

# BBC Trust

## BBC Store regulatory approval

27 March 2013

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# 1. The Trust's decision

## 1.1. Introduction

- 1.1.1. In July 2013, the BBC submitted proposals to the Trust to make available a broader range of BBC programming, on a commercial basis, via a BBC branded website, 'BBC Store'. While the proposal was for a commercial service, it involved a level of integration with, and changes to, BBC Online (and in particular, iPlayer) one of the UK public services.
- 1.1.2. In addition to undertaking a commercial service approval<sup>1</sup> therefore, the Trust also had to establish whether the proposed changes to iPlayer were significant, thereby triggering a Public Value Test. This document sets out the Trust's decision in respect of both the commercial service approval and the 'significance' of the proposed changes to BBC Online.

## 1.2. Decision on commercial service assessment

- 1.2.1. Requirements concerning the BBC's commercial activities are set out in the BBC Charter and Agreement. As a commercial service, BBC Store must align with the overarching commercial strategy of the BBC, and satisfy the requirements within the Charter and Agreement for separation. It must also comply with all of the criteria set in the Agreement for commercial services:<sup>2</sup>
- it must fit with the BBC's public purposes
  - it must exhibit commercial efficiency
  - it must not jeopardise the good reputation of the BBC or the value of the BBC brand
  - it must comply with the fair trading principles and in particular, avoid distorting the market.
- 1.2.2. Having considered each of these requirements, and sought external economic and privileged legal advice as part of our deliberation, we are satisfied that the proposals meet these requirements and can therefore be approved, subject to the following conditions.
- A review of some form in two years' time to confirm that the transfer pricing regime is operating as envisaged under proposals.
  - Confirmation that the [- **REDACTED** -] brand royalty payment from BBC Store (refer to section three), constitutes a cost item for BBC Worldwide.
- 1.2.3. We also noted the importance of ensuring that there was adequate delineation of paid-for and free content and a clear explanation of the rationale for charging. We are therefore asking the Executive to pay particular attention to this requirement in their initial design work and on an ongoing basis.
- 1.2.4. A summary of our commercial assessment is set out at section three.

## 1.3. Decision on 'significance' assessment

- 1.3.1. The proposed changes to iPlayer that arise as a result of BBC Store include:
- An extended search functionality that includes both public service and commercially available BBC content;

<sup>1</sup> A summary of which is provided at section 3.2 of this document.

<sup>2</sup> Clause 69.

- The inclusion of links to BBC Store and other commercial outlets retailing BBC content;
- A seamless purchasing experience via pop-ups and a single BBC account registration;
- The ability to view programmes purchased from BBC Store via iPlayer and playback this content using iPlayer.

1.3.2. Having taken account of Ofcom's advice and completed its assessment, the Trust has formed the view that these changes do not constitute a significant change to the UK public services. It has therefore decided that a PVT is not required. In reaching this decision the Trust considered the likely impact of the proposals, their novelty, proposed duration and financial implications.

## **1.4. Changes to the key characteristics of a service**

1.4.1. While we do not consider the proposals to be significant, they do require changes to the 'key characteristics' of the BBC Online and Red Button service licence. While these are minor changes, Clause 25(3) of the Framework Agreement states that where proposed changes require the alteration of key characteristics of a BBC service licence (as is the case here) the Trust should presume that the changes ought to be subject to a PVT, unless it can justify departing from the presumption. Section four summarises our assessment of significance and our decision to depart from that presumption (given our conclusion that the proposed changes are not significant). The Trust will publish separately the changes to the BBC Online and Red Button service licence that arise as a result of these proposals.

## 2. Background

### 2.1. Introduction

2.1.1. In July 2013, the Executive submitted proposals to the Trust to make available a broader range of BBC programming, on a commercial basis, via a BBC branded website, 'BBC Store'. While the proposal was for a commercial service, it involved a level of integration with BBC Online (specifically, iPlayer) and because of this it triggered both commercial and public service regulatory procedures:

- a. As a commercial service, under the Charter and Agreement, BBC Store had to undergo a commercial service approval;
- b. If the commercial service was approved, it would necessitate changes to BBC Online, and the Trust therefore also had to consider whether these changes were significant, thereby triggering a Public Value Test ('PVT').

2.1.2. This document provides an overview of: (a) the commercial assessment and how we reached our decision regarding the commercial service approval, and (b), our decision as to whether the changes to iPlayer are significant (i.e. whether a PVT is necessary).

### 2.2. Overview of BBC Store

2.2.1. While BBC Store will not affect the programming available free of charge as part of the BBC's public services, it will supplement the public service offer by making available a broader range of BBC programmes, on a commercial basis. It will offer new programmes and a selection of archive content to buy and keep in digital form, via a BBC branded website. The proposal will, over time, open up a significant portion of the archive providing audiences with an opportunity to watch and own titles from the BBC's library collection.

2.2.2. At launch it will offer around one year's worth of recent programmes (c. 6,000 hours) and 4,000 hours of archive content, including around 3,000 hours of older titles that are currently available commercially (for example, on DVD or download-to-own). The remaining 1000 hours will be editorially selected. The Executive hopes to release a further 500-1000 hours of archive programmes each year. As a commercial service, BBC Store will be provided through BBC Worldwide, a commercial subsidiary of the BBC.<sup>3</sup>

### 2.3. Summary of proposed changes to iPlayer

2.3.1. BBC Store requires a level of integration with, and changes to, BBC Online (specifically, iPlayer). These comprise:

- An extended search functionality that includes both public service and commercially available BBC content;
- The inclusion of links to BBC Store and other commercial outlets retailing BBC content;
- A seamless purchasing experience using pop-up windows and a single BBC account registration; and
- The ability to view programmes purchased from BBC Store via iPlayer<sup>4</sup> and playback this content using iPlayer.

<sup>3</sup> The BBC's commercial services must be organisationally separate from its public service activities. The BBC itself cannot directly provide commercial services. Such services must be provided through commercial subsidiaries, the Agreement, clause 68.

<sup>4</sup> Made possible by integration with a cloud-based digital locker belonging to BBC Store.

