

# Ofcom Content Sanctions Committee

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<b>Consideration of sanction against:</b>	<p>ITV Broadcasting Limited (“the Licensee”) in respect of each of its regional Channel 3 licences, namely:</p> <p>ITV Anglia ITV Border ITV Central ITV Granada ITV London (two licences) ITV Meridian ITV Tyne Tees ITV Wales and West ITV Westcountry ITV Yorkshire (collectively ‘the ITV plc licensees’)</p>
<b>For:</b>	<p>Breaches of Channel 3 licence conditions in respect of quotas for out of London production in 2006 and 2007.</p> <p>Condition 9 of the licences sets out the ‘out of London’ requirements; and paragraph 6 of Part 1 of the Annex to each of the Channel 3 regional licences (as varied) states that <i>“at least 50 per cent of expenditure on originated Network programmes in each calendar year shall be allocated to the production of programmes produced outside the M25 area”</i>.</p> <p>In 2006, 45.6 per cent of expenditure on originated Network programmes was allocated to the production of programmes produced outside the M25, against the requirement for at least 50 per cent;</p> <p>In 2007, 44.3 per cent of expenditure on originated Network programmes was allocated to the production of programmes produced outside the M25, against the requirement for at least 50 per cent.</p>
<b>Decision:</b>	<p>To impose a financial penalty in respect of each regional Channel 3 licence (11 in all) of <b>£20,000</b> (payable to HM Paymaster General) – a total of <b>£220,000</b>.</p>

## Summary

- 1.1 Under powers delegated from the Ofcom Board, the Ofcom Content Sanctions Committee (“the Committee”) has decided to impose a statutory sanction in respect of each Channel 3 regional licence held by ITV Broadcasting Limited<sup>1</sup>, controlled by ITV plc.
- 1.2 This is in light of the seriousness of their failure to ensure compliance with a requirement placed on each of the Channel 3 regional licences to ensure that "at least 50 per cent of expenditure on originated Network programmes in each calendar year shall be allocated to the production of programmes produced outside the M25 area." The licensees failed to meet the quota in either 2006 or 2007.
- 1.3 The breaches of licence conditions were found by Ofcom to have occurred in respect of all 15 Channel 3 regional licensed services. However, this adjudication concerns only the breaches by the 11 regional licensees within the ITV plc group (collectively referred to as ‘the ITV plc licensees’)<sup>2</sup>. Namely:

- ITV Anglia
- ITV Border
- ITV Central
- ITV Granada
- ITV London (two licences)
- ITV Meridian
- ITV Tyne Tees
- ITV Wales and West
- ITV Westcountry
- ITV Yorkshire

- 1.4 The ‘out of London’ requirements are set out under Condition 9 of the licences. Paragraph 6 of Part 1 of the Annex to each Channel 3 regional licence (as varied) states that "at least 50 per cent of expenditure on originated Network programmes in each calendar year shall be allocated to the production of programmes produced outside the M25 area".
- 1.5 The failure by Channel 3 regional licensees to fulfil the ‘out of London quotas’ in both 2006 and 2007 amounts to a breach of these conditions as follows:
- 1.6 (a) Quota for 2006  
  
The allocation of 45.6 per cent of expenditure on originated Network programmes to production outside the M25 represents a shortfall of 4.4 per cent against the requirement for at least 50 per cent;
- 1.7 (b) Quota for 2007

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<sup>1</sup> Since October 2008, the 11 ITV regional licences controlled by ITV plc have all been held by ITV Broadcasting Limited, a subsidiary of ITV plc.

<sup>2</sup> Ofcom has also conducted a separate sanctions process in respect of the licence breaches by the non-ITV plc owned regional licensees. The adjudication in respect of these breaches is being simultaneously published at [http://www.ofcom.org.uk/tv/obb/ocsc\\_adjud/itvjan09/nonitvplc.pdf](http://www.ofcom.org.uk/tv/obb/ocsc_adjud/itvjan09/nonitvplc.pdf)

The allocation of 44.3 per cent of expenditure on originated Network programmes to production outside the M25 represents a shortfall of 5.7 per cent against the requirement for at least 50 per cent.

- 1.8 Returns submitted by ITV Network in both 2006 and 2007 had originally indicated full compliance with the requirement that 50 per cent of original programme production by value should be 'out of London'. However, following a request from Ofcom to check the returns associated with some specific programmes, a subsequent audit by the Network revealed that a number of programmes had been misallocated as 'out of London' productions. As a result of adjusting the incorrect classifications, it became apparent that, although licensees had achieved the required quotas for out of London production by *volume* in both 2006 and 2007, they had failed to achieve the required quotas by expenditure. The revised figures and the consequent shortfalls against quota were reported to Ofcom immediately.
- 1.9 Ofcom concluded that the failures to meet 'out of London' production quotas in both 2006 and 2007 amounted to breaches of the Channel 3 regional licences controlled by ITV plc, as outlined above. In Ofcom's view, the breaches were sufficiently serious that they should be referred to the Committee for consideration of statutory sanctions.
- 1.10 ITV plc made both written and oral representations on behalf of the licensee in each case, all of which the Committee took into account. In its representations, ITV plc acknowledged the breaches and made a number of arguments in mitigation. It said the level of 'out of London' quota; the speed at which the quota increase to 50 per cent had been introduced; and the new definition of 'out of London' production applied by Ofcom were all mitigating factors. These needed to be considered within the context of a market structure heavily weighted in favour of production in London. The quota was also difficult to meet in practice as decisions made during the course of production of a programme could affect whether that programme qualified as having been made out of London. ITV had believed until early 2008 that the quota had in fact been met in 2006 and 2007. The fact of the quota breaches had been revealed by ITV Network's own internal audit and communicated to Ofcom immediately. Compliance arrangements had since been considerably strengthened.
- 1.11 In any event, if a decision to impose a sanction was taken, ITV plc argued that all licensees should be treated equally since all share equal responsibility for the quota breaches.
- 1.12 After considering all the evidence and all the representations made to it, the Committee decided that the breaches of licence conditions by the ITV plc licensees were sufficiently serious to attract a financial penalty.
- 1.13 Ofcom considers the fulfilment of all quota requirements as a very important aspect of the regulation of public service broadcasting. The quotas are in place to support the interests of citizens and consumers, in this case by ensuring that television production is not over-concentrated in the capital; and that the schedules of the PSB channels incorporate a diverse range of producers and editorial voices.
- 1.14 In considering the seriousness of this licence breach, the Committee took into account the effect of the breach. Namely, that a lower value of production,

