



Review of ITV Networking Arrangements 2006

Statement

Publication date:

13 March 2007

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Section 1

Summary

The requirements upon Ofcom

- 1.1 The ITV Networking Arrangements (the 'NWA') are a set of arrangements between ITV Network Ltd ('ITV Network') and the 15 regional Channel 3 licensees. These 15 licensees are currently under the control of ITV plc, SMG plc, Ulster Television plc ('UTV') and Channel Television Ltd ('Channel').
- 1.2 The NWA, which currently comprise five main documents, are intended to coordinate the provision of a national television service that is capable of competing effectively with other broadcasters in the UK.
- 1.3 Ofcom has a statutory duty to carry out from time to time a general review of the NWA, under section 293 of the Communications Act 2003 (the 'Act'). Essentially, such a review is intended to assess:
 - Whether regional Channel 3 services can be a nationwide system that can compete effectively with other UK television programme services; and
 - The impact of the NWA on competition
- 1.4 In addition, Ofcom is also required to consider the effect of the arrangements on the ability of the regional Channel 3 licensees to maintain the quality and range of regional programmes and other programmes contributing to the regional character of the services.
- 1.5 Ofcom must conduct such a review no more than a year after the previous review. Ofcom published its final recommendations on the 2005 NWA review in Autumn 2005. Following a consultation document issued on 28 November 2006¹, this statement concludes the 2006 review of the NWA.

Ofcom's conclusions

- 1.6 Ofcom's conclusions are as follows:
 - For the current review of the NWA, Ofcom considers that there will be a need to update the Network Centre Code of Practice to take into account changes to Ofcom's Guidance to broadcasters for drawing up Codes of Practice relating to the commissioning of independent producers. Following on from Ofcom's Television Production Sector Review ('TPSR')², Ofcom is consulting separately on revised Guidance to broadcasters³. Ofcom is not, therefore, making specific recommendations in this document as to how the Network Centre Code of Practice needs to change at this stage, simply stating that it will need to be amended in the light of that revised Ofcom guidance and the new media rights agreements. The Network Programme Licence ('NPL') and Tri-partite Agreement ('TA') will also need to be amended in the light of the changes made to the Network Centre Code of Practice;

¹ See http://www.ofcom.org.uk/consult/condocs/itv_network/

² See http://www.ofcom.org.uk/consult/condocs/tpsr/statement/review_tv.pdf

³ See <http://www.ofcom.org.uk/consult/condocs/cop/>

- Ofcom considers that no other changes are necessary to the NWA as part of the 2006 Review because there are no other significant changes to the operation of the NWA to take into account; and,
 - Going forward, Ofcom intends to streamline the process of future NWA reviews using a more informal consultation process where the proposed changes are not material. This will comply with the legal requirement for frequent reviews of the NWA whilst minimising the burden on stakeholders. Ofcom will continue to conduct formal consultations where it considers it appropriate to do so and, in particular, where changes are proposed to the NWA which are considered material. Ofcom also expects to consider in the 2007 NWA Review the scope to maintain the NWA obligations in a less specific way by removing at least the NPL and TA from the set of documents comprising the NWA.
- 1.7 Ofcom confirms that although it is recommending changes to the Network Centre Code of Practice, NPL and TA, the formal approval process required need not delay the commissioning of programmes based on the new agreement with Pact on new media rights. To delay such commissioning would neither be in the commercial interests of any party, nor in the interests of consumers who wish to receive the new services involved. Ofcom therefore considers that, at this stage, Ofcom would not object to ITV Network commissioning programmes on the basis of the revised NWA prior to formal approval being obtained. However, in the event that Ofcom is made aware of any issues arising from such a situation, Ofcom may decide to require commissioning to revert to taking place on the basis of the Network Centre Code of Practice, NPL and/or TA in place at the current time.

Section 2

Introduction

Background to the Networking Arrangements

- 2.1 Channel 3 is a free-to-air, commercially funded national television broadcast channel. Channel 3 is made up of 15 regional licensed areas, the licences for which are currently held by four companies: ITV plc (11 licences), SMG (two licences), UTV and Channel. Throughout this document, SMG, UTV and Channel are referred to collectively as the 'non-consolidated licensees'.
- 2.2 A key public policy objective for Channel 3 is to provide competition to other national broadcasters. The Channel 3 licensees were mandated under section 39 of the Broadcasting Act 1990 to conclude a set of arrangements that would enable them to work together to produce a national television service. This set of arrangements is known as the ITV Networking Arrangements. However, the Broadcasting Act 1990 did not dictate the structure or content of the arrangements.
- 2.3 ITV Network is a key organisation in the administration of the NWA. ITV Network is a company limited by guarantee, with a membership composed of the 15 licensees. The board of ITV Network is known as the Network Council and was set up to agree the ITV strategy and budget. A separate management structure known as the ITV Network Centre ('NWC') was created as a result of the initial NWA as the body to execute the instructions of the Network Council (to run the ITV network on behalf of all the licensees). The NWC exists within ITV Network.
- 2.4 The Networking Arrangements currently comprise five documents:
- Network Supply Contract ('NSC') - specifies each regional licensee's share of contribution to the Network Programme Budget ('NPB');
 - Network Programme Licence (NPL) – is the standard form of contract for use by the NWC when it commissions a programme from a regional licensee;
 - Tripartite Commissioning, Production and Compliance Agreement (TA) – is the contractual arrangement used by the NWC when it commissions a programme from an independent producer;
 - Network Centre Statement of Principles - deals with the control of network policy by the licensees, the implementation of that policy by the NWC, the selection of programmes, and the budget and the supply of a network schedule. It also provides for the NWC to be organised within the management structure of ITV Network Ltd; and
 - Network Centre Code of Practice - ensures that information about all the above procedures is disseminated fully to guarantee an even-handed treatment of in-house and external (independent) producers with respect to programme commissioning. The NWC Code of Practice also sets out the process by which licensees are appointed for programme compliance and production monitoring.