- 2.3.2. Launched in 2007 as a catch-up service, the scope of iPlayer is defined in and governed by the [BBC Online and Red Button](#) service licence, and any proposed changes must be considered with reference to that document.

## 2.4. Regulatory process for determining 'significance'

- 2.4.1. Under the terms of the BBC's Framework Agreement, the Trust may from time to time need to undertake assessments of certain BBC proposals in order to determine when a PVT must be applied. The PVT is a formal assessment process requiring: the Trust to assess the public value of the proposed change; Ofcom to assess the market impact of the proposed change; and two periods of public consultation. Ordinarily the overall assessment process lasts around six months and is both intensive and time consuming. The Trust recognises its responsibility to undertake a PVT where there is evidence that a proposal constitutes a significant change to the BBC's UK Public Services (in this case, to BBC Online and iPlayer).
- 2.4.2. In deciding whether a proposal constitutes a significant change, the Trust must have regard to the four considerations set out in clause 25(2) of the Framework Agreement; that is:
- Impact
  - Financial implications
  - Novelty; and
  - Duration of the proposed change
- 2.4.3. In 2011 the Trust made a commitment to expand its relationship with Ofcom to take full advantage of its understanding of the wider communications sector and, in particular, to invite Ofcom to provide its view of the 'impact on others' (e.g. providers or potential providers of alternative products and services) of a proposal from the Executive that the Trust considers should be subject to a significance test. Ofcom's view of the 'impact on others' will inform the Trust's decision in respect of its significance test, and in particular, the Trust's view of the 'impact on others' of the proposed changes.
- 2.4.4. This document relates specifically to proposals concerning BBC Store. As set out in clause 25 of the Framework Agreement, whether proposals in the end meet the criterion of significance is a matter for the judgment of the Trust.

## 3. Commercial service approval

### 3.1. Introduction

3.1.1. When a proposal is referred to the Trust for approval, we take into account whether it fits with the agreed commercial strategy and satisfies requirements in the Charter and Agreement for separation. We also consider whether it complies with the four criteria for commercial services, in particular, whether it:

- Fits with the BBC's public purposes
- Exhibits commercial efficiency
- Does not jeopardise the good reputation of the BBC or the values of its brand
- Complies with the fair trading principles and in particular, avoids distorting the market

3.1.2. The regulatory procedure for commercial services is different from the process we follow for public services but, subject to commercial confidentiality, we can, and do, report publicly on decisions that have been subject to our specific consideration. We therefore set out below a summary of our decision in respect of BBC Store.

### 3.2. Summary of findings

#### Fit with the agreed commercial strategy

3.2.1. We first had to consider whether the proposals fitted with the overarching commercial strategy; proposals for BBC Store support a sub-set of the BBCW strategy which focuses on developing routes to market in the UK and ways in which to:

- Enhance the public service on-demand offer with a wider range of content;
- Build a direct relationship with audiences to ward against the effects of disintermediation
- Improve access to BBC archive content; and
- Devise business frameworks and strategies that secure the best return for LFPs.

#### Satisfies the requirements for separation

3.2.2. We then had to consider whether, as a commercial undertaking, it met requirements within the Charter and Agreement for separation. The proposals envisage a level of integration between iPlayer and BBC Store: for example, there will be a 'seamless user journey' from iPlayer to Store as a result of the planned search functionality; BBC staff will be deployed in development work connected to BBC Store; and BBC Store will rely to some extent on iPlayer technology developed using licence fee funding, (such as users being able to play out DTO content via iPlayer). We therefore considered whether the proposals comply with the requirement imposed by the BBC Agreement that there be both structural and financial separation between the BBC and its commercial services. We are satisfied that they do comply.

3.2.3. Clause 68 of the Agreement provides that the BBC 'as a corporation' must not directly provide any commercial services (and such services must therefore be provided through commercial subsidiary companies). The fair trading guidelines state (at paragraph 3.5) that, 'there must be transparent operational and accounting separation between the BBC's public service activities and its commercial activities'.

3.2.4. In line with the guidelines, the Executive has told us that accounting and operational separation will be achieved via detailed contracts between the public service and BBC Store regarding access to iPlayer infrastructure and any further services which BBC Store requires. Such separation also

ensures that commercial services do not receive a selective advantage from the public service and that State Aid law is therefore not breached. The contracts mentioned will also set out the market-based transfer price which BBC Store will pay to the BBC for any public service assets it uses. This will ensure that the BBC is fully reimbursed for such assets and is not subsidising BBC Store. This is considered further below.

- 3.2.5. We are therefore satisfied that the BBC itself will not be supplying any part of the BBC Store commercial service, otherwise than under arrangements to secure a transparent separation between public service activities and commercial ones. We also consider that, editorially, it will be clear to users that BBC Store and iPlayer are separate services.
- 3.2.6. Clause 75 provides that the BBC may not use licence fee revenue to fund any activities carried on for the purposes of any commercial service. It follows that the BBC must therefore also observe strict financial separation, such that no licence fee money is spent on BBC Store. We are satisfied that, if the structural separation is observed, the necessary financial separation should follow.

#### Complies with the four commercial criteria

- 3.2.7. We then considered compliance with the four commercial criteria (as part of our assessment we sought external legal and economic advice). For BBC Store we considered, *among other things*, the following factors:

#### ***Fits with the BBC's public purposes***

- 3.2.8. The extent to which BBC Store will ultimately generate value rests on its ability to advance the public purposes. The liberation of the archive responds to audience expectations for a greater range of content on more flexible terms. Currently only c.7% of television programmes is available beyond the public service catch-up window, and this creates confusion when a user cannot find a programme on iPlayer.<sup>5</sup> BBC Store therefore supplements the public service offer by making available a broader range of programmes – including future commissions and a selected range of archive – to own and watch.
- 3.2.9. It is likely that at least some of the archive content will be of social, political and historical importance. Its wider availability will therefore help to sustain the first two purposes, related to citizenship and civil society and the promotion of education and learning. There is value also in being able to guide audiences to archive content and potentially, other BBC programmes, something that the integration with iPlayer will potentially allow. The integration of BBC Store will also enable the BBC to improve its editorial curation. A more personalised, relevant offer, with a broader range of content may over time lead to better engagement, with a corresponding increase in user satisfaction.