meeting the Ofcom criteria for Out of London production, had been commissioned by ITV and transmitted in 2006 and 2007 than required by the terms of ITV plc's regional licences. The effect of this lower level of commissioning was to reduce the activity of the production sector outside London and thus potentially to damage it. It was also to decrease the diversity of what viewers watched on ITV1.

- 1.15 The size of the shortfall was also significant and while the Committee accepted that there was no evidence that the breach was deliberate, the breach was clearly repeated, as the ITV plc licensees had failed to meet the Out of London quota in relation to each of their respective licences in both 2006 and 2007, and had done so despite a clear warning from Ofcom in early 2006 that "any failure to meet the 2006 target would be viewed seriously by Ofcom".
- 1.16 The new definition for out of London production had been published by Ofcom in March 2004<sup>3</sup> with the stated intention that it should apply with effect from the beginning of 2005, though Ofcom had subsequently agreed to ITV's request that 2005 be treated as a transitional year and that the higher quota and new definition be applied with effect from the start of 2006. ITV plc should therefore have been aware of and considering the implications of the new definition from early in 2004.
- 1.17 The Committee also considered the weaknesses acknowledged by ITV plc in the ITV Network compliance systems for tracking out of London production. Until 2008, when the failure to achieve the 2006 and 2007 quotas by value had become apparent, it appeared that little thought had been given to the compliance system implications of the way out of London production was defined.
- 1.18 Furthermore, despite the acknowledged challenge of achieving the quota in 2006 and thereafter, ITV plc had been unable to show any evidence of measures it had taken at that stage to ensure that the quota was achieved. It had argued that it would be normal practice to deal with this issue in informal meetings between the ITV Network Director and his subordinates, but no evidence had been presented that ITV plc had taken any steps to ensure that this issue was addressed by the Network. Similarly, there was no evidence of targeted activity by ITV Network to ensure that the quota was achieved in 2006 and thereafter, despite the letter sent from the Chairman of the Content Board to Simon Shaps in May 2006.
- 1.19 Having regard to the seriousness of the breaches and to Ofcom's penalty Guidelines, and having given careful consideration to the written and oral representations made, the Committee decided it was appropriate and proportionate in the circumstances to impose a financial penalty on the Licensee in respect of each of the regional Channel 3 licences it holds, of **£20,000** (payable to HM Paymaster General) (a total of **£220,000** in all).

## Background

- 2.1 ITV/Channel 3 is the UK's most popular commercial PSB TV channel in terms of audience share. However, the single channel comprises a network

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<sup>3</sup> [http://www.ofcom.org.uk/tv/ifi/guidance/reg\\_prod/](http://www.ofcom.org.uk/tv/ifi/guidance/reg_prod/)

of 15 separate regional licences held by 4 different licence holders. Eleven of these licences are held by ITV Broadcasting Ltd and controlled by ITV plc (as outlined above). The remaining four licences are held independently by Channel Television Ltd; stv (two licences – stv central Ltd and stv north Ltd); and by UTV Ltd.

- 2.2 The channel's network output is administered at the ITV Network Centre, (the term commonly used to describe the entity comprising ITV Network Limited and incorporating the Network Directorate) under Networking Arrangements which are required to be in place between all Channel 3 regional licensees in accordance with the relevant provisions of the Communications Act (Sections 290 to 294 and Schedule 11 of the Act). These establish the contractual relationships between the regional licensees making up the ITV Network, with the aim of providing a national television service capable of competing effectively with other broadcasters in the UK.
- 2.3 The Networking Arrangements, operating within the regulatory framework, dictate that ITV Council – comprising representatives of all the licensees - has responsibility for broadcasting and programme strategy. This body meets at least twice a year. Otherwise, the ITV Network Centre acts as an agent on behalf of all the licensees, to commission and manage the Network schedule. It is also responsible under the arrangements for reporting to Ofcom delivery against PSB quotas that apply to Network programming. All licensees are members of ITV Network Ltd.
- 2.4 Within the ITV Network Centre, specific responsibility for the task of reporting to Ofcom, delivery against PSB quotas, rests with the Network Director, a position held through the relevant period, by an employee of the Granada Media Group, (owned by ITV plc). Statutory responsibility for compliance, secured under the terms and conditions of the Channel 3 regional licences, rests with the individual licensees.

