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Scotland Independence: Media and Telecoms

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20 March 2014

Scotland's SNP-led Government has published its White Paper setting out its assumptions for independence, including on broadcasting and telecommunications

The SNP promises an unchanged commercial broadcasting environment, while the Scottish Broadcasting Service (SBS) would occupy the BBC's position today. SBS expects to obtain BBC One and BBC Two on free-to-air terms, which seems very unlikely to be agreed by BBC Worldwide

Spectrum management will be assumed by the new Government, implying a possible discontinuity in existing UK-wide 3G and 4G licenses attributed by Ofcom

On 18 September 2014, voters in Scotland will be called to vote in the referendum asking "Should Scotland be an independent country?" at the behest of the SNP led by First Minister Alex Salmond. If the Yes campaign wins, Scotland will declare its independence on 24 March 2016.

Surveys of those likely to vote indicate the No vote has the lead with 45%, the Yes campaign commands 37% voter share, leaving the critical undecideds to play for in the 6 months ahead. A victory for the No campaign is far from certain.

The implications for the regulated media and telecoms sectors of the UK are seismic: the territory of the UK will be divided by a new border, and Acts of the next Scottish Parliament, to be elected in May 2016, will govern both the commercial and public sector delivery of broadcasting and telecommunication services to 5.2 million Scots. Companies that operate in the UK today anticipate establishing new companies in the future should they remain in Scotland.

The White Paper's assumptions are outcomes most favourable to Scotland's economic interest, however also engaging the implicit agreement of external parties. By far the most important ask is for Westminster to agree a currency union, thus preserving existing safety nets for depositors in Scotland's banks. Whilst there is nothing stopping Scotland from using sterling (aside from the matter of EU accession and its insistence upon new members pledging to join the euro), George Osborne has made it clear the UK has no incentive to accede to SNP demands for a currency zone. In response, the First Minister has threatened to "walk away" from Scotland's share of UK debt, which could impair Scotland's ability to finance its own debt.

Next to the ambition of currency union, the assumption that the BBC will accede to free-to-air terms for BBC One and BBC Two pales into insignificance. We have estimated this amounts to a cross-border subsidy of £270 million, and consider it unlikely that BBC Worldwide, the commercial arm, will accede to this demand.

Spectrum and independence

The radio spectrum (radio frequencies 10 kHz to 3000 GHz) can be described in layman's terms as the aerial real estate that every Government manages for commercial and public sector purposes, in the wider context of European-level and international cooperation. The ITU is the broadest forum for spectrum management and is accustomed to modifying territorial demarcations for instances of the disintegration of states and the creation of new ones.

The responsibility for allocating spectrum will certainly be amongst the prerogatives assumed by the new Scottish state, possibly in time for the declaration of independence in March 2016.

In the UK, the public sector occupies a reserved 25% of the spectrum, as the armed forces and secret services maintain a dense channel of communications. Every sovereign Government has defence amongst its core missions and the SNP fully intends to assume this role. So we can expect a portion of the spectrum to be set aside for the future Scottish armed forces and secret services.

By Act of the UK Parliament, Ofcom is the regulator for private sector use of spectrum. Ofcom manages the spectrum in an open and transparent manner designed to balance efficiency of use and the public interest, consistently with spectrum's status as a public resource in finite supply. No private entity in the UK may use spectrum without Ofcom licensing it to do so, with the exception of Wi-Fi and Bluetooth.

The BBC is also a major public sector user of broadcasting to deliver its radio and TV services, overlapping with private market users. DTT broadcasting, radio services and mobile telecommunications are the leading private sector uses.

Access to spectrum is 'gifted' to radio and TV broadcasters in the UK for historical reasons and because of their assumption of obligations on public service broadcasting, as set out in their broadcast licenses granted by Ofcom.

Operator use of 3G and 4G spectrum has instead been auctioned since the turn of this century, generating a total of £24 billion in revenues in 2000 and 2013, absorbed by the Government.

Acts of the Scottish Parliament can be expected to establish the Scottish equivalent of Ofcom - let's call it Scotcom - which will also be a converged regulator for broadcasting and telecommunications, as is required by European Framework Directives.