ITV Network activities and governance

2.5 There are three broad areas of activity in the ITV Network 'supply chain'. These were set out in some detail in the 2005 consultation and statement on the NWA⁴, but in brief they are:

- i) Programme commissioning and acquisition. Content for ITV1 comprises a combination of original commissions and acquisitions (of programmes already made). New commissions (or programme production) can be purchased from both the licensees' in-house production divisions and external sources. There is a safeguard in commissioning in that the Network Centre Code of Practice sets out the principles to be applied by it when agreeing terms for the commissioning of independent productions. The Network Programme Licence and the Tripartite Agreement are based on this Code;
- ii) Channel operation services. These arrangements - either between the licensees, and/or between the licensees and third parties - are the 'nuts and bolts' of producing a national schedule and broadcasting it. They cover areas such as marketing and outsourced services (e.g., support services), interactive and on-line services, and transmission. A key recommendation of the 2005 Review was that these intra-licensee arrangements were put on a formal footing; and
- iii) Viewers, advertisers and programme sponsors - who are the ultimate consumers of the ITV Network output. The ITV channel is broadcast on a nationwide basis with differences in schedule resulting from specific obligations for hours of regional programming. Licensees earn revenue from selling airtime to advertisers, and from programme sponsors who pay to sponsor national networked programmes. ITV plc sells the network's airtime and network programme sponsorship on behalf of all licensees.

2.6 The involvement of the NWC in the above activities is relevant to assessing the potential competition and policy concerns that could arise with the NWA. The core activities of the NWC (also set out in more detail in the 2005 Review publications – see footnote 4) are:

- i) Commissioning and acquisition of programmes: decisions are made centrally on behalf of all licensees, and processes and contracts are governed by the NWA;
- ii) Scheduling: NWC schedules ITV1. The ITV2-4 channel management, who are housed within ITV Network, also have access to ITV1 schedule data which enables them to create complementary schedules. So that non-consolidated licensees can meet their regional programming obligations they are able to opt out of the national schedule at any time in order to schedule regional programmes. Currently there is limited coordination of the scheduling of regional programming between licensees, and in particular the higher volumes of regional programmes shown in the Nations as compared with the English regions are scheduled independently by the three bodies holding respective Channel 3 licences there (SMG, UTV and HTV (part of ITV plc)); and
- iii) Rights and Business affairs: this team negotiates the terms of commissions and acquisitions for ITV1 on behalf of all licensees although programme rights are then held collectively by the licensees, and ITV Network Ltd holds no rights itself.

⁴ See <http://www.ofcom.org.uk/consult/condocs/itv1/main/itv.pdf> and <http://www.ofcom.org.uk/consult/condocs/itv1/statement/261207/>

This team is also responsible for negotiating sports rights deals, which may be shared between ITV1 and ITV2-ITV4. It also negotiates the terms for programmes commissioned by ITV2-ITV4 and the contracts and commercial arrangements associated with ITV's on-line activities and interactivity.

Purpose of this review

- 2.7 Whilst the NWA were introduced under the 1990 Broadcasting Act, the Communications Act 2003 introduced a requirement for periodic reviews of the NWA. Section 293 of the Act requires Ofcom to carry out from time to time a general review of the NWA. The framework for this review is set out in Schedule 11 of the Act and summarised in Annex 1. This sets out a number of statutory tests which Ofcom must take into account, alongside its wider statutory duties, when carrying out this review. Essentially, these tests concern:
- The ability of regional Channel 3 services to be a nationwide system that can compete effectively with other UK television programme services; and
 - The impact of the NWA on competition.
- 2.8 In addition, Ofcom is also required to consider the effect of the arrangements on the ability of the regional Channel 3 licensees to maintain the quality and range of regional programmes and other programmes contributing to the regional character of the services.
- 2.9 Ofcom reviews the NWA in this document from the perspective of these statutory tests and duties. In addition Ofcom must also be mindful of its wider statutory duties and public policy objectives.
- 2.10 Such reviews are required to be carried out no more than a year after the previous review. Ofcom may also, at any other time, carry out a review of the NWA if prompted to do so by a licensee.
- 2.11 The first general NWA review under the provisions of the Act was concluded in June 2005 ('the 2005 Review'), with a further statement in October 2005 principally on matters relating specifically to UTV⁵. In those documents, Ofcom set out its recommendations on how the NWA should be revised in order to address the concerns identified by Ofcom. Before the 2005 Review, the NWA had been largely unchanged since 1993.
- 2.12 The 2005 Review considered both arrangements in relation to external third parties ('external arrangements') and arrangements or agreements between the ITV licensees ('intra-ITV arrangements') although it focused primarily on the intra-ITV arrangements. This was because issues relating to the arrangements between ITV Network and independent producers had recently been addressed through another statutory requirement⁶.

⁵ For these statements, see <http://www.ofcom.org.uk/consult/condocs/itv1/statement/261207/> and http://www.ofcom.org.uk/consult/condocs/itv1/further_statement/further_statement.pdf

⁶ Section 285 of the Act had put in place a framework for each public services broadcaster ('PSB') to have a code of practice for commissioning programmes from independent suppliers. ITV Network Limited produced its own Code of Practice in 2004, covering qualifying independent producers. A qualifying independent producer is one whose programming counts towards fulfilment of the independent production quota.