## **Legal Framework**

- 3.1 Section 286 (1) of the Communications Act allows Ofcom to set licence conditions to ensure that a suitable proportion of Channel 3 Network programmes made in the United Kingdom is produced outside the M25 area. The Act refers to proportions of both volume and expenditure. These have become known as the 'out of London' quotas. They apply equally to all 15 individual regional licences under which the Channel 3 Network operates.
- 3.2 Prior to 2005, the quotas for Channel 3 licensees were set at 33 per cent by volume and 40 per cent by expenditure. However, in 2005 these were increased to 50 per cent of both volume and spend, in line with conclusions reached in Ofcom's Public Service Broadcasting Review of 2004. At about the same time, a tighter definition of 'out of London' was also introduced. The definitions had been consulted on and decided in a statement published by Ofcom in March 2004<sup>4</sup>. At that point it was intended, as set out in the statement, that these definitions be introduced with effect from January 2005.
- 3.3 Ofcom's powers to impose statutory sanctions come from the Communications Act 2003 ("the Act") and the Broadcasting Acts 1990 and

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<sup>4</sup> [http://www.ofcom.org.uk/tv/ifi/guidance/reg\\_prod/](http://www.ofcom.org.uk/tv/ifi/guidance/reg_prod/)

1996 (as amended). If it deems it necessary, the Committee may impose a range of sanctions as set out below. The available sanctions relevant to this particular case were:

- a direction to broadcast a statement of Ofcom's finding;
- imposition of a financial penalty; and/or
- revocation of the licence.

3.4 The imposition of a statutory sanction against a broadcaster is a serious matter. The Committee may, following due process, impose a statutory sanction if it believes that a broadcaster has repeatedly, deliberately or seriously breached the terms of its licence conditions or Ofcom's statutory Codes. Ofcom will not impose a sanction against any broadcaster before it has been given a reasonable opportunity to make written representations (and in the case of more serious sanctions such as fines and/or revocation of licence an opportunity to make oral representations) about whether a sanction should be imposed and if so, what type and at what level. Ofcom will consider those representations and take proper account of them.

### **Ofcom's investigation and ITV plc's responses**

4.1 In both 2006 and in 2007, both on-going returns to Ofcom and ITV Network's self assessment review of PSB output suggested there had been full compliance with the out of London quota for those years. However, as a result of an Ofcom audit and a subsequent request for ITV Network to check some specific returns, it became apparent that a number of programmes had been misclassified as 'out of London'.

4.2 ITV Network then conducted its own internal audit, and a number of additional misallocations were revealed. As a result of adjusting the incorrect classifications, it became apparent that, although licensees had achieved the required quotas for out of London production by volume in both 2006 and 2007, they had failed to achieve the required quotas by expenditure:

- in 2006, 45.6 per cent of expenditure on originated Network programmes was allocated to the production of programmes produced outside the M25, against the requirement for at least 50 per cent;
- in 2007, 44.3 per cent of expenditure on originated Network programmes was allocated to the production of programmes produced outside the M25, against the requirement for at least 50 per cent.

4.3 Ofcom wrote separately to ITV plc in respect of the licences within its control and to each of the non-ITV plc Channel 3 licensees asking them to respond to the apparent breaches by the regional ITV licensees of licence conditions. The letters asked in particular whether the licensees agreed with Ofcom's initial conclusions, and invited each of the licence holders to make any relevant representations.

4.4 In its response, ITV plc accepted that the 50 per cent quotas for expenditure on out of London production were not met in either 2006 or 2007, and agreed with Ofcom's conclusions on the magnitude of the under-delivery (a shortfall of 4.4 per cent in 2006 and 5.7 per cent in 2007). The letter acknowledged

that the broadcaster's internal analysis had revealed "some weaknesses in ITV's internal processes in relation to compliance with the Out of London quota".

- 4.5 However, a number of representations in mitigation were made including:
- The breaches had been revealed by ITV Network's own internal audit and had been communicated to Ofcom immediately;
  - Compliance with the quota depends to a significant extent on the detail of where spend is incurred and where production staff are employed or freelancers live. As a result there is an ever present risk that short-term decisions made to keep a production on track can affect compliance in ways which only become clear ex post.
  - Quota requirements are complex to apply in practice, and compliance was hindered by a "lack of clear understanding" between Ofcom and ITV.
  - ITV had since taken significant steps to improve its compliance processes to ensure that data is accurate, and that there is clarity in internal accountability.
- 4.6 ITV plc also made a number of representations about the heavy burden that a 50 per cent production quota placed on the company including:
- The company said the quota was out of step with that applied to the BBC and other PSBs, and did not reflect economic realities. Accordingly, it should be reduced.
  - There were very real difficulties in complying with the quota because of the lack of available production talent, facilities, and producers outside London, especially for drama and entertainment programmes. For example, there were only five key drama production bases outside London, and the number of drama proposals from these suppliers compared to other suppliers inside the M25 did not merit channelling one third of ITV's discretionary drama budget in this way simply to meet the quota.
  - The Statement of Principles relating to the Channel 3 Networking Arrangements states that "all decisions to commission.... a particular programme will be based on the merits of the programme with a view to ensuring the most commercially attractive schedule." This conflicts with the requirement to fulfil the out of London quota.
  - ITV plc also said the definition of 'out of London' was too narrow, and did not give due credit to ITV's contribution to either on-screen portrayal of different parts of the UK or the company's regional economic investment.

### **Ofcom's decision that the ITV plc licensees were in breach of their licence conditions**

- 5.1 Having carefully considered the representations made by ITV plc, the Ofcom Executive ("the Executive") recorded on 2 June 2008 that:

- In 2006, 45.6 per cent of expenditure on originated Network programmes was allocated to the production of programmes produced outside the M25, against the requirement for at least 50 per cent;
- In 2007, 44.3 per cent of expenditure on originated Network programmes was allocated to the production of programmes produced outside the M25, against the requirement for at least 50 per cent.

5.2 This amounted to licence breaches as follows:

- For 2006, breach of licence condition 9 and the requirement in para 6, Part 1 of the Annex to each of the Channel 3 regional licences (as varied) which states that "at least 50 per cent of expenditure on originated Network programmes in each calendar year shall be allocated to the production of programmes produced outside the M25 area";
- For 2007, breach of licence condition 9 and the requirement in para 6, Part 1 of the Annex to each of the Channel 3 regional licences (as varied) which states that "at least 50 per cent of expenditure on originated Network programmes in each calendar year shall be allocated to the production of programmes produced outside the M25 area".