The White Paper states the three principles of the broadcasting policy for Scotland:

- "there should be an increase in production opportunities for Scottish producers, and an increase in productions that reflect life in Scotland and of Scots
- Scottish viewers and listeners should continue to have access to all their current channels
- there should be no additional cost to viewers and listeners as a consequence of independence"

The White Paper states that Channel 3 and 5 licences will be honoured in Scotland (renewed to 2025 in the UK). Publicly-owned Channel 4 (in the UK) will be required to agree a higher commissioning budget for Scotland as a quid pro quo for its broadcasting licence; its allocation to the Nations was recently increased from 3% of commissions to 9% as of 2015. In practice, it is highly likely that broadcasters with licenses issued by Ofcom will need to establish in Scotland and seek to secure licenses from Scotcom to broadcast in Scotland.

BSkyB does not require access to spectrum as satellite is over the top of spectrum. But it does require a license from Ofcom to broadcast to the UK. No mention in the White Paper, but it would not be a problem to serve multi-territory with no additional costs. It too would require a licence from Scotcom (Tier 1 obligations).

Other details of Scotland's broadcasting policy are left unclear. Will Scotland replicate the UK's PSB system? Will quotas on news programmes and current affairs programmes be imposed for Scotland? What about common standards (Tier 1 obligations) to all broadcasters? Ofcom's Broadcasting Code? These important questions affect the viability of broadcaster entry into Scotland, but at least the welcome mat is out for the commercial broadcasters.

Scottish Broadcasting Service

Culture is core to define national identity and the SNP has championed the promotion of Scotland to TV, radio and online audiences in Scotland and to the world. The First Minister said in 2008: "If broadcasting is to be a window on the world, it must be a world we recognise - portraying Scotland's identity and cultural diversity, and the new confidence and ambition of our people".

The Scottish Broadcasting Service will be established by Act of the Scottish Parliament and is to replace the BBC when its Charter ends in December 2016. The backbone of the SBS would consist of the BBC's publicly owned assets in Scotland, spanning its transmission network (shared with Arqiva in Scotland at key points), its physical assets and 1,000 employees. In addition, Scotland intends to claim a per capita profits share from all the BBC's commercial ventures to fund the SBS.

BBC assets will presumably be part of the pot of publicly-owned assets that would be the subject of horse-trading in the grand negotiations to take place once separation is decided, noting the conflict over currency union could undermine these negotiations. It is to be assumed that BBC employees, which are civil servants, will have the choice of being repatriated to rUK.

The White Paper states: "On TV, the SBS will begin with a new TV channel and take on the responsibility for BBC Alba [weekly audience of 687,000 viewers in a population of 5.2 million]. On radio, the SBS will begin with a new radio station in addition to taking on responsibility for Radio Scotland and Radio nan Gàidheal. The SBS will also provide online services, including a catch-up player and news website. Over time, the SBS will develop its services to reflect the broad interests and outlook of the people of Scotland."

The White Paper states: "On independence, the licence fee will be the same as in the rest of the UK, and all current licence fee payment exemptions and concessions will be retained." It expects to raise £320 million from the licence fee (based on 2.2 million households and £145.50/annum), £13 million from BBC commercial profits, and keep the £12 million already paid out by the Scottish Government for Gaelic broadcasting. The combined total for publicly-funded public service broadcasting in Scotland would amount to £345 million.

Looking at these figures in closer detail, it's important to take into account:

- the cost of collecting the licence fee, which are some £111 million annually, so perhaps £10 million in Scotland
- exemptions for blind people and households headed by 75+ (which will grow over time), which were 16.5% of licence-fee paying households. The licence fees of 75+ TV households are currently funded by the Department of Work and

Pensions, so we should expect the Scottish equivalent will need to contribute £53 million to the SBS
- The SNP's claim to a share of BBC Worldwide profits in perpetuity appears particularly preposterous, since Scotland is thus claiming to own a share of the commercial arm of the BBC

So the worst case scenario for the SBS is a budget of £257 million. This compares with Ireland's budget of £275 million for RTE.

Turning to the expenditure side, the latest published figures from the BBC on network TV, radio and online content spend in Scotland is £94 million. This figure is, according to the SNP, too low in relation to the £320 million raised by the licence fee in Scotland.

The BBC discloses in its accounts that it devotes 64p on content for every £1 spent, so everything else being the same, the SBS will presumably be able to double expenditure on commissioning productions in Scotland. It can also run a leaner public service broadcaster than the BBC, thus boosting the share to content.

A key assumption of the White Paper is that the SBS will obtain free-to-air terms for BBC One and BBC Two as a result of "working with the BBC in a joint venture". In exchange for Scottish programming fed in the BBC network, SBS will obtain BBC One and BBC Two.

