



Product Placement

A consultation on issues related to product placement

Consultation

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Section 1

Summary

- 1.1 Ofcom is the regulator for the UK communications industries with responsibilities across television, radio, telecommunications and wireless communications. The Communications Act 2003 defines Ofcom's statutory duties and includes a requirement to set, review and revise (as appropriate) standards for the content included in television and radio services. In setting these standards Ofcom is obliged to take into account the international obligations of the United Kingdom. Specifically Ofcom must have regard to the requirements of European legislation as described by EC Directive (89/552/EEC), as amended by EC Directive 97/36/EC ("The Television Without Frontiers Directive").
- 1.2 One of the key principles of the European framework is the 'separation principle'. This is designed to ensure audiences are not misled about the nature of the content – advertising or programming – they are watching. The Ofcom Broadcasting Code, published in May 2005, includes at Section 10 a specific requirement for commercial broadcasters to maintain appropriate separation between programme and advertising content.
- 1.3 The principle of separation between advertising and editorial material has been ever-present in regulation since the first commercial appeared on the UK's television screens in 1955¹. As with all areas of content regulation however, the way in which the separation principle has been interpreted and applied has evolved steadily over time to keep pace with commercial developments and audience expectations. Advertiser involvement in broadcasting is no longer limited to spot advertising. Sponsorship, for instance, is now a well-regarded feature of the commercial television landscape – generating important revenues for broadcasters and approval ratings from viewers. Controlled 'prop placement' sees commercial products and services appearing within programmes with limited prominence and due regard to context whilst interactivity allows advertisers to engage more closely with audiences.
- 1.4 This consultation recognises that the current EU legal framework contains an implicit prohibition on product placement (the inclusion of, or reference to, a product or service within a programme in return for payment or other valuable consideration). But in a climate of increasing pressures on traditional broadcast advertising revenues any potential new contributor to the commercial broadcasting funding mix needs to be given due consideration. Product placement is one potential revenue source that has long been prohibited in television programmes by virtue of the separation principle. Yet UK audiences are familiar with its use as product placement is seen frequently in a range of other media including feature films and imported US drama. This is recognised not just within the UK but also at European level, where the need to consider new forms of funding for commercial television, including product placement, has been an important aspect of the advance debate on the current TWF Directive review.
- 1.5 In this consultation Ofcom is seeking substantive debate on the implications for commercial broadcasting in the UK of a limited and controlled introduction of product placement into certain genres of programmes on commercial television channels. This will help to inform the debate on product placement at European level and will ensure that the views of both audiences and industry in the UK are well-rehearsed

¹ Television Act 1954 Schedule 2 Rule 1

should subsequent changes at European level mean that the legislative barriers to product placement are removed.

- 1.6 In considering the issues surrounding product placement Ofcom has had regard to a number of factors. These have included an evaluation of the commercial impact that any introduction of product placement might have; the impact of product placement on viewers; and the ongoing evolution of regulation from principles of separation to transparency. Ofcom has also taken into account that UK viewers are also served by the BBC which provides television services free of advertiser, sponsorship or any other commercial involvement. BBC channels will not be affected by the outcome of this consultation.
- 1.7 In both principle and practice, Ofcom believes that a cautious approach to the introduction of product placement to the funding mix of UK commercial television has merit. The proposed changes to the European framework² are a relevant context; and encouraging an early debate on what it means for UK commercial television, and the viewer, is a sensible step in the process of measured liberalisation.
- 1.8 There are however a number of significant policy questions that must be addressed in order to give certainty to viewers and guidance to broadcasters, advertisers and producers before any deregulation could be considered. Substantive discussion is therefore sought on the regulatory measures that would be required to accompany any introduction of product placement to commercial television in the UK. This must include recognition that introduction of product placement would be a deviation from the long-held 'separation principle' leading to a reliance instead on transparency to inform audiences about the nature of advertisers' involvement in programming.
- 1.9 Ofcom's aim throughout this debate is to ensure that the impact on viewers is reduced to a minimum whilst allowing broadcasters a degree of additional commercial flexibility in terms of the options they are able to offer advertisers. The areas on which Ofcom is seeking discussion and where it believes regulatory measures may be required include:
 - The genres of programmes that could be allowed to carry product placement;
 - The measures needed to ensure viewer transparency;
 - Whether the concept of undue prominence can be retained if product placement is permitted; and
 - To what degree there needs to be consistency with the Broadcast Advertising Code in product placement scenarios.
- 1.10 Product placement also introduces a new dimension to the commercial negotiations between advertisers, broadcasters and independent producers. For the first time, there is the potential for independent producers to directly negotiate for a share of marketing spend. There will inevitably be a period of 'bedding-in' as the market determines the most effective way to negotiate product placement deals and it is not unimaginable that commercial disputes will arise. Ofcom has considered whether the market may request it to play a role in the commercial arrangements underpinning product placement and its preliminary conclusions, in line with its regulatory principles, is that the market would be best placed to resolve disputes of this type. As such, Ofcom would propose not to intervene or arbitrate in commercial negotiations around product placement.