- 2.13 Ofcom notes that although there is no dispute about the recommendations of the 2005 Review it has nevertheless taken a considerable amount of time for the ITV licensees to agree the implementation of those recommendations with one another. In fact, Ofcom's recommendations have not yet been implemented in full by the licensees, although the NWA documents have been approved in principle by Ofcom. Ofcom does not consider that such a delay in implementation is acceptable and looks to all the parties to move to finalise implementation of the recommendations made in the 2005 Review as quickly as possible.
- 2.14 This document sets out Ofcom's conclusions for the 2006 Review of the NWA, taking into account developments in the sector since the 2005 Review. In the light of the recommendations by Ofcom in this document, Channel 3 licensees will need to amend the documents that make up the NWA, in consultation with Ofcom. Ofcom will then need to review the proposed set of revised NWA before giving its final approval.
- 2.15 Ofcom has also considered in this consultation process possible ways to streamline the NWA review process, given the legal requirement to conduct NWA reviews at regular intervals.

The consultation process

- 2.16 There were 6 responses to the November consultation document, including responses from all ITV licensees as well as from ITV Network in its own right. The two non-confidential responses are published in full on our website⁷. The other respondents submitted responses on a confidential basis.
- 2.17 The points made in the responses are summarised and considered in detail in Sections 3 and 4 of this document.

Structure of this document

- 2.18 The rest of this document comprises the following:
- Section 3 assesses the current NWA, taking into account the consultation responses received;
 - Section 4 addresses other issues raised in the consultation process, including possible future changes to the NWA and the process for reviewing them;
 - Annex 1 describes the statutory framework for reviewing the NWA; and
 - Annex 2 is a glossary of technical terms used in this document.

⁷ See http://www.ofcom.org.uk/consult/condocs/itv_network/

Section 3

Assessment of Networking Arrangements

Introduction

- 3.1 This section sets out Ofcom's review of the current NWA and proposals for how they might need to change. After describing the general framework for assessing the NWA, we look at developments since the 2005 Review and then assess the current NWA documents.
- 3.2 The statutory framework provides for an annual review of the NWA which in turn has necessitated this current review. Given the time taken so far to implement the recommendations of the 2005 review and the fact that no respondents indicated that developments had taken place in respect of intra-ITV arrangements Ofcom has not carried out an assessment of the impact of the 2005 changes on intra-ITV arrangements. In the absence of any other clear changes in the market that would alter the basis on which Ofcom had made its recommendations in the 2005 Review, Ofcom believes that it would be premature to recommend further changes to the relevant parts of the NWA at this time. Instead, the changes arising from the 2005 Review, which represented a major reappraisal of the NWA, should have time to 'bed down' before their efficacy can be properly tested. However, Ofcom considers that it may be appropriate to reflect the experience of how the recommendations of the 2005 review have been implemented as part of the 2007 review of the NWA.
- 3.3 This Review has therefore had a relatively limited scope, an approach which received support from licensees and Pact as Ofcom was scoping the 2006 Review. Notwithstanding this limited approach, Ofcom has considered in a structured way each of the elements of the current NWA.

The framework for this review

- 3.4 The framework for reviewing the NWA is set out in Schedule 11 of the Act. Ofcom must not approve revised NWA (or propose modifications to the existing arrangements), unless it is satisfied that the revised arrangements (or proposed modifications) satisfy the competition test set out in paragraphs 6(3) and 6(4) respectively of Schedule 11 of the Act.
- 3.5 The Act sets out the three statutory tests that Ofcom must take into account, alongside its wider statutory duties, when carrying out this review. These tests, whose precise details are explained in Annex 1 concern:
- The ability of regional Channel 3 services to be a nationwide system of services which is able to compete effectively with other television programme services provided in the United Kingdom;
 - The impact of the NWA on competition; and
 - The ability of Channel 3 licensees to maintain the quality and range of regional programmes and other programmes contributing to the regional character of the services.
- 3.6 In addition to the above statutory tests, paragraph 8 of Schedule 11 of the Act states that Ofcom must not approve, impose or propose arrangements and/or modifications

if such arrangements/modifications would be likely to be prejudicial to the ability of the Channel 3 licensees, or any of them, to comply with:

- a) their public service remits;
- b) their regional production obligations⁸;
- c) their regional programming obligations; or
- d) conditions imposed on them following a change of control.

3.7 Ofcom has reviewed the NWA from the perspective of these specific statutory tests and duties. In addition Ofcom must also be mindful of its wider statutory duties and public policy objectives. Ofcom has also taken into account broader issues stemming from ITV plc's position of strength within the ITV network.

3.8 Ofcom also believes that the following public policy objectives, set out in the 2005 Review, are appropriate guiding principles to use when reviewing the NWA. These objectives cover issues relating to either intra-ITV or external arrangements:

- The documents that together comprise the NWA should continue to reflect accurately the actual operational arrangements;
- Organisational arrangements should be robust to changes in corporate ownership;
- All of the Channel 3 licensees should be able to continue to meet their specific licence obligations efficiently and effectively;
- The principles which underlie the relevant cost sharing arrangements should be transparent and clearly understood by all parties to the NWA; and
- There should be an appropriate degree of non-discrimination between parties to the NWA and (where appropriate) any relevant third parties.

Developments since the 2005 Review

3.9 From Ofcom's perspective, there has only been one significant development in relation to the operation of the NWA since the 2005 Review that requires amendments to be made to the NWA. This issue, which is explained in more detail below, concerns the acquisition of so-called 'new media rights' from independent producers at the time of commissioning of programmes from those producers.