Currently, BBC Scotland feeds 939 hours of programming to the network, much of it commissioned from independent production companies located in Scotland. This includes the production of BBC shows which would naturally be relocated to rUK upon independence, thus reducing the network supply.

The BBC makes available some 50,000 hours of network programming to Scotland through all TV network services. For BBC One and BBC Two alone, the BBC spends a whopping £2 billion annually in programming and distribution (81% of total TV programming), plus a proportionate share of staffing costs (£540 million), financed by UK TV household licence fees and BBC Worldwide. Divided by 25 million licence fee households, that's worth at least £120/year or £10/month per household.

This content is supplied free-to-air to UK licence fee payers because they have paid the fee. However, the Scots will be paying their licence fee to the SBS. So in order to meet the SNP's pledge that there will no incremental costs to Scots, the SNP will insist the BBC give the Scots the extraordinary benefit of BBC programming produced at huge cost for its home audience. Surely, there will be howls of protest from licence fee payers in rUK regarding this largesse for households north of the border.

This is clearly no bargain for the BBC or for the UK licence fee payers that support the BBC. While free-to-air terms for the BBC in Scotland is on the SNP wishlist, along with sterling zone (and many others), it is not in the SNP's power to deliver on this promise, but the UK Government's.

We think it is unlikely that SBS will obtain free-to-air terms given the BBC's policy of applying commercial terms to carriage of its channels in foreign countries. For one thing, those foreign countries – Ireland at the top of the list – will want to question why Scotland gets the BBC on free-to-air terms, whilst the Irish have to pay for the BBC.

The BBC often buys in programming from abroad (e.g. *The Killing*), and would presumably wish to buy some Scottish programming if it was of potential interest to English audiences, but is unlikely to want all SBS network programming.

The external exploitation of the iPlayer on iTunes in the 18 EU markets where it is made available gives us some idea of the charges for BBC broadcast window programming, including BBC One and BBC Two. The iPlayer is charged at €7.99/month, which is a discount on the licence fee as it stands.

Another model for the future role of the BBC in Scotland is Ireland, alluded to by the First Minister in his address to the RTS in August 2012. Curiously, the 2010 Memo of Understanding between the state broadcaster RTE and the BBC on digital switch-over was initially reported as being on reciprocal free-to-air terms, but then corrected to commercial in the National Archives.[1]

Ireland is a good example of a small population producing good quality audiovisual content, which is sometimes exported to secondary exploitation in the UK and other English-speaking countries. But it pales into insignificance next to the BBC.

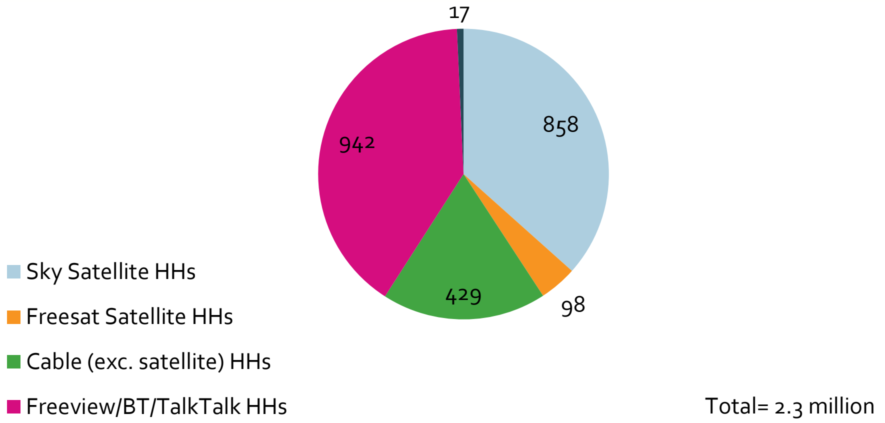
The question of free-to-air terms for Scotland is unanswerable by the BBC, which has understandably decided not to intervene in the referendum campaign. So the SNP has put forward a plan for broadcasting in Scotland that has little chance of being delivered, but on which the voters in the referendum will not be dealt the facts before the referendum is held.

TV homes in Scotland today

Leaving aside the future broadcasting environment in an independent Scotland, the current supply of broadcasting in Scotland is quite similar to that in the UK.

The free-to-air platform Freeview is available to all 2.2 million TV homes in Scotland, and is the main platform for 942,000 homes. BBC One and BBC Two are of course carried on the platform, along with other BBC channels. Scots living in the Borders region receive BBC transmissions from England and Wales due to signal overspill.