#### ***Exhibits commercial efficiency***

- 3.2.10. BBC Store is an attempt by BBCW to secure new routes to market and mitigate commercial risks associated with the structural decline of physical media (i.e., DVDs). It is, as such, a long-term play and this was reflected in the business case and factored into our analysis. We took into account the degree of risk and acknowledged in particular, that projects of this nature often necessitate longer periods of lower returns.<sup>6</sup> In assessing whether the proposal was commercially efficient, we considered a number of financial ratios, including net present value; internal rate of return; payback period and profit before interest and tax.<sup>7</sup>

<sup>5</sup> BBC application to the Trust for a new commercial service, BBC Store, July 2013.

<sup>6</sup> In assessing commercial efficiency, we also proceeded on the conservative basis that there would be an extended 30 day window. The Executive clarified with us that its financial projections for Store take into account a proposed extension of the window to 30 days.

<sup>7</sup> As per the requirements set out in protocol C4, Commercial Services, BBC Trust, May 2010.



***Does not jeopardise the reputation of the BBC***

3.2.11. While BBC Store has the potential to enhance the reputation of the BBC by making available archive content and enhancing the on-demand offer, the way it is integrated with iPlayer requires careful development, in order (in particular) to ensure:

- adequate delineation of paid-for and free content and a clear explanation of the rationale for charging;
- delivery of the archive promise, which we believe to be central to the ambitions for BBC Store: it must not be diluted over time by commercial drivers, and the curation of content provides a point of differentiation in a market where purchases are driven by a narrow selection of the biggest titles and a mix of older and new programmes;
- editorial integrity, compliance the BBC's Editorial Guidelines, prominence for public service catch up content, and objectively generated recommendations;
- that core iPlayer values are upheld; and
- that the trust of licence fee payers is not lost.

3.2.12. We are satisfied that the proposals duly respect these principles and requirements. In particular—

- to delineate paid-for and free content, the Executive has taken care to ensure a clear demarcation between the public service site and the new commercial destination and (in the digital locker) between purchased programmes and catch-up content;
- as to archive content, BBC Store must explain why certain content cannot be released or is no longer available, to avoid audience confusion and damage to the brand; and our approval is conditional on the Executive meeting a commitment set out in the application to release 500-1000 hours of archive programmes each year (across a range of genres).
- as regards editorial integrity, we are satisfied that the Executive is proposing adequate measures to mitigate the editorial risks in the areas of recommendations and content availability:
  - recommendations will be objectively generated and properly presented, with primacy given to programmes that are still in the catch-up window,<sup>8</sup> with blended archive and catch-up content appearing in recommendations only where editorially relevant;
  - in order to meet the editorial guidelines on fairness, privacy and duty of care to contributors as well as harm and offence, some categories of content will be excluded while others will be individually assessed, considered for sale for a limited period only or removed from future sale;
  - there will be a robust system to implement appropriate exceptions, restrictions and removals and to ensure serious complaints receive prompt attention;
- we are satisfied that the Executive is committed to ensuring that changes to the service respect the strong values that audiences attach to iPlayer, including by:
  - delivering a simple, familiar and consistent user journey, which provides adequate separation between the two sites
  - explaining the nature of any commercial partnerships
  - upholding brand values
  - addressing audience concerns about complex technical issues, such as storage, compatibility and security

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<sup>8</sup> Editorial control of commercial links will be managed within the BBC public service.

- we believe that clear communication with audiences regarding the scope and scale of the offer and the rationale for charging will mitigate the risk that the integration of BBC Store with iPlayer is seen as an unwarranted commercial incursion that could otherwise damage the BBC's relationship with licence fee payers (which is based on the general view among the public that the licence fee protects the BBC from commercial pressures).

***Complies with principles in the fair trading policy and avoids distorting the market***

- 3.2.13. Central to our assessment was the need to ensure that the proposal complied with the principles set out in the fair trading policy and did not distort the market. We considered these areas in particular depth and secured independent economic and legal advice to inform our decision. We concluded that the non-exclusive nature of BBC Store removed, in principle, any concerns about its distortionary effects on others because:<sup>9</sup>
- a. The rights for digitised BBC archive content will be made available on a non-exclusive basis to third party commercial providers
  - b. Any public service assets used by BBC Store, including iPlayer play-out technology, will also be available to other market players in line with BBC fair trading guidelines and at an established transfer price
  - c. The links from iPlayer to BBC Store and other commercial outlets retailing BBC content will not provide undue prominence to BBC Store.
- 3.2.14. In parallel, we considered the transfer pricing regime. Although BBC Store will be a commercial service, it will rely on some products and services used by the BBC to perform its public service functions – notably iPlayer. As a result, we needed to be satisfied that all public service assets and resources used by BBC Store were correctly identified, allocated and fully reimbursed (in the transfer price).
- 3.2.15. We therefore sought independent professional advice from RBB<sup>10</sup> on the proposed transfer pricing policy. In particular, we asked RBB to address the following matters:
- Whether the underpinning methodology adopted by the Executive for determining the transfer price is reasonable; and
  - Whether the transfer price properly identifies and correctly values all relevant cost items (although we note that our remit is not to provide a cost audit, but rather an opinion on the methodology used to identify and determine cost items included in the transfer price).
- 3.2.16. In summary, RBB recommended that the transfer price must take into account not only those costs that are incremental to BBC Store (i.e. the costs that the BBC would not occur save for the services that it is providing to BBC Store) but also an allocation of the common costs incurred by the BBC public service for the services which are to be utilised by BBC Store.
- 3.2.17. Specifically, RBB advised that a contribution – based on a cost-plus methodology – for the use of iPlayer play-out functionality should be factored into the transfer price in order to account for the benefits accruing to BBC Store from integration with iPlayer. Moreover, it recommended that the royalty fee that was to be paid in compensation for the use of the BBC brand should be treated as a standard cost item. Both recommendations were endorsed in the final version of the Executive's proposed transfer pricing policy that was approved by the Trust.