Ofcom's Television Production Sector Review

3.10 The TPSR examined the UK production sector as a whole, looking at both in-house and external (independent) production. There was a specific focus on the commissioning of original content, i.e., the material that broadcasters commission from producers for first transmission on their channels.

⁸ In addition to the above statutory tests, paragraph 8 of Schedule 11 of the Act requires Ofcom to take into account the impact of the arrangements or modifications to the arrangements on the ability of the Channel 3 licensees to comply with certain of their licence obligations

- 3.11 The TPSR looked again at the rationale for intervention in this sector. One of the three main factors which could require intervention was negotiating strength. The TPSR confirmed that there are relatively few buyers of originated programming – the PSBs accounting between them for over 90 per cent of all commissioning - but a very large number of producers. This imbalance was considered likely to provide PSBs with a relatively strong negotiating position with producers. Furthermore, given the current market structure, it might not be possible to rely on effective competition to ensure that PSBs were incentivised to use their negotiating strength in the interests of viewers. Although sources of demand for original content were growing, it was expected that the main terrestrial channels would remain the main buyers of originated content going forward.
- 3.12 The Codes of Practice required for each PSB under section 285 of the Act had sought to address this negotiating position when commissioning programmes from independent producers⁹. The Codes (introduced in 2004) set out a more transparent basis for commissioning deals to mitigate the exercise of broadcasters' negotiating strength. The Codes (and any changes to them) are subject to Ofcom approval.
- 3.13 The TPSR found that the Codes of Practice and the associated terms of trade were generally seen as working well for scheduled broadcast television. However, there was concern over rights for cross-platform distribution and the exploitation of content originally commissioned for TV broadcast¹⁰. Both broadcasters and producers argued that there was a lack of clarity on these issues in the existing Codes of Practice: rights traditionally had been defined in terms of exploitation by platform but were largely silent about emerging new media platforms. There was a concern that PSBs were using this uncertainty to obstruct exploitation of new media rights.
- 3.14 Ofcom set PSBs and the representatives of independent producers the challenge to resolve matters for themselves through commercial negotiation. Subsequently, Heads of Agreement were reached between the Pact and the BBC, ITV1 and Channel 4 in early Summer 2006.
- 3.15 In light of the development of a new windowing framework for commissioning from independent producers, Ofcom is currently in the process of amending its Guidance to broadcasters on Codes of Practice, which it is required to do under section 285 of the Act. This is currently the subject of a separate consultation process¹¹. Once the new Guidance has been put in place then PSBs will need to amend their Codes of Practice and submit them to Ofcom for approval. PSBs will also be in a position to finalise new Terms of Trade which take into account both the agreements on Heads of Terms and the new Codes of Practice.
- 3.16 In the case of ITV Network this specifically would entail changes to the Network Centre Code of Practice, the NPL and the TA.

⁹ The Codes only apply to programming commissioned from qualifying independent producers. Where BBC and ITV commission from their in-house production arms, they retain all rights in those programmes. Channel 4 and five do not have any in-house production – they follow a broadcaster-publisher model.

¹⁰ It should be noted that the Codes of Practice do not apply to content commissioned specifically for new media platforms.

¹¹ See <http://www.ofcom.org.uk/consult/condocs/cop/>

Assessment of the need for revisions to the NWA

- 3.17 Ofcom sets out below its assessment of the changes to the current NWA that it considers will be necessary, by looking at the three broad areas of activity in the ITV Network supply chain identified in paragraph 2.5. Ofcom considers both the arrangements governing the relationships between the Channel 3 licensees and third parties (external arrangements) and those relating solely to the relationships between the licensees themselves (intra-ITV arrangements).

Programme commissioning and acquisition

The Network Centre Code of Practice

- 3.18 As stated in paragraph 3.15, Ofcom is currently consulting on changes to the Guidance on codes of practice that it is required to have in place under section 285 of the Act. As the Code of Practice required under section 285 is the same document as the Code of Practice included in the NWA, changes in Ofcom's Guidance affect the contents of the NWA.
- 3.19 Until that consultation is closed and Ofcom has finalised its revised Guidance, the specific content of the changes needed to the Network Centre Code of Practice are not clear. At this time, therefore, there are no specific amendments to assess against the statutory tests. Ofcom's proposal in the consultation document was therefore limited to recommending that the Network Centre Code of Practice be amended to reflect developments following the TPSR, and that consequent changes also be made to the NPL and TA. In the consultation document, we also asked whether there had been any other major developments since the end of the 2005 Review that might suggest a need to revise the contents of any of the NWA documents.
- 3.20 ITV Network, ITV plc and all confidential respondents agreed with Ofcom about the need to update the three NWA documents to reflect the new heads of terms. ITV Network and ITV plc also wanted to secure subsequent Ofcom approval of these documents as soon as possible.
- 3.21 In the light of these responses, Ofcom confirms that ITV Network will need to amend the Network Centre Code of Practice, TA and NPL following the conclusion of Ofcom's consultation on guidance on the Codes of Practice under section 285 of the Act, and submit them to Ofcom for approval.
- 3.22 Ofcom has considered whether there is a need for the new heads of terms and Code of Practice to be reflected in the NWA before programme commissioning can take place under the agreement on new media rights. Ofcom considers that although the Code of Practice, NPL and TA will need to be amended in accordance with the new heads of terms and Ofcom's revised Guidance on the Codes of Practice, there is already broad agreement between the parties that would be consulted. Nevertheless, there is a formal requirement under Schedule 11 of the Act for Ofcom to consult upon changes to the NWA and Ofcom recognises that this process may delay commissioning on the basis of the new arrangements. It is not Ofcom's intention to adopt a formalistic approach which would delay commissioning on the basis of the new arrangements (both under the NPL and TA).
- 3.23 Against that background, Ofcom considers that it should be possible for the parties to begin to commission programmes based on the new agreement with Pact on new media rights despite the fact that the formal approval process for changes to the NWA may not have taken place at that time. Formal approval for the changes to the