Scotland TV HH (000s Nov-13)



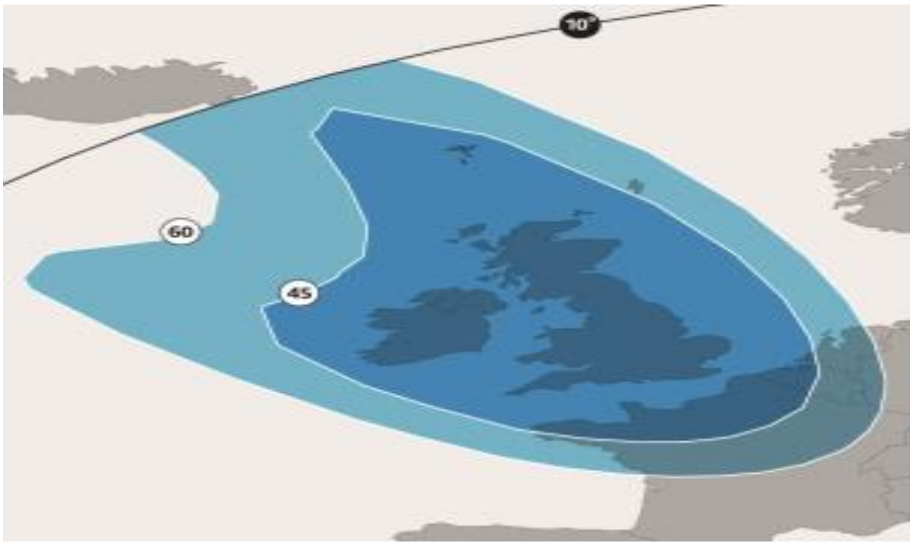
[Source: Enders Analysis based on BARB]

The BBC is also carried on Freesat whose satellite footprint coves both Scotland and Ireland. In Scotland, some 98,000 TV homes use Freesat. This stand-alone service requires the purchase of a receiver: it appears that a UK postcode is required to activate the decoder, but this has been circumvented in Ireland.

[1] "The Memorandum commits the two Governments to facilitating the widespread availability of RTE services in Northern Ireland on a free-to-air basis, and BBC services in Ireland on a paid for basis."

The BBC is also carried by BSkyB, which counts 858,000 subscribing TV homes in Scotland. If we look to Ireland, BBC One and BBC Two are also offered by Sky Ireland, and Sky Scotland would probably offer BBC One and BBC Two to its subscribing households. Scottish TV homes will also retain access to BBC One and BBC Two on cable provider Virgin Media. So it is likely that the only risk to reception of BBC One and BBC Two in an independent Scotland resides in the free-to-air homes on the DTT platform.

Astra 1N UK Range



[Source: UKFreeTV]

Scotcom and telecommunications

In contrast to broadcasting policy, where the SNP's tone was in the vein of "nothing much will change after independence", the SNP was roundly assertive on spectrum management and its implications for Scotland's telecommunications policy. It claims that Westminster's handling of the spectrum auctions has not served Scotland's interests, because there are substantial gaps in 2G and 3G coverage supplied by the four MNOs to date.

Scotland has a demanding geography for mobile communications. A recent report by the Scottish Executive identified 2,552 Not Spots.[2] These are generally found in areas where it is not commercially viable for the MNOs to provide their services, for example rural areas with scattered and remote premises. But MNOs can be forced to provide coverage through licensing conditions, which they will typically reflect in the price they are willing to pay for the spectrum.

The White Paper states: "In telecommunications policy, our approach will give greater priority to improving geographic coverage, particularly in remote rural areas." It devoted attention to the fact that Ofcom's auctioning of 4G spectrum had imposed a coverage obligation in Scotland on only one operator, Telefonica. It's true that only one of the 4G spectrum bands auctioned came with a coverage obligation attached, and O2 bought this spectrum band, hence the relevance to O2. As a result, O2 is to provide 95% indoor coverage across Scotland by 2017, which is likely to provide 98-99% outdoor coverage. The White Paper complains that parts of rural Scotland are still likely to endure poor 4G coverage and Sweden is already at over 90%.