### **Referral to the Content Sanctions Committee**

6.1 Taking all the circumstances into account, and after consideration of the Licensee's representations, the Executive informed the broadcaster that it considered the breaches of licence conditions were sufficiently serious for it to recommend that the case be referred to the Committee for the consideration of a statutory sanction.

6.2 The Committee - having reviewed the Executive's decision to refer the breaches - accepted that the case was sufficiently serious that it should be considered for sanction. Accordingly, ITV plc was invited to attend an oral hearing before the Committee on behalf of the 11 regional licensees it controlled.

### **ITV plc's written representations on the imposition of a sanction**

6.3 In further correspondence dated 27 July, 21 August, and 13 October 2008 ITV plc had expressed disappointment at the decision to initiate the sanctions process. It pointed out that measures had been taken to improve the compliance process and that firm undertakings had been given to ensure compliance with the quota in 2008. It also expanded on arguments made in mitigation - and restated the view that the quota level and the definition of out of London was unfair and presented too demanding a target for ITV.

6.4 Additional points raised included:

- Although Ofcom's stated intention in raising the target to 50 per cent by both volume and spend had been to 'lock-in' ITV's existing levels of out of London expenditure, the imposition of tighter definitions for out

of London production had - in fact – effectively increased the level of commitment required to fulfil the quota by a “seismic” amount.

- ITV plc had believed after the year end in both 2006 and 2007 that it had complied with the quota requirements. Once concerns had been raised, a thorough audit had been conducted which went well beyond what Ofcom had asked. The information thrown up by the re-analysis had been openly and honestly reported to Ofcom as soon as it became available. It would be “perverse” for licensees to be “punished” more severely as a result of this openness.
- Full account should be taken of all mitigating circumstances. In particular, ITV plc said that structural market and economic factors had made it extremely difficult to meet the increased out of London quota after its “significant and more or less immediate” increase in 2005.
- ITV plc had warned Ofcom earlier of the difficulty it faced in achieving the revised quota. It said this should militate strongly against the imposition of a statutory sanction.
- ITV plc highlighted the contrast with requirements now being placed on the BBC. The Corporation is not committed to achieving a 50 per cent out of London quota until 2016, at an average increase of 2 per cent a year. In contrast, the revision for ITV plc in 2005 required an increase of 7 per cent in a single year. There had been no increase in BBC out of London production in 2006 or 2007. As a result, there was no additional demand which could have helped sustain a broader Network production base outside the capital.
- ITV plc argued that all the Channel 3 licensees (including the non-ITV plc companies) shared equal responsibility for the breaches and should be treated equally. Licence obligations are applied equally on all Channel 3 licensees, and all licensees participate in the ITV Network, which acts on behalf of all. There is no case for ITV plc licensees to be treated differently to any of the non-ITV plc licensees.

## **Sanctions Hearing**

- 7.1 The Committee held an oral hearing to consider the sanctions case on 4 December 2008. At this meeting ITV plc was given the opportunity to make oral representations to the Committee before it decided whether the breaches of licence conditions warranted the imposition of a statutory sanction, and if so, at what level. The Committee was addressed on behalf of the Licensee by Magnus Brooke (Director of Regulatory Affairs) and Andrew Garard (General Counsel).
- 7.2 ITV plc said it wished to make representations on two main issues. Firstly, that a fine was not justified in the circumstances and secondly, that there was no case for treating the Licensee in any different way to the non-ITV plc licensees, since all shared equal responsibility for the breaches.
- 7.3 In addressing the issue of a fine, ITV plc reiterated the arguments made in its written submissions and said the level of ‘out of London’ quota; the speed at which the increase to 50 per cent had been introduced; and the new

definitions applied by Ofcom were all mitigating factors. These needed to be considered within the context of a market structure heavily weighted in favour of production in London. Although ITV plc accepted the logic and desirability of spreading production around the UK, it had been asked to buck the natural economic logic of the existing market too quickly.

- 7.4 The difficulties were particularly apparent for drama and entertainment production, which accounted for 75 per cent of ITV's programme budget. Dispersing production in drama and entertainment across the UK necessarily imposed significant costs, and potentially could even have an impact on quality too. For example, the number and quality of programme proposals submitted to ITV by drama producers outside London had not merited placing an even larger proportion of ITV1's discretionary drama budget with these producers.
- 7.5 A significant amount of ITV1's regular drama series were already produced outside the capital. A significant amount of 'discretionary' drama was also set in - and portrayed - the UK regions, but did not technically qualify as 'out of London' under the Ofcom definitions. There was also a contradiction between the requirements for 'out of London' production and the obligation to commission programmes on merit, as set out in the legally binding Networking Agreements.
- 7.6 ITV plc contested the suggestion that the Network should have begun preparing for a new quota in 2004 since the quota was only consulted on in that year and the consultation clearly implied that production levels outside London need not change, since an increase to 50% would simply "lock in current levels of production for ITV1". It was not until well into 2005 that Ofcom had confirmed both the increase to 50% and the far stricter out of London criteria. Rather than "lock-in" current levels the proposal now very significantly and unexpectedly increased the substantive obligations on Channel 3. This increase was also contrary to Ofcom's recognition in the same PSB Review that ITV's PSB obligations would need to reduce, given the "inexorable decline in the historic analogue model".
- 7.7 The licensee contrasted the demands being made on the regional Channel 3 licensees with the much slower rate of quota increase which the BBC had accepted. With no additional demand from the BBC in 2006 or 2007 to encourage and sustain high budget Network production outside London it was unrealistic to expect ITV to suddenly and single-handedly buck market and ITV-specific economic trends which both ITV and Ofcom had identified. ITV plc said it would be unfair for significant account not to be taken of the difficulties which the Channel 3 licensees faced in meeting this quota.
- 7.8 It was significant that the new definitions of 'out of London' imposed by Ofcom applied – in effect – on an "all or nothing" basis to productions. First, this meant that even programmes which incurred a very significant level of expenditure outside the capital often ended up counting as London productions. Secondly, it also took no account of portrayal on screen and therefore risked distorting decision-making expenditure in a way that is contrary to the interests of viewers. Thirdly, the quotas took no account of news and non-news programming produced in the regions. Fourthly, productions which begin and are commissioned as out of London can become in-London productions very easily as a result of mid-production changes – which the Network in many cases may not be aware of until

programme delivery. It would be uneconomic to build in vast over-delivery to buffer the Network against risk of under-delivery.