<sup>9</sup> The same point was made by Ofcom in its advice on the potential impact on others, summarised in section 4. We addressed, and subsequently dismissed, any market distortion concerns before approaching Ofcom for advice on the question of impact.

<sup>10</sup> We will publish this advice.

### 3.3. Current and future proposals for changes to iPlayer

- 3.3.1. In November 2013, the Trust received proposals from the Executive to extend the catch-up window from seven to 30 days and to remove series stacking functionality. While the proposals were submitted separately and are being considered separately (because unlike the commercial BBC Store proposals, these are for the development of the BBC's public services) with advice taken from Ofcom, there is a degree of overlap relating to the catch-up window. We factored this into our analysis of BBC Store (see further section 4.5.25 to 4.5.30). So far as concerns the length of the free catch-up window, we recognised that this could affect the propensity of users to buy content.
- 3.3.2. We therefore conducted our assessment of the commercial case for BBC Store on a conservative basis, by assuming that the free catch-up period would be extended to 30 days, but without pre-judging the question whether that change should be approved or not (which is currently under assessment by the Trust).
- 3.3.3. We also considered the Executive's publicly stated longer term vision for the development of iPlayer with the aim of transforming it from being 'catch-up TV' – to 'online TV'. We have already indicated that such proposals would be subject to any necessary regulatory scrutiny by the Trust. Since no proposals have yet been submitted to us we are unable to specify at this point what those processes will be. We are, however, mindful of the principle that that when these proposals do come forward we will need to take into account the cumulative effect of changes to iPlayer in our processes at that time.

## 4. Test of significance

### 4.1. Regulatory process

4.1.1. As part of our assessment we considered whether the proposed changes to BBC Online and iPlayer that arose as a result of BBC Store were 'significant'. While BBC Store is a commercial service, it involves changes to BBC Online, specifically, iPlayer, and for this reason we had to consider whether these were significant, thereby triggering a Public Value Test. In doing so, we took account of:

- a. The likely impact on audiences and others in the market;
- b. Novelty;
- c. Duration; and
- d. Financial implications.

### 4.2. The proposed changes

4.2.1. BBC Store requires a level of integration with, and changes to, BBC Online (notably, iPlayer) these comprise:

- An extended search functionality that includes both public service and commercially available BBC content;
- The inclusion of links to BBC Store and other commercial outlets retailing BBC content;
- A seamless purchasing experience via pop-up windows and a single BBC account registration; and
- The ability to view programmes purchased from BBC Store via iPlayer<sup>11</sup> and playback this content using iPlayer.

### 4.3. Are the changes significant?

4.3.1. We considered whether the proposals represented a significant change to the UK Public Services, which could not be approved without the application of a PVT. Clause 25 does not apply to commercial services and so the frame of reference was particularly narrow; we assessed only the potential significance of the changes to BBC Online and iPlayer, which arose as a result of BBC Store, including the impact of an extended 30 day catch up window for iPlayer. Having reviewed the proposals, we concluded that the changes did not represent a significant change to the UK Public Services.

4.3.2. In reaching this conclusion, we noted that the proposals entail a change to the 'key characteristics' of BBC online as set out in its service licence<sup>12</sup> and we therefore applied the presumption (see clause 25(3)) that such a change requires a PVT. We decided that the presumption was rebutted in this case, as the changes to the key characteristics, and to iPlayer as a whole, were relatively slight, and our conclusion as to the significance of those changes (in particular, as to their impact on others) was clear that these changes were not significant. We set out our reasoning below.

<sup>11</sup> Made possible by integration with a cloud-based digital locker belonging to BBC Store.

<sup>12</sup> See BBC Online and Red Button Service Licence, issued September 2013 and available at [http://downloads.bbc.co.uk/bbctrust/assets/files/pdf/regulatory\\_framework/service\\_licences/online/2013/online\\_red\\_button.pdf](http://downloads.bbc.co.uk/bbctrust/assets/files/pdf/regulatory_framework/service_licences/online/2013/online_red_button.pdf).

## 4.4. Impact on audiences

- 4.4.1. iPlayer already has considerable pull; in January 2014 it received over 315 million television and radio requests.<sup>13</sup> Half of all adults use BBC Online each week and it is the only UK-owned website in the top 10 most-used websites in the UK. The proposed changes are likely to result in a more personalised, relevant offer which may in turn improve satisfaction levels among users over time. The usefulness of recommendations in particular is closely linked to the total volume of content available and the integration of BBC Store will allow the BBC to develop algorithmic and social curation and improve its editorial curation and its ability to direct audiences to content they may value but would not otherwise find.
- 4.4.2. But while the changes may improve overall satisfaction, it is inherently difficult to forecast a corresponding uplift in reach. While 66% of participants in a 2012 BBC study<sup>14</sup> said they were either much more likely or slightly more likely to use iPlayer as a result of BBC Store, this rests on the assumption that they would largely use BBC Store to purchase BBC content. But the same set of findings show that only 27% was either slightly less likely or much less likely to use other places (such as iTunes) to buy Download To Own (DTO) programmes as a result of BBC Store, making any uplift in usage less certain. While the impact on audiences is likely to be positive and worthwhile, therefore, it is unlikely, in our view, to constitute a significant change to the Public Services.

## 4.5. Impact on others in the market

- 4.5.1. The Executive submitted to us its assessment of potential significance, having particular regard to the impact on others (providers or potential providers of alternative products and services). Its assessment was that the proposal did not represent a significant change. However, we decided that we should undertake our own separate assessment in this case and in line with our commitment,<sup>15</sup> we asked Ofcom to assess the potential impact on others. Ofcom wrote to the Trust in December 2013 with its advice, which we have published alongside this document.
- 4.5.2. Ofcom's assessment considered only the proposition as it would be at launch – essentially with content accessed and played in a PC, mobile or tablet environment. It advised the Trust to consider the impact of further elements, including post-launch evolutions to enable viewing on television screens, and the inclusion of radio content. Ofcom also advised the Trust to consider the cumulative impact of other planned changes to iPlayer including an extension of the catch-up window<sup>16</sup> and improved customisation.
- 4.5.3. Overall, Ofcom advised that the non-exclusive nature of BBC Store alleviated, in principle, any initial high-level concerns about the distortionary effects on others, because:
- The rights for digitised BBC archive content will be made available on a non-exclusive basis to third party commercial providers
  - Any public service assets used by BBC Store, including iPlayer play-out technology, will also be available to other market players in line with BBC fair trading guidelines and at an appropriate transfer price
- 4.5.4. In other areas, however, Ofcom identified concerns. In particular, it queried whether the Executive had chosen the most appropriate counterfactual and whether sufficient analysis of alternatives was conducted. It made the following points about impact on others:

<sup>13</sup> BBC research, 2014.

