are put forward for the UK's unique approach to free to air network retransmission. First, UK PSB broadcasters receive significant direct funding (via the licence fee) and indirect support (through privileged access to spectrum and EPG prominence) and so there is no need to enforce copyright and/or levy a copyright charge on re-transmission platforms as is the case in the US and across continental Europe.

Second, the existence of near universal DTT and co-located Freesat (able to access BSkyB homes) in the UK means households can gain access to the PSB networks without the need to go through the main pay TV platforms (in contrast to the US where poor digital terrestrial transmission reception and the absence of a co-located free satellite mean that access is often only possible through the chosen pay TV system).

As far as the UK's retransmission regime is concerned, access fees and terms for PSB networks on cable are a non-issue, as networks enjoy no copyright protection over the re-use of their signal by cable providers (under Section 73 of the Copyright, Designs and Patents Act of 1988). Even though a must carry obligation can be called upon within current legislation should a cable system deny access to a PSB network in the UK, this provision has never been relevant as cable systems can take the signal off air and retransmit for no fee as there is no copyright protection.

BSkyB's constraints on charges to the PSB networks are not set by the re-transmission regime but rather by the TPS access as applied in the UK which requires BSkyB to establish an FRND access pricing regime for all channel users.

This regime is designed to (1) ensure third party pay TV channels can gain access to BSkyB households without being part of the Sky pay TV retail package, (2) ensure that BSkyB does not earn an excessive rate of return from its platform and (3) ensure BSkyB does not design its access charges so as to distort competition in the pay TV retail market in its favour.

5. A Critique of the Current UK Approach – Three Levels of Critique

A critique of the current system for setting retransmission fees in the UK market can be made at three levels. The first is a critique of the retransmission regime itself. The second, is a critique of the use of the TPS regime as a way of regulating PSB access charges to the BSkyB platform, and the third, relates to potential errors in the way the TPS regime has been applied to the PSB networks.

The Retransmission Regime Fails To Recognize Platform Bargaining Leverage in the UK

The existence of DTT and a co-located Freesat system are seen as sufficient guarantors of universal PSB network access to UK households and a constraint on any potential charges that might be levied on the PSB networks by specific platforms.

In reality, the significant consumer inconvenience caused if a PSB network were to lose carriage on either the Virgin Media or BSkyB platform, and the subsequent likely loss of effective reach and share for the dropped service, means that the platform providers enjoy significant bargaining leverage over any individual PSB network provider. The PSB networks "must offer" obligations further reduce their bargaining leverage with platforms. Furthermore, whatever bargaining leverage the PSB networks might enjoy over cable is completely undermined by the absence of copyright protection – the networks cannot stop the cable systems retransmitting their signal.

Leaving the negotiation of access fees largely to a commercial deal between the parties (under a general FRND framework with respect to BSkyB) enables the platforms to extract a large proportion of the economic rents attributable to the channels from carriage but does not allow the channels to extract the value of their benefit to the platform (given the channels have must offer universality obligations for BSkyB and no copyright protection on cable they cannot effectively threaten to withdraw their channels from the platforms while the platforms can drop the channels).

The Retransmission Regime Fails to Recognize the Public Value Created by PSB Networks

Universal access to PSB networks creates significant public value. Universality is itself one of the sources of public value – a shared experience, equal access to all UK households – and a means of maximising the impact of other sources of public value – such as investment in indigenous UK content and PSB heavy genres.

In so far as platforms are able to act in a way that either denies PSB networks effective universal access or charge fees that divert funds from investment in PSB content (funds provided by the licence fee or the gift of terrestrial spectrum), the current retransmission regime is reducing the effective public value of the UK PSB system.

The TPS Regime is Not the Appropriate Framework for Determining PSB Access Charges

The level of charges to PSB networks for access to platforms should be set with regard to the specific bargaining leverage and public value issues raised by PSB carriage and not by reference to a system designed primarily to deal with a fair pricing structure for mostly pay TV channels based on their incremental revenue from the platform.