- 7.9 ITV plc considered a fine was not appropriate because, despite these factors, the failure to meet the 'out of London' quota had not been deliberate, conscious or reckless. ITV plc had reasonably believed the requirements had been met in both 2006 and 2007 and the scale of the shortfall was only revealed in retrospect after an internal ITV Network investigation as a result of questions being asked by Ofcom. The investigation had gone well beyond the limited audit that Ofcom had requested – and the shortfalls were openly and honestly conveyed, including revealing other programmes that had been misclassified, which had not been questioned by Ofcom. It would be perverse for ITV plc to be punished more seriously as a result of its openness – to do so would be to encourage a lack of candour between the regulator and the regulated and would not be in the public interest.
- 7.10 It was also significant that steps had been immediately introduced to ensure compliance was achieved in future: the ITV Network, reinforced by the Executive Chairman of ITV plc, had made it very clear that the Channel 3 licensees would meet the quota in 2008, and the Network Centre and ITV plc had made changes to internal compliance systems – to improve the quality of source data and to ensure clarity in terms of responsibility and accountability for compliance with the quota. In view of the action already taken by ITV plc it was not justified to impose fines on its Licensee in order to ensure future compliance.
- 7.11 Turning to the possible treatment of non-ITV plc licensees in a different way from the ITV plc licensee itself, ITV plc said this could not be justified. Under the legislation and the Networking Arrangements, all the Channel 3 licensees were members of the Network and bore equal responsibility. For Ofcom to imply that ITV plc had greater influence and bore greater responsibility for commissioning or compliance would amount to saying that ITV plc is in breach of the Networking Arrangements, since ITV plc would be exercising control over commissioning rather than the ITV Network. There was no compelling evidence to support that conclusion and ITV plc was not guilty in that regard. The position was different with regard to programme compliance where independent producers had a choice of compliance licensee. But in this case, the fact that ITV plc provided assistance to the Network in analysing and reporting information, did not in itself support the conclusion that as a result the ITV plc licensee is more culpable than the non-consolidated licensees. Firstly, because the information provided to the Network suggested that Channel 3 licensees would comply with the quota in 2006 and 2007 and therefore access to the information would have made no difference in substance. Secondly, the non-ITV plc licensees were under identical licence obligations to the Licensee and were perfectly free to ask for information and to check whether the systems and procedures were effective. To seek to distinguish between the ITV plc licensees and the non-ITV plc licensees would be to conclude that the Networking arrangements are not fit for purpose.
- 7.12 ITV plc was questioned about why the levels of 'out of London' production had fallen in 2005 from the previous year even though 2005 was supposed to represent a transition to the higher quota. It was also challenged over the action it had taken after it had received a letter from Ofcom in May 2006

clearly indicating the importance Ofcom ascribed to meeting the quotas and warning of the possible consequences of non-compliance with the quotas.

- 7.13 ITV plc responded by saying the programmes transmitted in 2005 had been commissioned in earlier years, at a time when a lower quota had applied. The ITV plc controlled licensees and ITV plc had been aware of the challenge of meeting the new quotas but there had been little concern about compliance in 2006 because the data suggested the quota was going to be met. ITV plc said the quotas did not work in the interests of viewers because they did not deliver the desired outcome – namely portrayal of the UK’s regions. Many programmes that did achieve that objective did not actually qualify as ‘out of London’.
- 7.14 The Committee asked ITV to describe the actions taken by ITV Network and ITV plc, after receipt of the May 2006 letter from the Chairman of the Content Board to Simon Shaps, who was at that time the ITV Network Director and responsible for all the commissioning of content for the Network on ITV1. The Committee asked what action had been taken to ensure that the quota was met in 2006 and beyond? In response ITV plc said that the matter would have been addressed at the Network Centre by the Network Director and his subordinates as part of their informal regular management meetings and that ITV plc had placed reliance on this action. The ITV representatives present at the sanctions hearing were not aware of any correspondence on file on the matter or of any discussion of the matter at the ITV Council. The issue of compliance with the quota had been raised at an Executive Board meeting of ITV plc in late 2006, attended by Simon Shaps, who in addition to being ITV Network Director was also ITV plc’s Director of Television and a member of ITV plc’s Executive Board, where it was reported that ITV would “scrape over” the quota in 2006 by value and volume.
- 7.15 ITV plc rejected suggestions that it had a greater responsibility than the non-ITV plc licensees because it acted as the agent for processing the data. Compliance remained a Network responsibility and all licensees had equal responsibility as members of the Network. On this basis ITV plc was not clear why it was not up to non-ITV plc licensees to ask for information and to ask the Network whether they were going to be able to comply with their licences, as opposed to closing their eyes to any issue of compliance and not asking any questions. The Networking arrangements prohibited ITV plc having a greater power or control over commissioning and compliance than the non-ITV plc licensees in the way that Ofcom had alleged.
- 7.16 The Committee asked what processes had been in place prior to the recent changes to ensure compliance with the out of London quota and whether there had been a lack of systems or an audit process. In response ITV plc said that accurate reporting relied on accurate data collection, and there had been no hint of problems in that regard. ITV Network had collected data from producers on whether their programmes qualified as having been produced outside London and had passed that data on to ITV plc which analysed and reported on the data. Responsibility for commissioning and compliance lay with ITV Network and the commissioner liaising with producers is responsible for gathering the raw information about whether productions comply and therefore where the spend has been incurred, where the employees were and so on. That data then goes into the ITV plc system. In the circumstances, there had been no cause for alarm. Only in hindsight was it now accepted that there had been some weaknesses in the system – namely

a lack of attention to small details which could have a marked effect on allocations to London or out of London production.