<sup>14</sup> Optimisa Research conducted on behalf of the BBC Executive into BBC Store (August 2012).

<sup>15</sup> In 2011 the Trust expanded its relationship with Ofcom to take full advantage of its understanding of the wider communications sector and, in particular, to invite Ofcom to provide its view of the 'impact on others' of proposed new services or changes, to inform the Trust in its decision on significance.

<sup>16</sup> Which we factored into our analysis.

- a. The Proposals could potentially hasten the decline of the DVD market for television content and this impact could extend beyond BBC specific content
- b. While the Executive identified transactional Video On Demand (VOD) and Public Service Broadcaster (PSB) catch-up services as being potentially impacted, Ofcom thought there could be wider impacts on other VOD models (especially subscription VOD) and linear channels (especially those carrying a large proportion of BBC archive content);
- c. Time spent watching DTO content could substitute other viewing,<sup>17</sup> although some of that may be other viewing of BBC content, reducing the net impact on others;
- d. The most notable impacts are likely to arise from increases in use of iPlayer, and the Executive may have underestimated the potential growth in use resulting from BBC Store:
  - (i) The 'seamless user journey' will encourage users to remain in, and purchase from, BBC Store rather than looking elsewhere for content. While accepting the Executive's argument that any such impact would be primarily limited to BBC content, and recognising that changes in behaviour were inherently difficult to predict, Ofcom considered that the impact of increased iPlayer use could spread to other types of content on other services if consumers spent more time in iPlayer; and given its position in the market and its forecast growth, such impact could be 'substantial'; and
  - (ii) Improvements to iPlayer could contribute to increased use including through increases in the number of people using it as a starting-place for discovering content, and increases due to improved functionality (e.g. fewer 'dead' searches, due to the availability of DTO content outside the present 7-day catch-up window).
- e. With regard to the potential effects of increased iPlayer usage, Ofcom suggested that:
  - (i) It could have a detrimental impact on other PSB catch-up services and on subscription VOD services;
  - (ii) As regards transactional VOD services, the impact could be positive (stimulating the market, and competition) or negative (stifling new players, as iPlayer offers a better experience);
  - (iii) The impact on linear channels was not likely to be material.
- f. Ofcom also considered possible impact on the (already-declining) DVD market, and the emerging market in 'storage lockers', and recognised possible benefits to independent producers.

4.5.5. In its overall conclusions, recognising the limitations of its analysis and inherent uncertainties, Ofcom repeated its view that there is 'potential for the impact [on others] to be substantial', but noted also the possibility of positive impacts.

4.5.6. In accordance with Ofcom's advice, we undertook further more detailed analysis. With the benefit of this additional work, we reached a better understanding of the potential impacts. Our findings are set out below.

#### Further analysis undertaken by the Trust following Ofcom's advice

4.5.7. Ofcom's principal concern was that the Executive may have underestimated the increase in iPlayer usage resulting from improvements to the service brought about by BBC Store, and so may therefore have underestimated the impact of BBC Store on other services.

4.5.8. It was not able to fully consider the potential impact of proposals on television screen formats (such as smart televisions) where it suggested there may be a wider range of considerations, for example:

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<sup>17</sup> Assuming there is unlikely to be any increase in total time spent by consumers viewing audio-visual content.



- The scale of the difference between the user experience of a fully-linked BBC Store from iPlayer versus the alternatives may differ depending on the platform used; and
- The range of commercial alternatives available to consumers may also differ by platform, which in turn could result in different degrees of impact.

4.5.9. Similarly, Ofcom noted that radio or audio products may also generate impacts which had not been considered.

4.5.10. While we therefore looked at the potential increase in iPlayer usage, and likely impact on other VOD providers, we *also* considered the impact of a BBC Store on television platforms. We *did not* consider further the potential impacts of offering radio or audio content. If the Executive wishes to extend the product offer to cover radio, it will need to return to the Trust for a separate decision.

4.5.11. With regard to the potential impact of BBC Store on television platforms, we concluded:

- There are currently technical obstacles to the inclusion of a fully-fledged BBC Store on these platforms, as regards sign-in, authentication, deep-linking and micro-payments.
- There are also commercial obstacles, as roll-out would be subject to a commercial agreement between the BBC and the platform. In this respect, availability of BBC content is secured by the terms of the [on-demand syndication policy](#), under which refusal by a platform owner to allow commercial links from iPlayer cannot be used as a pretext by the BBC to withdraw from a syndication deal. Therefore, the widespread availability of iPlayer does not necessarily entail a correspondingly large commercial footprint for BBC Store.
- As regards the concern that the availability of commercial alternatives on television platforms may be limited when compared with range of choice typically available over open online platforms, the absence from a specific platform may be the result of an exclusivity agreement between the VOD provider and a rival platform<sup>18</sup> – a content deal would typically entail a complex bilateral negotiation between the content provider and the platform owner.<sup>19</sup>
- In any event, the competitive impact of the presence or absence of BBC Store – whether integrated or a counterfactual free-standing version – on a particular platform is arguably immaterial to the main challenge for a new entrant which would be to match the range of content already on offer from existing VOD commercial stores, including BBC content.

#### Potential increase in iPlayer usage

4.5.12. Ofcom believes that the Executive may have underestimated the potential growth in usage of iPlayer as a result of the improvements to the service brought about by BBC Store.