[2] "Mobile Performance and Coverage in Scotland", September 2013

2G and 3G mobile coverage								
	2G				3G			
	Geographic coverage		Premises coverage		Geographic coverage		Premises coverage	
	No signal for any operator	Signal for all operators	No signal for any operator	Signal for all operators	No signal for any operator	Signal for all operators	No signal for any operator	Signal for all operators
England	4.6%	72.8%	0.2%	95.2%	6.0%	32.7%	0.5%	82.6%
Scotland	26.2%	41.7%	0.7%	91.9%	50.5%	4.9%	3.4%	69.8%
Northern Ireland	8%	56.5%	1.5%	81%	13.3%	16.7%	2.6%	62.9%
Wales	15.7%	52.8%	1.2%	87%	21.9%	11.49%	2.3%	58.4%
UK	12.7%	62.4%	0.4%	94.1%	22.9%	21%	0.9%	79.7%

[Source: Ofcom, Infrastructure Report 2013]

The SNP is likely to re-auction licences upon independence. If we look at rough rules of thumb regarding how much these licences are likely to raise at auction, we think that an upper bound is the per capita share of Ofcom's last auction, which was noteworthy in not being exclusively designed to yield maximum revenue. Of the total raised of £2.3 billion, Scotland's per capita share would be £200 million. The 2G and 3G licenses that sold for £22 billion in 2000, may also be re-auctioned, and Scotland's per capita share was £1.8 billion. In short, Scotland might raise as much as £2 billion from re-auctioned licences.

At the same time, a coverage obligation makes a spectrum band less valuable if it is more onerous than a commercial plan would be. In the 4G auction, O2's band was not materially cheaper than the others, as the obligation was not onerous. However, extending it in Scotland would likely increase the coverage cost, likely to the point where the spectrum is not worth much at all on a purely Scotland basis.

So what the MNOs would end up bidding for licences depends critically on coverage obligations given the challenging geography of Scotland for mobile communications. Since the White Paper states 99% as a likely target, that will heavily reduce the price they are willing to pay, bearing in mind their sunk investments in network infrastructure.

On fixed fibre broadband: "The Scottish Government is already building the foundation for world-class digital infrastructure in Scotland. We are making a significant investment in the Step Change programme which will see investment of over £410 million, from a range of funding sources, to make available fixed fibre broadband to 85 per cent of Scottish properties by the end of 2015 and around 95 per cent by the end of 2017. This will significantly enhance digital connectivity and is essential for bridging the digital divide in coverage that exists today between urban and rural areas. Under our proposals, this initiative will continue after independence."

Of course, unlike the MNOs, fixed-line telecommunications providers like BT or Virgin Media have no requirement to use spectrum. This suggests that their existence will be continuous before and after independence in Scotland. They will however be regulated by Scotcom, whose approach to regulation may differ from Ofcom's. In particular, we might expect Scotcom to focus a great deal on coverage in rural and remote locations.

Other known unknowns

If we look at the landscape of the UK media and telecoms sectors, the White Paper was silent on two relatively significant issues for the media which we have covered in detail over time.

The first is the impending regulation or self-regulation of the newspaper sector of the UK. There is no word on this matter in the White Paper.

The Scottish Government's rather cool response to the McCluskey Report on implementing Leveson's recommendations in Scotland suggest they will, like Westminster, tread carefully on this issue. One reason for its absence from the White Paper could be the desire to avoid antagonising editors ahead of the referendum debate, or to avoid the SNP being painted as draconian. Another could be that the Scottish Government simply has not arrived at a position. The McCluskey Report was an attempt to translate Leveson's proposed system of press regulation – which leans heavily on incentives that take effect through the courts in England and Wales – into a Scottish legal framework. McCluskey's solution involved an element of compulsion unacceptable to editors, but in an independent Scotland there would be no need to achieve fit with the solution accepted by Westminster.

Roughly speaking, we think the most likely outcome would be something like the Irish Press Council: a solution involving some element of statute, but not a large, powerful regulator, which would simply be unnecessary. The newspaper market in an independent Scotland would be smaller and with fewer competitors than the UK national market; the competition would not be as fierce; the likelihood of serious abuses would therefore be lower and the need for a powerful regulator less.

Another blank spot in the White Paper is the regime for media mergers, a special case of the mergers regime. While Scotland has pledged to regulate competition more effectively than is done by Westminster, it did not mention media mergers.

About Enders Analysis

Enders Analysis is a research and advisory firm based in London. We focus on the media, entertainment, mobile and fixed telecoms industries, with a special focus on new technologies and media, and we cover all sides of the market, from consumers and leading companies to regulation. For more information see www.endersanalysis.com. Contact us at info@endersanalysis.com.