

S4C Response to Ofcom's Consultation on Spectrum Pricing for Terrestrial Broadcasting.

Introduction

S4C welcomes the opportunity to respond to this consultation, *Spectrum pricing for terrestrial broadcasting*, dated 13 March 2013. S4C is the only Welsh language television channel in the world and alongside the BBC, ITV, Channel 4 and Five, it is one of the five public service broadcasters in the UK with a duty to fulfil programme and service requirements, set out, in the case of S4C, in statute and where relevant, by agreement with Ofcom. The S4C Authority¹ has a duty to ensure that the S4C service provides a broad range of high-quality and diverse programming, providing information, education and entertainment², available wholly or mainly by members of the public in Wales.

We recognise that spectrum below 1 Ghz, including the 600Mhz and 700Mhz bands, currently used by digital terrestrial television (DTT) in the UK, has a significant economic value and represents a scarce resource. We also recognise that Ofcom has a duty to ensure this spectrum is utilised as efficiently as possible. However, this requirement for resource efficiency has to be balanced, in our view, by the requirements of public service broadcasting and the wider citizen interest. While Ofcom has a duty to ensure optimal use of spectrum, with the introduction of administered incentive pricing (AIP) it risks a conflict with its statutory obligation to review ways to maintain and strengthen the quality of public service broadcasting. From S4C's perspective, any additional charges, passed on to us from our multiplex operator, are likely to impact significantly on our investment in programmes and content. We therefore welcome Ofcom's decision to postpone the imposition of AIP on digital terrestrial television spectrum held by multiplex operators and broadcasters until 2020. However, as we explain later in this response, we do not believe there will have been any material change to the conditions under which the PSBs operate, which would justify the introduction of AIP after that time.

We believe that in practice, publicly service broadcasters are bound by a range of constraints and regulatory obligations that make it very difficult to respond effectively to the spectrum efficiency mechanism represented by AIP. S4C currently broadcasts its service on PSB Multiplex 2, operated by D3&4, using spectrum that has been reserved by order³ of the Secretary of State. Along with the other PSBs, the 2008 Multiplex Order also granted spectrum for S4C to run a high definition service on Multiplex B known as Clirlun, (although this service has now been discontinued).

In common with other public funded bodies in the UK, S4C has faced significant cuts to its funding. Following the Comprehensive Spending Review in 2010, S4C's budget was cut by 24% over a period of 4 years (equivalent in real terms to a cut of 36%). Following the Chancellor's Autumn Statement last year, the DCMS announced a further round of funding reductions for S4C (1% in 2013/14 and 2% in 2014/15). We were recently informed that further cuts of 1.09% and 1.06% will be applied to our funding from DCMS for 2013/14 and 2014/15 following the 2013 Budget Statement.

For the duration of the current BBC Charter and since April this year, the majority of S4C's funding now comes from the Licence Fee, through the BBC Trust. However, the new Operating Agreement between the S4C Authority and the BBC Trust also provides for incremental cuts of 1% in the level of funding from this source in each of the 2015-16 and 2016-17 financial years.

¹ It is the statutory responsibility of the S4C Authority, whose members are appointed by the Secretary of State for DCMS, to provide the S4C service and be accountable for it.

² 2003 Communications Act, Section 204 (5)

³ The Television Multiplex Services (Reservation of Digital Capacity Order) 2008 <http://www.legislation.gov.uk/ukxi/2008/1420/contents/made>. "Digital capacity sufficient for the broadcasting (as a standard definition television service) of the service known as S4C Digital (or S4C Digidol), throughout Wales;"

In response, S4C has already made significant savings internally and in our view there is no material scope to reduce our overheads further without directly affecting our programme service. As part of our review of costs, we identified that the Clirlun service did not deliver value for money within the new funding conditions which applied after October 2010. As a result, and with great regret, it was terminated in December 2012, delivering an annual saving of £1.5m. At a time when other broadcasters are investing heavily in HD, S4C is currently only available as a standard definition service.