NWA would then be obtained in accordance with Schedule 11 of the Act. The position adopted by Ofcom at this stage would change, however, in the event that Ofcom were to be made aware of issues arising from the operation of the revised NWA subject to the approval process which may be inconsistent with the tests laid down in the Act. In addition, in light of the delays with the implementation of the recommendations of the 2005 Review, if after two months from the point at which Ofcom's Guidance has been finalised, ITV Network has not submitted a Code of Practice for approval, then Ofcom will revisit the issue and will consider requiring ITV Network to return to commissioning under the existing Network Code of Practice.

Other issues

- 3.24 In the consultation document Ofcom stated its view that there have not been any other substantive changes in programme commissioning and acquisition since the 2005 NWA review that would lead it to propose any changes to the relevant parts of the NWA documents. This view applied to both external arrangements and intra-ITV arrangements. Ofcom therefore proposed no further changes to the relevant provisions in the NWA beyond those recommended in the 2005 Review.
- 3.25 Stakeholders' responses all agreed with Ofcom's view (albeit that some raised a related issue that is covered in paragraphs 3.31 to 3.32). Ofcom therefore confirms that there are no developments in this area requiring a change to the NWA.

Channel operation services

- 3.26 From Ofcom's perspective, there have not been any substantive changes to the working of channel operation services since the 2005 Review that would lead it to propose any changes to the relevant parts of the NWA documents. This applies to both external arrangements and intra-ITV arrangements. As discussed above, the recommendations of the 2005 Review in respect of intra-ITV arrangements are still in the process of being implemented. Ofcom therefore proposed no further changes to the relevant provisions in the NWA beyond those recommended in the 2005 Review.
- 3.27 Stakeholders' responses all agreed with Ofcom's view. Ofcom therefore confirms that there are no developments in this area requiring a change to the NWA.

Viewers, airtime sales and sponsorship

- 3.28 As with channel operation services, to the best of its Ofcom's knowledge, there have not been any substantive changes to the arrangements for airtime sales and sponsorship since the 2005 NWA review that would lead it to propose any changes to the relevant parts of the NWA documents. This applies to both external arrangements and intra-ITV arrangements. Ofcom therefore proposed no further changes to the relevant provisions in the NWA beyond those recommended in the 2005 Review.
- 3.29 Stakeholders' responses all agreed with Ofcom's view. Ofcom therefore confirms that there are no developments in this area requiring a change to the NWA.

Conclusion

- 3.30 Ofcom considers that the existing NWA meet the tests of Schedule 11 of the Act and, in particular, the competition test set out at paragraph 6 of that Schedule. On this basis, Ofcom proposes to approve the NWA at this point without requiring any immediate amendment to the documents comprising the NWA. The ITV Network

Code of Practice, TA and NPL will need to be amended after Ofcom has revised its Guidance on codes of practice under section 285 of the Act.

- 3.31 In response to Ofcom's preliminary assessment of the need for changes to any of the NWA documents as a result of changes in the sector, one other point was raised. Some of the confidential respondents expressed concerns about ITV plc simulcasting its licensed PSB content on broadband and believed that this issue was relevant to the 2006 Review. The underlying concern was the extent to which this development might undermine a licensee's exclusivity in the delivery of the Channel 3 service in its licence area. There was a suggestion that these concerns needed to be addressed as part of the NWA.
- 3.32 Ofcom acknowledges the fact that the delivery of a Channel 3 service by broadband raises a number of interesting questions. However, the provision of regional variations of the Channel 3 service as part of the ITV Broadband service is subject to on-going discussions between licensees and the service has yet to launch. Ofcom therefore considers that it would be premature for it to take a view on this matter without any evidence. Ofcom considers that it may be appropriate to examine this issue in more detail as part of the 2007 NWA Review at which time the effect of the ITV Broadband service on the NWA may be clearer.

Section 4

Other issues from the consultation

4.1 In the consultation document, Ofcom asked some specific questions about the future conduct of NWA reviews and also afforded the opportunity for stakeholders to raise any other points. This section addresses each of the issues arising from those questions.

Future NWA reviews

4.2 The Act requires that the NWA are reviewed on an annual basis. In the consultation document, Ofcom raised the possibility of making changes so that future NWA reviews follow a streamlined process, where possible.

4.3 The first issue raised was the future process of consultation for NWA reviews. Ofcom has an obligation under the Act to bring possible changes to the NWA to the attention of parties who, in Ofcom's opinion, are likely to be affected¹². Ofcom must then allow a reasonable time for representations between publishing those potential changes and deciding whether or not to approve the NWA.

4.4 Ofcom proposed in the consultation document that this requirement may be met within a more flexible approach whereby a formal consultation stage is included only where there is cause to believe it is necessary. The process in this situation was set out as:

- Informal consultation with the most directly interested parties – licensees and the representatives of independent producers¹³ - on the operation of the NWA and any changes they would like to see; followed by
- Publication of a brief Ofcom statement that would: refer to the analysis in the preceding NWA review; assess whether the legal tests are met in respect of any proposed minor modifications to the NWA; and confirm how and when the NWA should change in the event that further representations are not received.