- 7.17 ITV plc added that the collation of actual raw information about whether productions qualified as having been made out of London or not, was a process which end-to-end effectively had to be run by the Network because the Network is legally responsible under the Networking Arrangements. With the benefit of hindsight it appeared that not enough questions had been asked by ITV Network. Programmes could flip during the course of production from qualifying as made out of London to qualifying as being made in London. It appeared that there had not been enough attention to detail in the commissioning process and on seeing the process through to the end and it appeared ITV Network had not had as tight a grip on Out of London production as they probably should have had. There had been significant reliance on independent producers.
- 7.18 ITV Network had now made much greater efforts to ensure that producers, (including both independents and ITV Productions) absolutely understood what the criteria were and that they applied them systematically in relation to where production staff live, where the budget was being spent etc, in order to give the Network sufficient assurance that productions were genuinely out of London pursuant to Ofcom's tests. To this end, new guidance had been issued for independents as to what the out of London test actually requires.
- 7.19 In summing up, ITV plc stressed that it had genuinely believed the quota had been met in both 2006 and 2007. However, there had been insufficient rigour in the system, and the retrospective audit had revealed a shortfall. Systems had now been tightened and ITV had given assurances that there would be full compliance in 2008. A fine was not justified as a means to ensure future behaviour and compliance with the quota.

### **Decision by the Committee**

- 8.1 The Committee may impose a range of sanctions which may be a direction to broadcast Ofcom's finding; a financial penalty; and/or revocation of the licence(s). In this case, having considered all the evidence and representations before it, the Committee decided that for the reasons set out below, it was appropriate to impose a financial penalty on the ITV plc licensee in respect of each of its Channel 3 services.
- 8.2 In deciding on an appropriate and proportionate level of financial penalty the Committee had regard to Ofcom's Penalty Guidelines.<sup>5</sup>

### **The seriousness of the breaches**

- 8.3 Licence condition 9 and the requirement in para 6, Part 1 of the Annex to each of the Channel 3 regional licences (as varied) states that "at least 50 per cent of expenditure on originated Network programmes in each calendar year shall be allocated to the production of programmes produced outside the M25 area". Having taken account of all the evidence, the Committee

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<sup>5</sup> Ofcom's Penalty Guidelines are available at <http://www.ofcom.org.uk/about/accoun/pg/>. Section 392 of the Communications Act 2003 requires Ofcom to prepare and publish a statement containing guidelines it proposes to follow in determining the amount of any penalties imposed by Ofcom, which Ofcom must have regard to in setting any penalty.

considered that the breaches of this licence condition were both serious and repeated for the reasons set out at Paragraphs 8.4 to 8.15 below.

- 8.4 It is a general principle of regulation that licensees should comply with the terms of their licences. Compliance with production quotas in general and the out of London quota specifically is a key element of the obligations placed on the public service broadcasters. The Communications Act also places on Ofcom a duty to set conditions to ensure that a significant proportion of Networked programmes are made outside London. In failing to meet the out of London quota the Licensee had clearly breached this term in respect of each of its Channel 3 licences.
- 8.5 The 2003 Communications Act had made significant changes in the way that the commercial public service broadcasters were regulated and moved away from a system of multiple genre based quotas towards a greater degree of self-regulation by broadcasters. However in doing so, Parliament had clearly signalled the importance of promoting the production of programmes outside London by leaving this as one of the relatively few remaining Tier 2 quotas. These quotas are in place to support the interests of citizens and consumers, in this case by ensuring that television production is not over concentrated in the capital and that the PSB channels' schedules include a plurality and diversity of producers and editorial voices.
- 8.6 In considering the seriousness of this licence breach, the Committee took into account the effect of the breach. Namely, that a lower value of production, meeting the Ofcom criteria for Out of London production, had been commissioned by ITV and transmitted in 2006 and 2007 than required by the terms of ITV plc's regional licences. The effect of this lower level of commissioning was to reduce the activity of the production sector outside London and thus potentially to damage it. It was also to decrease the diversity of what viewers watched on ITV1.
- 8.7 The size of the shortfall was also significant and the fact that the shortfall had increased over time. A shortfall of 4.4 per cent in 2006 and 5.7 per cent in 2007 relative to a quota of 50 per cent by value, represents an under achievement of the quota by nearly 9 per cent in 2006 and by just over 11 per cent in 2007.
- 8.8 The Committee accepted that there was no evidence that the breach was deliberate. However, the breach was clearly repeated, as the ITV plc licensees had failed to meet the Out of London quota in relation to each of their respective licences in both 2006 and 2007, and had done so despite a clear warning from Ofcom in early 2006 that "any failure to meet the 2006 target would be viewed seriously by Ofcom".
- 8.9 The Committee also considered ITV plc's arguments that the nature of the quota, the level of the quota and the speed of increase in the level of the quota, having moved from 33 per cent by volume and 40 per cent by expenditure in 2004 to 50 per cent by both volume and expenditure in 2005, were in themselves to be considered as mitigating factors in the consideration of ITV's licence breach.
- 8.10 The Committee rejected this argument because it had been made very clear to ITV plc throughout the process of the PSB Review and subsequent correspondence that Ofcom regarded the level of out of London production

on ITV1 as important and compliance with the quotas as a serious matter. Moreover it was an important principle of regulation that licensees adhere to their licence conditions and meet their licence obligations.