It should also be noted that transmission costs already represent a disproportionate share of S4C's overall budget compared to the other PSBs. Although they have broadly similar DTT carriage costs, in the case of S4C, these amount to approximately 0.75% of our total budget, a far higher proportion than for the other PSBs.

As a public service broadcaster serving the whole of Wales, S4C's service aims to fully reflect the life of the nation and its communities, across the full range of programme genres. We operate as a publisher broadcaster and 96% of our public fund expenditure⁴ is invested in commissioned programmes, programme-related costs and content support (including transmission, distribution, broadcast licences and access services), with only 4% spent on overheads. The bulk of our funding is therefore directly spent on programmes and any additional charges, such as AIP, would result in a reduction in our ability to deliver original and innovative content, which would be very evident on screen.

We have, to date, succeeded in protecting our on-screen content spend from the full impact of funding reductions incurred so far. However, this will not be possible with further cuts or with the imposition of additional charges, such as AIP.

Viewers in Wales are also viewers of other channels and expect S4C's programmes to be comparable in quality to those broadcast on other mainstream channels as well as to compete, in terms of range, with the hundreds of other digital channels available. In such a competitive environment, a reduction in the range and quality of S4C's service, for example through additional budget cuts or lower production values, would be likely to lead to reduced reach figures and lower appreciation scores, thus undermining S4C's ability to fulfil its remit as a PSB.

Background to our response

We believe that there are significant factors which prevent S4C, along with the other PSBs, from responding to a pricing incentive mechanism such as AIP. Although we welcome Ofcom's decision to postpone applying AIP to DTT capacity until 2020, in our view these factors will still be just as relevant at that time as in 2014, when Ofcom intends to introduce regulatory management charges. However we are concerned about the impact of any additional charges (passed on to us from our multiplex operator) which will reduce the amount we have available to spend on programmes. Should Ofcom decide to introduce this fee, we would request that it be kept as low as possible.

As a PSB, we will continue to be subject to universal coverage requirements in Wales and we will not be able to reduce the amount of spectrum used to fulfil this requirement without undermining this requirement. There will be a continuing need to secure international agreement following any proposed change to the frequencies used by S4C and if new transmission technologies were introduced, to secure greater spectral efficiency, there is a risk that viewers and consumers would be left behind. Indeed, as explained below (see page 4), in Wales it could be argued that DTT is largely a secondary transmission platform and faced with additional costs, many consumers might decide not to bother to acquire new equipment or upgrade.

From S4C's perspective, as a broadcaster which does not control any spectrum, imposing AIP would not result in greater spectrum efficiency. S4C has no control over the technology and

⁴ Annual Report and Accounts, 2011

techniques which affect the efficiency of spectrum use. S4C is a recipient of capacity, which is allocated in accordance with Ofcom's technical parameters and the multiplex operator's working practices. However, under standard carriage agreements, the multiplex operator is entitled to pass on AIP charges to the broadcasters in proportionate shares. This reflects the financial model of carriage agreements, where operators pass on their third party costs to the broadcasters. For S4C to share the economic burden of AIP would not therefore help to further Ofcom's desired aim of delivering better spectrum efficiency.

We note that Ofcom has already recognised these constraints and factors in the consultation document. Section 4.18 states that,

"In this context, we recognise that to some extent, broadcast multiplex operators have less room for manoeuvre than other users of spectrum for a number of interlinked reasons. First, they are subject to regulatory obligations imposed through licence conditions. These are designed by Ofcom to reflect our duties under the Communications Act to secure a wide range of television services throughout the whole of the UK and to promote, in particular, public service television (PSB). Second, there is a risk that an uncoordinated transition to more efficient transmission technologies would leave significant numbers of consumers with obsolete receiver equipment to the detriment both of those using the DTT platform and to the reach of public service content. Third, broadcasters' use of particular spectrum frequencies in the UK is dependent on internationally agreed co-ordination because of the need to avoid cross-border interference."

It is worth noting the broadcasters and multiplex operators collectively have already been achieving efficiency gains in relation to their use of spectrum for DTT transmission. The S4C service is carried on the D3&4 multiplex in Wales, which is due to undergo substantial engineering work this summer. This work, in conjunction with the multiplex provider, will result in efficiencies that will release enough spectrum for an additional service.