- In its letter, Ofcom suggests that evidence of existing usage of commercial links on BBC Online is not a good indication of likely future consumer behaviour after BBC Store is implemented. However, previous initiatives to link from iPlayer to external suppliers of television content (on editorial grounds) have similarly not had a noticeably large impact on overall iPlayer usage (e.g. the introduction in February 2011, of external links to commercial PSBs' catch-up players in response to active searches for their content by iPlayer users). We regard this other precedent as a more appropriate indicator of the potential scale of change in iPlayer usage that might obtain; in particular:
  - With regard to a 'seamless experience', existing links to external websites (i.e., PSB players) take users directly into the programme page to play the desired television programme, without the need to execute any transaction;

<sup>18</sup> For example, in June 2012 Samsung – by far the larger smart television manufacturer in the UK obtained the exclusivity of ITV Player for its smart TV product line. Indeed, Samsung and ITV had already agreed ITV Player's exclusivity for Samsung's Android smartphones and tablets in 2013: see [www.itv.com/presscentre/press-releases/itv-enters-exclusive-partnership-samsung-itv-player-app-android](http://www.itv.com/presscentre/press-releases/itv-enters-exclusive-partnership-samsung-itv-player-app-android).

<sup>19</sup> The negotiations could cover issues such as potential sharing of revenues coming from advertising, subscription and/or transactional VOD; on-boarding costs and fees; and collection, ownership and exploitation of usage data, just to name a few obvious examples.

- (ii) As an improved content discovery portal, it can be argued that iPlayer is already evolving in this way and that the expansion in discoverable content already includes not only the 30-days free (catch-up) offers from the three commercial PSBs, but also the rental offer of primarily type-A (the most in demand) content recently launched by ITV in October 2012, and that this adds a new dimension in terms of variety that would not be matched by the corresponding catalogue expansion under the proposals
- (iii) 'Dead' searches are more to do with the BBC's current short (seven-day) free catch-up window as compared with commercial PSBs' 30-day availability;
- (iv) According to the Executive, the percentage of visits on iPlayer homepage which lead to linking to an external URL is consistently very low with an overall average of only 0.21% since August 2011; and with respect only to the use of the search function, the percentage is again consistently very low with an overall average of 1.95% since August 2011;
- (v) Even so, the use of external links to the ITV Player might overestimate the use of commercial links under the proposals, because external links to the ITV Player are for both free (catch-up) and pay (rented) content; do not indicate whether the programme searched is free or for rental (i.e. a user might link to the ITV Player and discover that the desired programme is not available as free catch-up); and content available to rent from the ITV Player is largely type-A content but under the proposal, type-A content would, over time represent less than 10% of the overall catalogue available for sale.

b. In any case, it is fair to say that the current use of external links on iPlayer is so low that it lends some weight to the Executive's central forecast (provided in its application) that the percentage of active iPlayer users purchasing from BBC Store would be [- REDACTED -] in 2018.

4.5.13. In suggesting that users will be more likely to stay within iPlayer as a result of BBC Store, Ofcom refers to findings from consumer research commissioned by the Executive that shows that 66% of participants were either much more likely or slightly more likely to use iPlayer.<sup>20</sup> However, for this to translate into users spending more time within iPlayer they would need to be using BBC Store to purchase BBC content and the consumer research finding suggest that this may not be the case. The findings show that only 27% of respondents was either slightly less likely (15%) or much less likely (12%) to 'use other places to buy television programmes as downloads e.g. iTunes'; and Ofcom cautioned that 'that this type of stated preference could potentially lead to some optimism bias.' This is particularly the case given that, according to the same research findings, 72% of participants expected a single episode of a BBC television programme to cost between 50p and £1. [- REDACTED -]

4.5.14. Ofcom regards iPlayer's market position as material to its conclusion that there is a potential for BBC Store's impact to be 'substantial'. There is no doubt that iPlayer is prominent among catch-up players and, more generally, VOD content aggregators.<sup>21</sup> The Executive's submission also noted that the ratio of iPlayer unique reach to that of 4OD is 2.7 (and has been broadly the same over the previous three years), which is broadly in line with the corresponding ratio of portfolio shares of viewing in multi-channel homes. Estimates produced by Mediatique indicate that there are 872m viewed hours on iPlayer, which are forecast to grow to 3.5bn in 2018. Mediatique further estimates that iPlayer share of catch-up viewed hours in 2012 was c.40%, followed by 4OD with 14%, ITV Player with 9% and Demand5 with 2%.<sup>22</sup>

4.5.15. On the other hand, Mediatique expects that market share will converge to a closer read-across to linear share. It observed how the BBC's share of consumption reflects, in part, also ITV's

<sup>20</sup> Optimisa Research conducted on behalf of the BBC Executive into BBC Store (August 2012).

<sup>21</sup> In arguing that there is potential for the impact on others to be substantial Ofcom reported that 'according to ComScore MMX data, the unique audience of iPlayer on desktop and laptop computers was 7.6m in April 2013, compared to 2.8m for 4oD.' These data originally reported in the Executive's C25 assessment were quoted from Ofcom's Communications Market Review (2013).

<sup>22</sup> The study by Mediatique was commissioned by the BBC Executive as part of the 30-days proposals.



restrained market share, which reflects a bias towards live and event programming that does not lend itself to catch-up viewing. Another explanation could be that, besides the traditional PC and laptop platforms, other PSBs have developed, incrementally, new versions of their catch-up players in line with their commercial objectives,<sup>23</sup> whereas the BBC pursues its public-value goal to reach out to as many platforms as possible.

4.5.16. For the prominence of iPlayer to translate into substantial market impact one has to believe that iPlayer users would predominantly prefer to purchase from BBC Store rather than from any other VOD provider (so that they will stay within iPlayer environment). The main reason for any such preference would be 'the potential for a more seamless user experience when purchasing content BBC Store compared to other commercial offerings.' (BBC Store would not benefit from undue prominence, because the brand names of prominent competitors would be clearly stated in the second link next to BBC Store whenever a programme is available elsewhere).