- 8.11 The Committee also considered the fact that the new definition for out of London production was published by Ofcom in March 2004 with the stated intention that it should apply with effect from the beginning of 2005, though Ofcom had subsequently agreed to ITV plc's request that 2005 be treated as a transitional year and to apply the definition with effect from the start of 2006. ITV plc should therefore have been aware of and considering the implications of the new definition from early in 2004.
- 8.12 In consequence, the Committee did not accept ITV plc's argument that the difficulty of achieving the quota and the timing of the quota increase were to be considered as factors militating against a sanction being imposed for the licence breaches.
- 8.13 The Committee also considered the weaknesses acknowledged by ITV plc in the ITV Network compliance systems for tracking out of London production. Until 2008, when the failure to achieve the 2006 and 2007 quotas by value had become apparent, it appeared that little thought had been given to the compliance system implications of the way out of London production was defined.
- 8.14 In considering the responsibility and culpability of the individual licensees owned by ITV plc at the time that the breaches occurred, the Committee imputed the same level of knowledge and culpability to each of the ITV plc owned licensees. There had been correspondence between ITV plc's then Director of Regulatory Affairs and Ofcom in 2005 and 2006 which had discussed the interpretation of and the delivery of the out of London quota. ITV plc had acknowledged that it knew from early 2005 onwards that it would be challenging to meet the quota in 2006 and thereafter and the issue of whether ITV1 would achieve the quota in 2006 had been on the agenda of the Executive Board of ITV plc in late 2006.
- 8.15 However, despite the acknowledged challenge of achieving the quota in 2006 and thereafter, ITV plc had been unable to show any evidence of measures it had taken at that stage to ensure that the quota was achieved. It had argued that it would be normal practice to deal with this issue in informal meetings between the ITV Network Director and his subordinates, but no evidence had been presented that ITV plc had taken any steps to ensure that this issue was addressed by the Network. Similarly, there was no evidence of targeted activity by ITV Network to ensure that the quota was achieved in 2006 and thereafter, despite the letter sent from the Chairman of the Content Board to Simon Shaps in May 2006.
- 8.16 The Committee was of the view that due to the serious and repeated nature of the breaches and the resulting harm caused to the out-of-London production sector and to the quality and diversity of the ITV1 Network schedule watched by viewers, the imposition of a financial penalty on the licensee in respect of each of its regional Channel 3 licences, was warranted.

## **Precedent**

- 8.17 In considering the appropriate level of financial penalty the Committee was aware that there were no previous precedents for sanctions cases dealing with the failure to achieve a Tier 2 quota and the resulting breach of a licence term. Previous sanctions cases dealt with by the Committee had related to breaches of the Broadcasting Code by licensees. Nor were there any previous sanctions cases where there had been consideration of the level of the financial penalty to be imposed on all the individual members of the regional ITV Network for a breach of a Network quota.
- 8.18 Recent cases in which a very substantial penalty had been imposed on an individual ITV licensee had related to breaches of the Broadcasting Code causing direct and significant consumer harm and a clear breach of the viewers' trust. Such factors are not relevant to this case.

### **Incentive**

- 8.19 In considering the level of the financial penalty the Committee took into account that ITV plc had believed that it had met the out of London quota in both 2006 and 2007 and that the failure to achieve the quota had not resulted in any direct financial benefit to ITV plc. However, the Committee was mindful of the importance of licensees adhering to the terms of their licences and took the view that a financial penalty would provide an appropriate incentive to ensure compliance with licence terms and Tier 2 quotas in the future.
- 8.20 The Committee considered that the 'starting figure' for any penalty, should be sufficient to act as a significant incentive to discourage further quota breaches. In this the Committee took into account that while the individual regional licences owned by ITV plc are of differing sizes, the Licensee, as holder of 11 ITV regional licences has significant resources and revenue. The quota breach had also been at Network level rather than an individual breach attached to a single licence; thus the incentive effect would operate both at the level of the individual licence and for ITV plc overall. The Committee considered that the incentive impact of a penalty could be achieved without imposing such a large financial sanction as could in itself damage viewers' interests.
- 8.21 Taking all these factors into account the Committee considered that it would be proportionate for the starting figure for any financial penalty imposed in respect of each regional licensee owned by ITV plc to be modest. In considering this, the Committee took into account that the maximum penalty that could be imposed on each of the regional licensees is 5 per cent of its qualifying revenue.
- 8.22 The Committee also took into account the position of the non-ITV plc licensees (who made separate representations at a subsequent hearing relating to the same breaches under their licences), and considered that the 'starting figure' for the penalty imposed on each ITV plc owned regional licensee should be higher than the 'starting figure' for any penalty that the Committee decided to impose on each licensee in the separate cases against the non-ITV plc licensees relating to the same licence breaches.