4.5 We proposed that in circumstances where more material changes to the NWA were proposed, due to a change in the market or experience of how the NWA are working, a more formal consultation process would be more suitable. However, with changes that are considered to be minor and uncontroversial we considered it reasonable to retain the ability to amend the NWA without unnecessarily formal steps.

4.6 We also suggested that avoiding in-depth formal reviews of the NWA may also encourage a focus on the pragmatic and effective implementation of the NWA rather than regular and detailed redesign of the NWA documents. In Ofcom's view, changes to NWA documents and processes should generally be assessed only after they have been operating for a reasonable period of time.

4.7 It is important to note that, in proposing this approach, Ofcom was mindful that the Act also allows it to review the NWA at any time in response to a request to do so from a licensee. Ofcom can therefore decide at any point to conduct a formal consultation if major issues are raised outside of the annual review process.

¹² see Paragraph 3 of Schedule 11

¹³ and the OFT, who must be consulted under the Act

- 4.8 In response to this proposal, stakeholders' views varied between ITV plc not wanting Ofcom to bind itself to holding formal consultation even for material changes, to one respondent wanting formal consultation when any party disagrees with, or has major concerns with, a proposed change. Responses varied on whether it was possible and preferable to set out clear criteria beforehand for when a formal review would be needed.
- 4.9 However, respondents did agree that informal consultation was an acceptable first step in preference to necessarily always embarking on a formal consultation process.
- 4.10 In light of these views, Ofcom has decided that – as a first step - future NWA reviews will initially consult the most directly interested parties – licensees and the representatives of independent producers¹⁴ - on an informal basis. Ofcom does not consider it appropriate to adopt a set of fixed criteria as to whether a formal consultation should be used. Instead, following informal consultation on the operation of the NWA and any changes that interested parties would like to see, Ofcom will consider whether formal consultation is needed. This approach would still provide the relevant parties with the opportunity to raise concerns and to make representations to Ofcom.
- 4.11 The second issue raised in the consultation document about future NWA reviews was whether all the documents that currently sit within the NWA needed to remain part of the NWA. The Act does not specify the form that the NWA should take, so there is no absolute requirement that the NWA documents should remain in their current form. For example, removing the NPL and the TA from the NWA could allow greater flexibility in how the NWC commissions programmes from regional licensees and independent producers respectively, in that necessary changes to those documents would not first require Ofcom scrutiny and public consultation.
- 4.12 When raising this issue with key stakeholders informally before consultation there did not appear to be a clear appetite to consider this issue within the 2006 NWA review. This seems understandable given that the implementation of the recommendations of the 2005 Review, including the consequent changes to the NWA documents, have taken a long time to finalise.
- 4.13 However, stakeholders' formal consultation responses varied on this issue. ITV Network considered that the TA and NPL no longer needed to be regulated as producers had recourse to PACT were ITV to seek to impose tougher terms than in the Terms of Trade agreed with PACT. ITV Network also considered that the Code of Practice should not be regulated under the NWA as it is already regulated under section 285, and that such double regulation was counter-productive and confusing. ITV Network suggested that the ITV Code of Practice and Statement of Principles could include a commitment that all producers - licensees & external - would be treated equally. ITV plc also considered that the Code of Practice under section 285 was sufficient, without having the Code of Practice also in the NWA. Further, ITV Network considered that it was not necessary to keep the TA & NPL regulated as that over-prescribed the documentation used to commission programming.
- 4.14 Other stakeholders were less keen on changing the set of documents in the NWA. One respondent appreciated the value of commercial flexibility but also wanted appropriate safeguards for its interests. Another suggested that the TA and NPL might be removed if a separate Code of Practice continued for ITV producers within the NWA. However, some comments have been made by these stakeholders, both in

¹⁴ and the OFT, who must be consulted under the Act

their responses and since then, that they would be concerned if these documents were removed from the NWA at this point in time, i.e., while the new terms of trade that include new media rights issues are still in the process of being finalised. Concern was also expressed that there should be equal treatment between in-house and external suppliers.

- 4.15 Ofcom consulted on this issue in order to gain views for future NWA reviews, and the consultation responses were provided on that basis. Whilst Ofcom did consider whether there might be scope to remove documents from the scope of the NWA sooner, as part of the 2006 review, subsequent discussions with consultation respondents on the potential for such a move have indicated that it may be premature to do so at this stage when the revised Network Centre Code of Practice, TA and NPL remain to be seen. Ofcom has therefore decided not to change the set of NWA documents now, which reflects our consultation document approach. However, Ofcom does believe that it should be possible to maintain the NWA obligations in a less specific way by removing at least the NPL and TA from the set of NWA documents once the agreements have been updated to reflect the new terms of trade and a new Code of Practice. Ofcom therefore expects to take forward this proposition in the course of the 2007 NWA Review.

Relevance of the 1992 MMC report

- 4.16 In its consultation response, ITV Network asked for clarification that a specific recommendation of the 1992 report of the Monopolies and Mergers Commission¹⁵ - that ITV should only acquire primary broadcast rights – could be no longer deemed to be binding on ITV. ITV Network noted that the recent deal with PACT allows ITV to acquire a larger set of rights.
- 4.17 Ofcom can confirm that this specific recommendation of the MMC report can be deemed no longer to apply. Ofcom considers that this recommendation has been superseded by market events and, in particular, by other regulatory and statutory provisions (including but not limited to, Ofcom's annual review process set out in the Act. Ofcom does not therefore consider that the recommendation in respect of limiting the sets of rights which ITV NWC may seek to acquire continues to bind ITV Network and ITV plc. Ofcom will, however, continue to monitor the issues raised in the 1992 report as part of its annual reviews of the NWA.