4.5.17. But we believe there are reasons to question the extent of any such 'preference':

- a. Under the proposals, there will be 'deep-linking' (consumers would be able to link straight into the programme page ready to execute the transaction without the need to sign-in first) so the user journey for executing a purchase from other commercial providers will require only one more click-through compared to the user journey proposed for the BBC Store;
- b. While Ofcom believes 'a low-friction purchasing experience' may keep people within the BBC environment, it also acknowledged the possibility that 'consumer stickiness' may lead people to stay with their current services (such as iTunes). Further, this 'stickiness' may be attributable to more than simple inertia:

- (i) It might equally be the result of loyalty to a brand or technology which remains the preferred choice;
- (ii) Consumers may stick with their incumbent VOD provider because of the breadth of the catalogue;
- (iii) Key media content aggregators (e.g. Google Play, Apple's iTunes and Lovefilm, Amazon's Kindle platform) not only offer a much wider range of VOD (i.e. they are not restricted to BBC materials), but also offer other media categories such as books, music, online games, not to mention a corresponding apps store, all under the same customer account.

- c. It seems likely that the main obstacle for any new emerging players, particularly those of a smaller scale, is to match the user experience and the breadth of content offered by these incumbents, rather than the BBC Store. Indeed, BBC Store might lower entry barriers by making it easier for smaller emerging players to gain brand awareness through the provision (at no cost to them) of commercial links on iPlayer (where they offer BBC content) next to those of established incumbents.

4.5.18. We consider it unlikely that storage lockers offered by BBC Store will have a major impact on iPlayer usage. It is hard to see how the development of a virtual storage locker<sup>24</sup> could realistically have any chance of setting a de-facto industry standard. Indeed, it seems more likely that the BBC Store would follow whatever industry standard emerges in order to overcome the disadvantage of its limited content offering, by making its virtual locker compatible and interoperable with others.

#### Potential impact on other VOD services

4.5.19. Ofcom identified subscription VOD (SVoD) services as being among those potentially impacted by the changes to iPlayer, because:

<sup>23</sup> For example, as referenced above, ITV has opted to be absent from Apple's smartphone and tablet platforms in order to benefit from an exclusivity agreement with Samsung.

<sup>24</sup> For example, a cloud-based service.

- a. Television viewing time is finite so some consumers could move away from their SVoD services, even if only for a matter of months, if they spend more time using iPlayer; and
  - b. Given the prominence of television 'box-set' series being promoted on SVoD services, overlap in content types may be greater than the Executive argued
- 4.5.20. However, the appeal of SVoD services is their very broad range of content for a reasonably small monthly fee. The main promise is that by taking up an account consumers will be able to find something to watch every time they turn on their television.
- 4.5.21. While Ofcom was principally concerned about the impact on others of the changes to iPlayer overall, we make some further following observations regarding the impact of BBC Store itself. SVoD is a very different proposition from the one underpinning BBC Store, where the central assumption is that consumers would, on average, purchase the equivalent of [ - **REDACTED** - ] television series per year.
- 4.5.22. Moreover, the fact that the UK content offer of these services (i.e., Lovefilm Instant and Netflix) already includes the most popular BBC programmes strongly suggests that there would be an asymmetric relationship in terms of demand-side substitutability between BBC Store and SVoD services. [ - **REDACTED** - ]
- 4.5.23. In terms of consumer behaviour, it seems highly unlikely that SVoD customers would consider temporarily discontinuing their accounts in order to purchase BBC content at a higher price-per-hour-watched, when the large majority of type-A content is already available in the SVoD catalogue. In contrast, it is likely that a consumer who buys television series from Store may decide to switch to a SVoD in order to access a wider range of television programme and movies.
- 4.5.24. We conclude, accordingly, that the consideration that SVoD services could provide a competitive constraint on BBC Store, but not vice versa, strongly indicates that it is unlikely that the former would be impacted by the launch of the latter.

#### Potential cumulative effects of an extended catch-up window

- 4.5.25. As part of our further work (and in response to one of the issues raised by Ofcom) we also considered the potential cumulative effects of an extended catch-up window. In November 2013, the Trust received proposals from the Executive to extend the catch-up window from seven to 30 days. While the proposal is technically separate from BBC Store (and is still under consideration by the Trust) there is a degree of overlap relating to the catch-up window, and we factored this into our analysis. In particular, we wanted to know whether the proposals for BBC Store were based on the current seven-day window, or the proposed 30-day one.
- 4.5.26. The Executive clarified that the financial projections for BBC Store take into account an extension of the window to 30 days. Moreover, its submission refers to an economic study from Mediatique, originally commissioned as part of the 30-days proposals (and provided to Ofcom) which also takes into account the launch of BBC Store.
- 4.5.27. In detail, the Mediatique report shows that the extension of the catch-up window would cause a reduction in consumption of all Pay-VOD, including BBC Store, in proportion to their overall share of pay-VOD consumption under the counterfactual *without* the 30-days extension.<sup>25</sup> The overall negative impact on third party pay-VOD operators is estimated to be less than 4% of overall viewed hours in 2018. It is reasonable to conclude, therefore, that BBC Store would fare marginally better under the current seven-day window, but also that the gains or losses in either scenario are limited.

<sup>25</sup> It is fair to say that this assumption is conservative, given that the chances are that the extension of the 30-days window is more likely to cannibalise the BBC Store, that is, more than proportionally than its future share of the overall Pay-VOD market, which is defined as all discrete paid-for content, thus including both DTO and DTR, and covering content aggregators such as iTunes, but also vertically integrated commercial outlet such as Sky Store and ITV player.

- 4.5.28. With respect to the current proposals for BBC Store, the extension of the catch-up window might have two offsetting impacts on BBC Store, and, by reflection, on other operators. On the one hand, the extension might cannibalise DTO sales of BBC content, on which BBC Store is exclusively reliant. On the other, the increase in content availability might strengthen the retention of users within iPlayer.
- 4.5.29. In this respect, it is worth pointing out that the 30-days catch-up extension would benefit primarily infrequent iPlayer users, whereas for those users who visit iPlayer on a weekly basis it would not result in an increase in content availability in practice. This is particularly so given that users can currently download a BBC catch-up programme and have up to 30 days to begin watching it, thereby extending the availability window to more than six weeks (i.e., 7+30+7 rule – that is, seven days to download the programme, plus 30 days to watch it, and a further seven days from the date of watching to re-watch it).<sup>26</sup>
- 4.5.30. Based on data provided by the Executive, we know that around 50% of users visit iPlayer on a weekly basis, whereas around 30% visit iPlayer less frequently than on a monthly basis. This would tend to limit the expected impact of the 30-days proposal. Moreover, under the plausible assumption that frequent users exhibit a relatively stronger preference for BBC programmes than infrequent ones, thus would be more likely to consider buying BBC content on a DTO basis, the cumulative effect of the two sets of proposals may be further mitigated.