### **Other specific factors**

- 8.23 The Committee considered whether there were factors which differentiated the ITV plc owned licences from those held by stv, UTV and Channel Television, against whom separate sanctions cases in respect of the same licence breaches were in progress. In this connection the Committee noted that ITV plc's Broadcasting Resources unit had provided services to ITV Network in holding and analysing data which was relevant to compliance with the quota on the composition of the ITV Network schedule and in preparing reports for ITV Network and Ofcom - including tracking and forecasting the value and volume of Out of London programmes within the Network schedule. The Committee also noted that ITV Productions, owned by ITV plc, was the largest supplier to ITV1 and that ITV plc therefore had information available to it on the programmes commissioned from ITV Productions which was not available to the other licensees.
- 8.24 The Committee further noted that at the time when the May 2006 letter was sent by Ofcom's Chairman of the Content Board, its recipient, Simon Shaps, who was employed by Granada Media Group Limited, was both the Network Director of ITV Network and the Director of Television of ITV plc and a member of ITV plc's Executive Board. Despite this dual role ITV plc in its evidence had suggested that Ofcom had no compelling evidence on which to base a conclusion that the ITV plc licensees should be treated differently to the non-ITV plc licensees. However, in the view of the Committee, this dual role appeared to provide a further clear distinction between ITV plc's position and that of the other licensees.
- 8.25 The Committee acknowledged that the initial letter from the Chairman of the Content Board to ITV's Network Director had not been copied to the other licensees and that the correspondence relating to the out of London quota in 2005 had been with ITV plc's then Director of Regulatory Affairs.
- 8.26 ITV plc had acknowledged that adequate compliance systems were not in place in 2006 and 2007 and that ITV Network had not had as tight a grip on whether particular programme commissions initially qualified and continued to qualify as out of London produced as they should have done. This was despite the fact that the definition of out of London production had been published by Ofcom in early 2004 and (at that time) had been intended to come into operation with effect from the start of 2005.
- 8.27 ITV plc had recognised that there had been insufficient attention to detail and that there was a need for compliance procedures to be more systematic than they had previously been. In particular there was no process in place when programmes were commissioned as out of London productions, to check during pre-production and during production itself that the programme continued to qualify as out of London produced. ITV plc acknowledged that too much reliance had been placed on the independent producer and procedures had now been tightened up for producers' reporting on the out of London quotas.
- 8.28 The Committee also considered the arguments made by ITV plc as to the difficulty in achieving the quota and considered the fact that Ofcom has recently, in its second review of Public Service Broadcasting, consulted on a potential reduction in the ITV Network out of London quota from 50 per cent by volume and value to 35 per cent by volume and value with effect from 2009. The Committee considered that this proposed change in the out of London quota was not a reflection of any reduction in the importance of the

quota; rather a recognition that the value of the regional ITV companies' PSB licences is diminishing with the approach of digital switchover and accordingly, it is proposed that the burden of regulatory obligations placed on the licensees also needs to diminish.

### **Financial gain**

8.29 The Committee noted that while there might be some financial advantage to ITV Network and ITV plc in being subject to a reduced quota, the licensees had believed until early 2008 that the 50 per cent quota by volume and value had been met in 2006 and 2007. There was no evidence that the Licensee gained financially from these breaches of the Code.

### **Factors tending to increase the level of penalty**

8.30 The Committee considered that the warning letter sent by the Chairman of the Content Board to Simon Shaps had made clear the importance that Ofcom attached to the achievement of the out of London quota, but that despite this no evidence had been presented that the letter had resulted in action being taken either by ITV Network or by ITV plc to ensure that the quota was met. Rather, ITV's oral evidence suggested that the culture within ITV plc and ITV Network at that time had been to push the issue to one side and assume that the quota would be met, rather than to put specific measures in place and strive to achieve it.

8.31 In the Committee's view, ITV plc and its licensees had also had control of a number of the levers which would have helped to ensure that the quota was met. ITV plc was a major supplier of services to ITV Network and a major supplier of out-of-London produced programmes.

8.32 Through its control of the production process for ITV Production-made programmes, ITV plc was also in a position to know when a programme which had previously qualified as out of London produced (according to the Ofcom definition) ceased so to qualify as a result of decisions made during the production process. The Committee further noted that a number of the programmes wrongly classified as out of London productions were made by ITV Productions.

8.33 In addition, ITV Broadcast Resources was in possession of full information as to the composition of the Network schedule and the extent to which the composition of the schedule met the Tier 2 quotas. ITV plc had acknowledged that they had the best access to information and that the non-ITV plc licensees had received little real time information.

8.34 The Committee also considered that the breach was repeated, in that ITV had failed to achieve the out of London quota in both 2006 and 2007, and in fact the size of the shortfall against quota had been greater in the second year.

### **Mitigating Factors**

8.35 The Committee then considered whether there were any factors which in its view might limit or decrease the level of financial penalty.

- 8.36 The Committee acknowledged that ITV Network and ITV plc had co-operated fully with the Ofcom investigations and had undertaken a comprehensive audit of the 2006 and 2007 data once they had an indication that there had been non-compliance with the quota. It was this comprehensive audit which had revealed the extent of the failure to meet the 2006 and 2007 quotas and the details of the non-compliance had been revealed to Ofcom in an open and honest way.
- 8.37 The Committee also acknowledged the improved compliance measures which ITV Network had put in place since the initial audit by Ofcom in early 2008 and ITV Network's own subsequent audit. The quality of source data from both independent and licensee producers had been improved, system changes had been made, and responsibility and accountability for meeting the quotas had been clarified.
- 8.38 The Committee recognised that the breaches of the quota were not deliberate. ITV plc had believed until Ofcom's audit in early 2008 that the quotas by both volume and value had been met in both years.
- 8.39 The Committee also took into account the letter of 15<sup>th</sup> May 2008 from the Chairman of ITV plc to Ofcom in which he had acknowledged the breaches and the weaknesses in ITV's internal processes. He had acknowledged the need to comply with quotas, whatever the company's view of their nature or level and committed to ensuring there was no recurrence of this under-delivery and to meeting the out of London quota in 2008.

## **Conclusion**

- 8.40 Having considered the relevant facts as outlined above, and especially the seriousness of the breaches and all the representations made by ITV plc, the Committee decided to impose a financial penalty on the Licensee in respect of each regional Channel 3 licence it held, of **£20,000** a total for ITV Broadcasting Limited of **£220,000**, (payable to HM Paymaster General), which it considered to be a proportionate and appropriate penalty in all the circumstances.

## **Content Sanctions Committee**

Philip Graf  
Richard Ayre  
Stewart Purvis  
Joyce Taylor

16 January 2009