The TPS regime allows for no calculation of the public value benefits of PSB carriage nor the inability of PSB networks to extract the commercial value of their carriage to platforms through the threat of withholding their channels (given their universality requirements).

Other things being equal, this is likely to apply higher fees than appropriate to the free to air PSB channels as it neither recognizes the public value of these channels, nor the two sided nature of free to air commercial TV, where significant unrealised consumer value is being created by advertiser funded networks to the benefit of the platform.

The Charging Mechanism Adopted by the TPS Regime is Wrongly Applied to PSB Networks

Application of the TPS regime is not only wrong in principle but has also been applied wrongly in practice. Calculation of incremental income of the free to air commercial networks should be made with reference to the difference in the revenue they would make from gaining access to the BSkyB

platform and that revenue they would make if viewers were forced to seek out the channel on Freesat or DTT. At the moment the charges are based just on the revenue from the BSkyB platform, not the difference with the next best alternative.

In addition, the use of an effective advertising income proxy for the BBC (by using the comparative BBC audience share to commercial PSB channels as the guide) takes no account of the significant impact on the UK advertising market should the BBC be funded by advertising and effectively assumes the UK advertising market is infinitely elastic (something Ofcom's own studies have shown not to be the case).

The allocation of a proportion of all platform marketing charges (based on relative incremental income with a host of pay TV services), to PSB networks, when the vast majority of these marketing expenses are concerned with selling various tiers of pay TV is inappropriate. In addition, the inclusion of marketing expenses in the cost allocation formula means that the PSB networks are effectively subsidising the competitive strategy of BSkyB in the pay TV market and the success of a platform whose growth actually damages their overall audience share, and in the case of commercially funded PSB networks, their revenue.

This regime also implies that the more competitive the TV platform market is, the more monies the PSB networks have to pay to maintain carriage to their audience.

D. THE FINANCIAL CONSEQUENCES OF THE UK'S APPROACH

1. The Current Financial Impact of the UK Approach

There are four factors to take into account when trying to assess the cost to channel operators and content producers of the current UK approach to re-transmission of free to air networks. First, the current payments being made to the Sky DSAT platform by UK PSB channels – a payment not made in any other developed market reviewed for this report.

Second, the foregone carriage fees from all current platforms – something that applies in many markets across the world. Third, the absence of any copyright payments in the UK – charges which are made in most European territories and the USA. Lastly, the direct satellite transmission costs paid by UK channels, often gifted to free to air networks by leading DSAT platforms overseas. Each area is reviewed in more detail below.

Payments for DSAT Carriage

As outlined above, BSkyB charges the UK PSB networks for access to its DSAT platforms under the Television Platform Services (TPS) access regime set by Ofcom in 2006. Total annual charges to PSB networks currently run at almost £16.5m per year. The details of how these charges are arrived at and the various different components of the charges are contained in Appendix II.

In broad terms Sky charges for EPG listings, access to the its interactive TV system, regionalisation of the network channels where relevant (e.g. ensuring people in Wales get ITV1 Wales on slot 103 on the EPG), and access to its set top box. While the EPG listing, interactive access and regionalisation charges are based on standard fees per channel charged to all users of the platform, the set top box access charge is based on BSkyB's need to recoup its set top box roll out and marketing costs from all users of the platform (including Sky retail) on the basis of their "ability to pay". For PSB networks this charge is based on the estimated advertising revenue that accrues to those networks in DSAT homes (for the BBC audience share is used as a proxy for advertising revenue).

In terms of the set top box costs that can be included when calculating such a charge these include marketing, set top box subsidy and subscriber acquisition costs as well as the technical costs of maintaining the system. This means that the more aggressively Sky compete with other platforms (such as cable and DTT) for home connectivity the larger the fees that can be charged to PSBs for access to the DSAT system.

No account is currently taken in the TPS access regime of the potential value to the platform from carrying leading PSB channels (i.e. the loss of consumer uptake that might result from failure to carry the main PSB channels). While the Ofcom review of TPS did recognise that platform value was an issue it maintained it was too difficult to measure.