#### Ofcom comments concerning the Executive's counterfactual

- 4.5.31. Ofcom questioned whether the counterfactual (a stand-alone commercial service without any links from iPlayer or associated storage, purchase or playback functionality) was viable given that 'the commercial case for the BBC Store... includes an assumption that over two thirds of its visitors and transactions will be click-throughs from iPlayer.'
- 4.5.32. After further consideration, we are satisfied that a standalone BBC Store would still capture some customers and transactions that are assumed to be click-throughs from iPlayer under the proposals, because:
- a. Plausibly, the take-up of the BBC Store would not merely cannibalise DVD sales, but also offset revenue that would otherwise be lost, since consumers would typically differ in their preferences for DVDs: that is, early adopters would stop purchasing DVDs regardless of whether the BBC Store is launched;
  - b. DVD sales are in decline, and we believe it likely that BBCW would want to hedge, as other content owners are already doing, against an unmitigated decline in DVD sales in the counterfactual scenario by developing strategies to secure digital routes to market (such as setting up a standalone BBC Store), so any decision *not* to launch a standalone BBC Store under the counterfactual scenario would carry risk;
  - c. Where the buyer actively seeks out desired content (for example by searching online), as is typically the case for the purchase of a DVD, it is plausible to argue that a BBC-branded store would probably be the destination of choice even in the counterfactual.

#### Conclusions on impact on others

- 4.5.33. Ofcom's advice concluded that 'the impact of extending the linking and purchase elements of the Proposals to other platforms, notably smart television services and closed television platforms, may result in different competitive impacts which have not been assessed.' Having now reviewed these issues further, we conclude that the proposals are uninfluential in this respect, given that the launch of BBC Store would be unlikely to have any impact on the barriers to entry and expansion in these emerging platforms.

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<sup>26</sup> Therefore, under the 30-days proposal the maximum length of content availability for frequent iPlayer users would actually shorten by approximately two weeks.

- 4.5.34. Regarding the definition of the appropriate counterfactual, we believe that a standalone BBC Store would constitute a viable commercial proposition, in particular, both as a hedge against the prospect of an unmitigated decline in the UK DVD market and as a basis for developing a digital VOD offer for BBC content in markets beyond the UK.
- 4.5.35. We agree with Ofcom that:
- a. 'The proposals may result in positive impacts (for example, growing the DTO market and increasing revenues to the independent sector)', and
  - b. 'Any impact is likely to be spread across a range of markets and players.'
- 4.5.36. However, we believe it unlikely that the proposals will lead to changes in user behaviour towards iPlayer compared with the counterfactual. In particular, we are doubtful as to whether the seamless user experience due to the integration between iPlayer and BBC Store could realistically put BBC Store at a competitive advantage vis-à-vis other VOD content aggregators, whose content offer is far wider than that envisaged under the proposals, not only in terms of audio-visual content, but also across other categories of media content.
- 4.5.37. Therefore, we believe that it is unlikely that the (neutral) use of commercial links on iPlayer would cause iPlayer users to be captured within its environment for longer at the expense of other VOD providers, notably, PSB players.
- 4.5.38. Further, having factored into our analysis an extended 30-day window, we think the cumulative effect, for the reasons given above, is likely to be slight and does not affect our overall conclusion on impact on others.

We also believe that the combination of content non-exclusivity, neutral use of commercial links allocated on a fair, reasonable and non-discriminatory basis, availability of integration with iPlayer on the same terms and conditions afforded by BBC Store and the existing protection built in to the on-demand syndication policy, which would prevent any unfair advantage for BBCW, would remove any risk of anticompetitive foreclosure under these proposals.

## 4.6. Novelty

- 4.6.1. The relevant question here is not the novelty of a download-to-own proposition, but of its integration with iPlayer and the changes that brings about. Central to these is the inclusion of links to commercial providers. There is some precedent however, which reduces the novelty of proposals; in 2008, the Trust approved the introduction of links to commercially available BBC content from BBC Online.
- 4.6.2. The BBC continued to evolve the commercial user journey to include television programmes available on DVD, Blu-ray disc and digital formats from a range of suppliers. And, in 2011, it introduced external links from iPlayer to the commercial PSBs, in response to active searches for third party content by BBC users. The inclusion of links to external commercial sites, as envisaged by BBC Store, is therefore very much an extension of existing practice.
- 4.6.3. Further, the inclusion of these links is consistent with the current service licence for BBC Online and the specific conditions to, 'increase the volume of click-throughs to external sites from all parts of BBC Online year-on-year.'<sup>27</sup>
- 4.6.4. While integration with a digital locker (which would allow users to view and access programmes purchased from BBC Store via iPlayer) and the ability to playback BBC Store content on iPlayer are new activities for the BBC, they do not, in our view, carry a high degree of novelty. Nor is an extended search functionality that includes both public service and commercially available BBC

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<sup>27</sup> Page 5, BBC Online and Red Button Service Licence, issued September 2013.

content in itself novel. A search today on iPlayer will generate results for both the BBC and other providers. Changes envisaged by BBC Store are very much an evolution of that feature.

**Figure I:** a search for 'Sherlock' generates both public service and commercial results



## 4.7. Duration

4.7.1. BBC Store will be provided on a permanent basis; but when considered alongside the other criteria, we do not think that duration is a source of concern.

## 4.8. Financial implications

4.8.1. The cost of establishing and running BBC Store will not be funded by the BBC from the licence fee but as a commercial venture, borne by BBCW. Where resources or assets are provided by the public service, they will be fully compensated at market value under the transfer-pricing regime. We sought external advice on the methodology used by the Executive from RBB and are satisfied with the proposed transfer pricing arrangements. Further, we will revisit this area in two years' time as a condition of our approval (as set out above).