First run on ITV1

- 4.18 One respondent asked that Ofcom should reinforce that programmes purchased out of NPB should have their first run on ITV1, not another platform or channel.
- 4.19 Ofcom considered this point in the 2005 NWA Review. Ofcom stated in its October 2006 statement that "as a general rule, programming..... funded from the Network Programme Budget is intended to be for first run exclusive transmission on ITV1. This is a general principle, which would not prevent ITV Network from agreeing different arrangements in some circumstances where this is of benefit to ITV1. Indeed, this is consistent with the general principle that the operation of ITV Network should be led by the needs of ITV1"¹⁶. Ofcom's view has not changed since then.

¹⁵ See http://www.competition-commission.org.uk/rep_pub/reports/1993/331.htm

¹⁶ See Section 4 at http://www.ofcom.org.uk/consult/condocs/itv1/further_statement/

Detailed points of clarification from ITV plc

- 4.20 ITV plc raised a number of detailed points of clarification in its consultation response. Two of these points related to the criteria used in reviewing the NWA. ITV plc referred to Ofcom's statement that it had "taken into account broader issues stemming from ITV plc's position of strength within the ITV Network". ITV plc stated that Ofcom should also consider whether ITV plc's 'position of strength' had increased since immediately after the Carlton-Granada merger and, if so, whether that has harmed Channel 3's ability to be a competitive nationwide system or caused a negative effect in terms of the NWA's impact on competition.
- 4.21 Ofcom does not consider that the position of ITV plc within ITV Network has changed over the period of review. Ofcom understand that ITV plc continues to hold a 92% holding of the shares in ITV Network and therefore holds a position of strength within ITV Network in comparison to the other licensees. In considering the matters set out in Section 3 of this document, Ofcom has therefore taken account of ITV's position within ITV Network to reach its conclusions.
- 4.22 ITV plc also refers to Ofcom's comment in the consultation document (paragraph A5.13) that one of its guiding principles when reviewing NWA documentation is that: "the non-consolidated licensees should be able to continue to meet their specific licence obligations efficiently and effectively". ITV plc suggested a slightly different principle, that: "all of the Channel 3 licensees should be able to continue to meet their specific licence obligations efficiently and effectively". Ofcom agrees with this suggestion and has reflected this in paragraphs 3.8 and A1.13 of this document.
- 4.23 In addition, Ofcom agrees with ITV plc's detailed clarifications that:
- The current Code of Practice applies to all producers, including Channel 3 licensee producers and external producers;
 - Whilst the scope of the NWA was phrased broadly in the consultation document, the areas of activity within the NWA are the 'core functions' of ITV Network - commissioning, acquisition, scheduling and negotiation of the price of ITV1 network programmes, and that Ofcom also regulates ITV Network activity in relation to the undertakings given to the OFT on the Granada-Carlton merger; and
 - Paragraph 3.7(c) of the consultation document should have acknowledged the 2005 Review decision that secondees to ITV Network, as well as its employees, could perform the core functions of ITV Network Centre;

Annex 1

The statutory framework for reviewing the NWA

Introduction

- A1.1 The framework for this review is set out in Schedule 11 of the Act. Ofcom must not approve revised NWA (or propose modifications to the existing arrangements), unless it is satisfied that the revised arrangements (or proposed modifications) satisfy the competition test set out in paragraphs 6(3) and 6(4) respectively of Schedule 11 of the Act.
- A1.2 The Act sets out the three statutory tests - described below - that Ofcom must take into account, alongside its wider statutory duties, when carrying out this review. Ofcom reviews the ITV Networking Arrangements in this document from the perspective of these statutory tests and duties. In addition Ofcom must also be mindful of its wider statutory duties and public policy objectives. As a general rule, Ofcom must not propose, impose or approve arrangements or modifications to the arrangements unless it considers that such arrangements or modifications are satisfactory.
- A1.3 The statutory competition test is focused on restrictions of competition arising from the arrangements themselves, as opposed to restrictions of competition arising from the unilateral behaviour of one of the parties to the arrangements. When this test was conceived, the Channel 3 licensees were not so unevenly matched. ITV plc now owns 11 of the 15 licences, affording it a position of strength within the ITV network that creates different competition issues, which we believe are not covered by the statutory competition test, but which are nevertheless relevant to the arrangements between ITV licensees.

The 'Competition Test'

- A1.4 The statutory Competition Test set out in paragraph 6 of Schedule 11 of the Act is in two parts:
- Arrangements satisfy the first Competition Test if they do not have as their object or effect the prevention, restriction or distortion of competition within the United Kingdom. If the arrangements satisfy this test, there is no need to consider the second test; and
 - Arrangements satisfy the second Competition Test if (a) they do have such an object or effect; but (b) they would satisfy the criteria set out in section 9 of the Competition Act 1998.
- A1.5 Before making a decision about whether a competition test is satisfied or not, Ofcom must consult the Office of Fair Trading. In determining whether arrangements or modified arrangements would satisfy either of the tests, Ofcom must ensure the principles it applies and the decisions it reaches are consistent with the EC Treaty and any relevant decisions of the European Court. In addition, it must have regard to any relevant decisions or statements of the European Commission.

A1.6 The NWA are excluded from the application of the Chapter I Prohibition under Schedule 2 to the Competition Act 1998 to the extent that they fulfil the relevant competition tests set out in Schedule 11 of the Act. However, the licensees are still prevented from engaging in any practice which is prejudicial to fair and effective competition (towards external parties and to each other) by conditions in their licences. The licensees also remain subject to the Chapter II prohibition in the Competition Act 1998.