Foregone Copyright Payments

Cable systems in the UK are specifically exempted from the copyright charges for re-transmission that apply in much of the rest of Europe. While digital satellite is not exempt, the UK Government recognises that in effect no copyright payment is charged. The copyright charges that apply to cable systems in much of Europe (in those countries such as Belgium, the Netherlands and Germany where cable is the dominant distribution system) tend to be about £2 per relevant TV household per year. With total UK Sky digital satellite and cable households in the UK totalling about 13 million in 2010, this would mean extra potential income of £26 million in 2010 if the UK adopted the European view.

Foregone Carriage Payments

The US system of re-transmission consents allows the network station affiliates to extract carriage fees from both cable and satellite systems. Such payments are either monthly carriage fees or sometimes agreement to place extra "spin off" channels in favourable positions on the relevant EPG. Where carriage fees do apply, such as in the USA, they tend to be set at around 5 to 10 cents per month per household per network broadcaster.

A similar approach in the UK could yield £5m to £10m per year per network, or £25m to £50m across all five main PSB networks.

Satellite Transmission Costs

In the UK the PSB networks pay their own satellite transmission costs, which in many other countries (such as the USA and France) the relevant satellite platform makes capacity available. Current fees for transmitting the PSB networks in standard definition (plus the regional versions for ITV1, BBC1 and BBC 2) amount to approximately £5m per year.

Overall

The US system of re-transmission provides for copyright payments from both cable and satellite delivery, the payment of broadcaster transmission costs in the case of satellite platforms and the payment of carriage fees (where broadcasters opt for the re-transmission consent route) in the case of both cable and DSAT platforms.

If the UK were to adopt the US system and similar charges were set by broadcasters then rather than paying out £16.5m in 2009 the UK PSB networks and associated content providers would be gaining £55m to £80m a year. This represents a difference of between £72m and £96m a year. (See Appendix III for details of calculation).

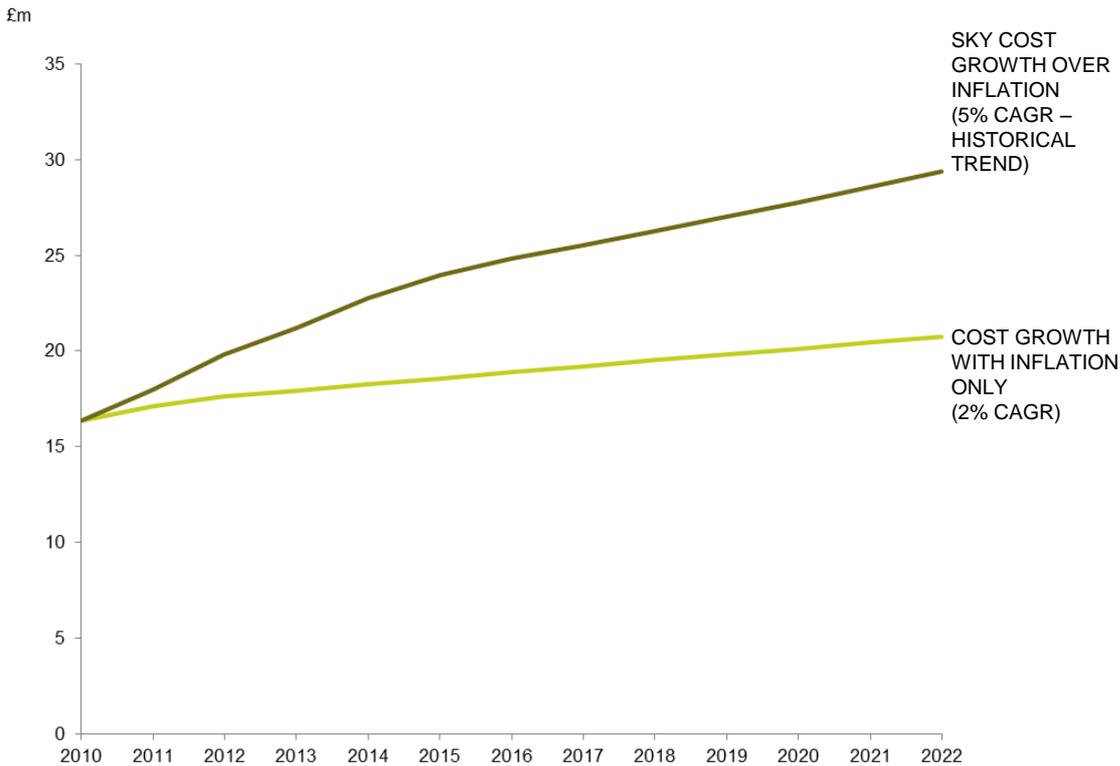
2. The Future Financial Impact of the UK Approach