We note that Ofcom's analysis at this stage is high level, and does not take account of specific geographic and demographic factors within the nations and regions, which could impact on spectrum value, thereby reducing opportunity costs and options for alternative commercial use.

Coverage has historically been a particular issue in Wales in relation to television reception. When DTT services were first introduced in the mid 90s, their pre-switchover coverage in Wales was limited and this resulted in the rapid take-up of satellite by viewers in Wales. Although switch-over was completed in Wales in April 2010, as noted by Ofcom's Communications Market Report for Wales 2012⁵, 53% of homes in Wales have satellite installed for their main TV set, higher than in England and Scotland and above the UK average (41%). Any proposed changes in DTT transmission technology in Wales, in order to promote spectral efficiency, could have a disproportionate impact, with significant numbers of consumers deserting the platform altogether, rather than investing in new equipment which would be of secondary use only. This outcome would not appear to support the objective, likely to be endorsed by the World Radiocommunications Conference in 2015, for DTT to remain a central broadcasting platform throughout Europe.

The imposition of AIP is predicated on the existence of alternative use and excess demand. In parts of rural Wales, which are sparsely populated, a situation of market failure is a more likely outcome. For example, while across the UK the commercial multiplexes achieve a coverage of around 90%, in Wales the coverage is just 72%, because the operators took the commercial decision at switch-over, not to roll out their networks beyond nine sites, out of the total of 214 sites which transmit DTT in Wales, even though spectrum was available. This reflected the relative lack of value to the commercial multiplex operators in seeking to attain additional coverage for their services in Wales.

⁵ <http://stakeholders.ofcom.org.uk/market-data-research/market-data/communications-market-reports/cmr12/wales/>

Taking account of the significant efficiencies and cost savings already delivered by S4C, in response to cuts in funding, in our view the imposition of AIP charges would inevitably lead to a reduction in our programmes and content spend, undermining our role as a PSB. We therefore believe that Ofcom should take this risk into account when considering the imposition of AIP as a long-term mechanism to promote spectrum efficiency, in relation to broadcasting.

Responses to the consultation questions

Question 1: Do you agree that the principle of applying AIP remains relevant to spectrum used for broadcasting?

We do not accept that AIP will be an effective tool for promoting spectrum efficiency in relation to broadcasting. We do not believe that broadcasters, and the PSBs in particular, are in a position, due to regulatory and technical constraints, to effectively respond to price based mechanisms such as AIP, either now or in the long term. In the case of S4C, the inevitable consequence of levying AIP would be a reduction in programme and content spend, undermining our ability to fulfil our duties as a PSB.

Question 2: Do you agree with our revised proposals to delay the introduction of AIP based on opportunity cost for national DTT multiplex operators until we have materially progressed our proposals for the future use of the UHF spectrum?

We agree with the proposal not to introduce AIP for broadcasting until 2020 but as explained earlier in this response, we do not believe the regulatory context and technical constraints will have changed by that time, making it no more appropriate to introduce AIP than in 2014.

Question 3: Do you agree with our proposals to apply a fee for spectrum used for national DTT, in the meantime, based on the cost of administration instead?

We are concerned that any costs passed on to us would impact on the funding we have available to spend on programmes and content. Should Ofcom decide to introduce this fee, we would request that it be kept as low as possible.

Question 4: Do you agree that charges based on the costs of managing the spectrum should be applied to DAB radio and to local TV broadcasting?

This question is not applicable to S4C.

Question 5: Do you agree that when full AIP is applied for spectrum used for national DTT broadcasting (once we have materially progressed our proposals for future use of the UHF spectrum) it should be applied gradually, rising over five years.

We do not believe it is appropriate to comment on any timing arrangements for the introduction of AIP as we do not believe it is an appropriate mechanism to fulfil the aim of increased spectrum efficiency. We also take the view that this mechanism could conflict with Ofcom's duties in relation to public service broadcasting.