The 'Effectiveness Test'

A1.7 Ofcom must not approve, impose or propose arrangements and/or modifications unless Ofcom considers those arrangements / modifications to be satisfactory for the purpose of enabling regional Channel 3 services (taken as a whole) to be a nationwide system of services which is able to compete effectively with other television programme services provided in the United Kingdom.

The 'Regional Programming Test'

A1.8 Ofcom must not approve, impose or propose arrangements and/or modifications unless Ofcom considers those arrangements/ modifications to be satisfactory, including the likely effect of the arrangements/ modifications on the ability of Channel 3 licensees to maintain the quality and range of regional programmes and other programmes which contribute to the regional character of the services.

A1.9 It should be noted that the second and third statutory tests relate to public policy rather than specifically to competition law.

A1.10 In addition to the above statutory tests, paragraph 8 of Schedule 11 of the Act states that Ofcom must not approve, impose or propose arrangements and/or modifications if such arrangements/modifications would be likely to be prejudicial to the ability of the Channel 3 licensees, or any of them, to comply with:

- a) their public service remits;
- b) their regional production obligations¹⁷;
- c) their regional programming obligations; or
- d) conditions imposed on them following a change of control.

Ofcom's other duties and objectives

A1.11 Section 3 of the Act sets out Ofcom's general duties and the matters that Ofcom must take into account in performing its duties. These matters include:

- a) the desirability of promoting the fulfilment of the purposes of public service television broadcasting in the United Kingdom;
- b) the desirability of promoting competition in relevant markets;

¹⁷ In addition to the above statutory tests, paragraph 8 of Schedule 11 of the Act requires Ofcom to take into account the impact of the arrangements or modifications to the arrangements on the ability of the Channel 3 licensees to comply with certain of their licence obligations

- c) the desirability of promoting and facilitating the development and use of effective forms of self-regulation; and
- d) the desirability of encouraging investment and innovation in relevant markets.

A1.12 Ofcom also has a general regulatory principle that it will always seek the least intrusive regulatory mechanisms to achieve its policy objectives.

A1.13 Ofcom also believes that the following public policy objectives (as articulated in the 2005 Review) are appropriate guiding principles to follow when reviewing the NWA:

- the documents that together comprise the NWA should continue to reflect accurately the actual operational arrangements;
- organisational arrangements should be robust to changes in corporate ownership;
- all of the Channel 3 licensees should be able to continue to meet their specific licence obligations efficiently and effectively;
- the principles which underlie the relevant cost sharing arrangements should be transparent and clearly understood by all parties to the NWA; and
- there should be an appropriate degree of non-discrimination between parties to the NWA and (where appropriate) any relevant third parties.

Annex 2

Glossary

<i>Act, the</i>	Communications Act 2003
<i>Channel</i>	Channel Television Ltd: Owner of the Channel Islands regional Channel 3 licence
<i>Channel 3</i>	Free-to-air, commercially funded, national television broadcast channel, made up of 15 regional licensed areas
<i>Code of Practice</i>	(1993) - Network Centre Code of Practice: NWA document intended to guarantee an even-handed treatment of in-house and independent producers with respect to programme commissioning
<i>Code of Practice</i>	(2004) – ITV Network Limited Code of Practice for Commissioning Programmes from Independent Producers: Code of Practice concerning the commissioning from independent producers, drawn up in line with requirements under section 285 of the Act
<i>Competition Test</i>	Statutory Competition Test set out in paragraph 6 of Schedule 11 of the Act
<i>Effectiveness Test</i>	Statutory Public Policy Test set out in Schedule 11 of the Act
<i>External Arrangements</i>	arrangements in relation to external third parties, such as external programme producers
<i>Intra-ITV Arrangements</i>	Arrangements or agreements between the ITV licensees
<i>ITV1</i>	ITV national broadcast channel comprising the Channel 3 licensees (as distinguished from ITV plc wholly-owned channels, e.g., ITV2, ITV3)
<i>Non-consolidated Licensees</i>	SMG, UTV and Channel
<i>NPB</i>	Network Programme Budget: Budget for the ITV1 network programming made up from contributions from each Channel 3 licensees
<i>NPL</i>	Network Programme Licence: the standard form of contract for use by the NWC when it commissions a programme from a regional licensee
<i>NSC</i>	Network Supply Contract: Part of NWA, specifying each regional licensee's share of contribution to the Network Programme Budget
<i>NWA</i>	Networking Arrangements: Set of arrangements between ITV Network and ITV plc, SMG, UTV and Channel to coordinate the

provision of a national television service capable of competing with other broadcasters in the UK

NWC	ITV Network Centre: Management structure within ITV Network Ltd, responsible for executing instructions of the Network Council
Network Council	(‘Council’): The Board of the NWC, responsible for agreeing the strategy and budget for ITV1
Pact	Producers Alliance for Cinema and Television – UK trade association that represents the commercial interests of independent feature film, television, animation and interactive media companies
PSB	Public Service Broadcaster licensed under the Act
Regional Programming Test	Statutory Public Policy Test set out in Schedule 11 of the Act
SMG	SMG plc: Owners of Grampian Television Ltd and Scottish Television Ltd, the two Scottish regional Channel 3 licensees
Statement of Principles	Network Centre Statement of Principles: NWA document dealing with the control of network policy by the licensees, the implementation of that policy by the NWC, the selection of programmes, the budget and the supply of a network schedule and provides for the NWC to be organised within the management structure of ITV Network Ltd
Tripartite Agreement	Tripartite Commissioning, Production and Compliance Agreement: Contractual arrangement as part of the NWA, used by the NWC when commissioning a programme from an independent producer
UTV	Ulster Television Plc: Owner of the Ulster regional Channel 3 licence