Going forward, if no changes were made to the UK system, fees paid by the PSB broadcasters would be likely to increase significantly for two main reasons. First, BSkyB's marketing and management costs have been growing by about 5 per cent a year driven by a desire to drive up subscriber acquisition within the UK platform market and to increase customer ARPU (average revenue per subscriber from tiers of pay TV channels and features such as HDTV, Sky Plus and broadband connectivity).

The current TPS regime is based on an allocation of these costs to each user of the platform based on relative attributable revenue. Other things being equal access fees to the PSB networks are likely to rise by up to 5 per cent a year over the next 10 years or so, reaching almost £30m a year by 2022.

Even if the share of costs allocated to the network PSBs declines – either because their audience share in BSkyB homes falls or the attributable pay TV revenue to pay channels increases, it is likely that payments will grow by 2 per cent a year.

Figure 2 – Likely future payments by UK PSB networks to the Sky platform



Second, over the next 10 years it is likely that a number of new delivery systems will emerge bringing TV channels to UK households and individual's mobile devices. This is likely to be a combination of new satellite delivered services, IPTV service without Freeview access built in, over the top (OTT)

based internet services that offer multicast or streamed versions of the main PSB networks and mobile services either delivered through customised spectrum/capacity for linear channels.

Given the universality and must offer requirements that apply to the PSB networks any system that builds up a reasonably significant user base will be asking for fees in return for making the PSB networks available to their customers. The TPS regime sets a precedent for setting such charges with relation to the costs of running the platform and the share of consumption accounted for by the main PSB networks. Furthermore, the more competitive the platform market becomes, the greater the marketing and management costs per household reached are likely to be, and, therefore, the higher the charges to the PSB networks.

D. POTENTIAL REMEDIES AND SOLUTIONS AND THE IMPACT ON CONSUMERS

There is a strong case for reforming the current PSB network re-transmission and access regime in the UK. However, there are several potential ways in which the system could be reformed to help set a fairer price for access. Any reform must be assessed in terms of the likelihood that it will result in a fairer outcome, the ease of implementation, and any competition law issues that might be raised.

Across all potential forms of reform, any modification must also be assessed in terms of the likely eventual impact on consumers. But such an assessment of impact needs to reflect the two-sided nature of broadcast markets, and review both the likelihood of raised prices for platform access and the likelihood of increased investment in content by the PSB networks.

1. Five Potential Alternatives

This review has looked briefly at five potential changes to the current system of access regulation in order of increasing levels of intervention – starting with a system that simply allows the PSB networks to bargain collectively within the current regime, through to the imposition of a US style re-transmission consent regime aimed at allocating most the bargaining leverage to the PSB channels. In between these two extremes, reform of the existing TPS regime and mandated “must carry” for all platforms and removal of “must offer” for all relevant channels are also examined.

Collective Negotiation

O&O commissioned consumer research suggests that 37 per cent of BSkyB and Virgin Media households would consider switching pay TV provider if none of the PSB services (all the BBC networks plus ITV1, Channel 4 and Channel 5) were available on their main EPG (and they had to switch to Freeview or a Freesat EPG/set top box every time they wanted to watch these channels). Such a collective action would clearly do harm to the platform that could not agree carriage terms that might be approaching or equal to the harm caused to the audience share of the PSB channels in those homes that decided not to switch platforms.

While collective action might secure better terms from platforms with no must carry obligation there are several reasons to believe such a system might be problematic. First, collective action would have to be defended within UK and EC competition law which usually condemns such behaviour. Second, collective action would have to be mandated rather than just allowed, as it would still be possible for a platform to re-establish its superior leverage over the PSB networks as a whole by striking slightly more generous terms with one or two providers, and then raising its fees to those that remained without carriage.

Lastly, even if collective negotiation could be mandated (perhaps by vesting carriage negotiation rights in a jointly held organisation) the must offer and universality obligations of the PSB networks would need to be modified in order for them to engage in a negotiation process that led to any protracted stand off period where their channels were not available.

A Re-configured TPS Regime

The TPS regime could be adjusted to make specific provision within the cost allocation process for account to be taken of the potential benefits the PSB channels bring to the platform and the broader public benefit created from their reception. However, as previous reviews of the TPS regime have made clear, these factors are difficult to quantify.

In addition, without a must carry obligation on BSkyB it is still possible for BSkyB to withhold carriage if it believes the fee to be insufficient compensation. The problem is not so much with the way the charges are calculated (although there are plenty of issues in this area as well) but more the regime for setting prices, which is a light touch FRND framework. This regime would not stop BSkyB denying the PSB networks access while arguments over the appropriate fee continued.

Mandated Must carry for No fee on All Platforms

A mandated must carry of PSB networks for all significant third party TV platforms in the UK (which currently applies only as a back stop power with cable in the UK) would mean that no platform could deny the PSB networks carriage. Given the universality and must offer obligations that apply to the PSB networks this would be likely to result in carriage/access for no fee in the UK.

While this would still leave PSB networks in the UK with no copyright fees (which many networks in developed markets receive) and paying their own satellite transponder costs, it would avoid their highest current expense, namely access fees for the BSkyB platform. Such an approach would be based on the assumption that the platform and public benefits of PSB network access were at least as high as the platform carriage benefits to the PSB channels but avoid the need for on-going detailed calculations and manoeuvring every time the carriage deals came up for re-negotiation.

It would also ensure that PSB networks would not see their carriage costs rise as the number of platforms rises and the competitive battle between them intensifies.

Mandated Must Carry, And No Must Offer

This would have a similar impact to the previous intervention, but with the added ability for the PSB networks to withhold their services in order to extract some kind of fee from the platforms. It would, in effect, mirror the US retransmission consent framework in all but name. The only difference being the lack of a formal framework for resolving any protracted fee dispute and absence of PSB channels on the main TV platforms.

A "Re-Transmission Consent" Regime for the UK

The re-transmission consent regime in the US places much of the bargaining leverage with the free to air networks, they can either elect for must carry with no fee, or withdraw their channels (they have no must offer) and hold out for a fee. The regime is adopted in the US due to the inability of these networks to secure high reach access without carriage on the main cable and satellite systems. In the US there is no open system alternative to retail package carriage by cable operators and direct satellite platforms, and DTT coverage is nowhere near universal.

This effectively means that the cable and satellite systems are able to extract significant extra revenues from subscribers by delivering the main free to air networks to their TV sets, and the networks themselves are handed the ability to extract some of that value added through the re-transmission consent regime.

While this review has shown that despite the existence of Freesat and Freeview the availability of the PSB networks on cable and satellite platforms does create value for these platforms it is unlikely to be as high as that created by the free to air networks in the USA (where there is no free satellite system, and where effective DTT reception is limited).

2. The Likely Impact of Changes on Consumers

A move to a "must carry" regime across all platforms in the UK, would be likely to lead to an end to the £16.5m per year of fees paid by the PSB networks to BSkyB, and an avoidance of future likely higher charges from BSkyB and other new platforms to emerge over the next 10 years. A move to also ending "must offer" or even to adopt a more formal retransmission consent type regime could allow the PSB channels to extract a fee from the platforms. While these fees would be unlikely to be as high as those achieved in the US (on a per TV household basis) they could yield £15m to £25m a year for the channels in payments from the platforms, representing a total switch of funding from platforms to PSB channels of £35m to £40m a year.

Given that platform costs are unlikely to reduce due to this change, the platforms will have to recoup the lost fees from other channel providers using their platform.

In order to assess the overall impact of this change on consumers we need to have regard to the likely increase in consumer prices that might occur and the likelihood that the broadcasters will use the released funds to create more programming to the benefit of consumers of the free to air channels.

A Limited Direct Consumer Price Impact is Likely

The likely impact on consumer prices depends on which of the five alternative intervention regimes is adopted.

The introduction of a must carry for no fee regime would only impact BSkyB (as Virgin already pays no fee). If all BSkyB's lost platform revenue was recouped from other users of the BSkyB platform, most notably the Sky retail package, and these costs were then passed on to all retail BSkyB customers, each subscriber would have to pay about £1.70 a year more, or about 14 pence per month more.

However, it is not clear that given the current structure of the UK pay TV market that all such costs would be passed on to BSkyB subscribers. BSkyB pay TV prices in the UK are set with reference to the ability of consumers to pay and the pricing of rival offerings, not the marginal costs of the BSkyB retail offer.

A move to must carry with no fee would not increase Virgin Media's costs or prices, this in turn would be likely to mean that BSkyB would not be in a position to raise retail prices for pay TV packages even though BSkyB Retail would be incurring higher charges from the BSkyB platform.

The most likely result of the loss of access fees to BSkyB from public service networks, and a re-apportionment of these costs to Sky Retail, would be slightly reduced margins for Sky Retail, and not any increase in Sky's consumer price.

If the regime was changed to either a "must carry but no must offer" regime, or perhaps a "retransmission consent" regime, then not only might BSkyB end up paying £15m to £25m to the PSB channels, but, more importantly, Virgin Media would also end up paying monies to the same channels. The raising of costs to a number of rival platforms would be more likely to be passed on to consumers, although the actual rise in price would be likely to reflect just the fees paid by Virgin Media and BSkyB to the PSB channels not the total recoupment of BSkyB's financial loss (which could be a total of about £32m to £42m a year compared to the current regime –i.e. the lost £16.5m from the PSB channels plus the extra £15m to £25m now paid to the channels).

The likely outcome would be a reduced margin for Sky retail and some increase in consumer prices across all pay platforms in the order of £2 per year – or less than 20 pence per month.

There Would Be Indirect Consumer Benefits of Content Investment

While consumer prices would be unlikely to rise significantly, and even then only if Virgin Media and BSkyB ended up paying fees to PSB channels, it is very likely that most of the financial gain for the PSB networks would end up in more programming spend by these channels and increased consumer benefits. Both the BBC and Channel 4 are non-profit maximising entities, Channel 4 being commercially funded but being required to carry out a public service remit within a general requirement for sufficient financial reserves to remain viable in the long term. The BBC is required to use its revenues to maximise public benefit.

Both Channel 4 and the BBC would be likely to use the released carriage monies from BSkyB to fund more programming. While ITV and Channel 5, as profit maximising broadcasters might be tempted to simply boost their profitability, the extra programme spending by their closest rivals – BBC1, Channel 4, BBC 3, BBC 2 etc would be likely to encourage them to put at least some of the monies gained back into their schedules. Given current UK network market dynamics, therefore, it would be likely that a high proportion of any saving would end up enhancing channel schedule to the benefit of viewers in the two sided free TV market.

In particular, an intervention which removed the current payment by PSB channels to BSkyB but that did not increase Virgin Media's costs would be unlikely to increase consumer prices while shifting a high proportion of the £16.5m a year currently paid by PSB channels from Sky Retail's profit margin into programming spend by the PSB networks.

A stronger form of intervention where BSkyB and Virgin Media both ended up paying fees to PSB channels, might increase consumer prices by £2 per year, but would be likely to result in increased programming spend by PSB channels of c£40m a year.