² http://europa.eu.int/comm/avpolicy/regul/regul_en.htm#4

- 1.11 Finally, whilst instinctively discussion about product placement focuses on its use in television programming, it should be borne in mind that there is a similar prohibition on product placement in radio programming. There is however a fundamental difference in the regulatory regimes for the two media as there is no equivalent EU-level justification for the prohibition in radio of product placement as there is for television. In addition to seeking views from stakeholders on a degree of deregulation of product placement on television, Ofcom is also seeking views on whether, in principle, deregulation of product placement should also be considered for radio.
- 1.12 NOTE ON TIMETABLE - Whilst Ofcom is at liberty to consult on the potential for deregulation of product placement, stakeholders must be aware that its ability to act on the outcome of this consultation will be influenced and constrained by the EC Directive and its current review. This means that the timetable for implementation of any changes suggested by the outcome of this consultation will be primarily determined by the timetable for review of the TWF Directive.

Section 2

Background and introduction

- 2.1 The Communications Act 2003 (“the Act”) requires Ofcom to ensure that a wide range of television and radio services of high quality and wide appeal are available throughout the United Kingdom and that sufficient plurality of providers of different radio and television services is maintained. In performing its duties the Act also obliges Ofcom to have regard to the desirability of encouraging investment and innovation and the opinion of consumers in relevant markets and members of the public generally.
- 2.2 Ofcom has developed a set of regulatory principles to provide a consistent means of interpreting the Act’s requirements which can be found on our website³. Of key importance is a commitment to operate with a bias against intervention; where a case for intervention can be made, we will choose the least intrusive means of achieving policy objectives. This aligns closely with the duty imposed on us by Section 6 of the Act to keep our regulatory activities under review so that we do not maintain regulatory burdens which have become unnecessary.
- 2.3 These principles were front of mind throughout the development of Ofcom’s new Broadcasting Code published in May 2005. The new Code, which came into force on 25 July 2005, deregulated significantly in the area of sponsorship and commercial references, although the fundamental principles of editorial independence, separation between advertising and programming material and undue prominence were maintained.
- 2.4 Separation between advertising and editorial material has been a requirement of regulation since the inception of commercial television in 1955⁴. As with all areas of content regulation however, the way in which the separation principle has been interpreted and applied has evolved steadily over time to keep pace with commercial developments and audience expectations. Advertiser involvement in broadcasting is no longer limited to spot advertising. Sponsorship, for instance, is now a well-regarded feature of the commercial television landscape – generating significant revenues for broadcasters and approval ratings from viewers. Controlled ‘prop placement’ already sees commercial products and services appearing within programmes (at no or less than full cost) with limited prominence and due regard to context whilst interactivity allows advertisers to engage more closely with audiences. The next step, paid-for product placement, is a potential revenue source for commercial broadcasters that have long been prohibited in television programmes by virtue of the separation principle, enshrined at European level.
- 2.5 Although the ban on product placement remained in place in the new Code, Ofcom did acknowledge the points raised by several respondents to the Broadcasting Code review consultation that increasing pressures on traditional broadcast advertising risked affecting the key sources of funding for commercial broadcasters and committed to taking a closer look at the subject.
- 2.6 In developing this consultation we have borne in mind the way regulation of audio-visual content is evolving. Increasingly regulation is moving towards measures which ensure transparency of content over simple physical separation as the means of ensuring viewers are adequately informed about the nature of the content – editorial

³ <http://www.ofcom.org.uk/about/sdrp/>

⁴ Television Act 1954 Schedule 2 Rule 1

or commercial - they are consuming. We also recognise however that the principle of separation between advertising and programming remains a cornerstone of the current European legislative framework⁵. A discussion of the legal position and its impact on the introduction of any relaxation of controls in this area is discussed at Section 3 below.

- 2.7 In addition to these deregulatory motives we have considered the potential financial impacts that change in this area would bring. We have spoken to broadcasters, independent producers, advertisers, suppliers, media buyers and 'prop placement' agencies amongst others to gain the widest possible understanding of the impact that permitting paid-for product placement might have. These conversations illustrated quite a diversity of views about the potential size of the product placement market, its attractiveness as a promotional medium for advertisers and the possible reaction from viewers. Advocates of product placement believe that removing rules preventing broadcasters from maximising their revenues and allowing them to expand the menu of media products available to advertisers would be a helpful measure to keep advertisers engaged with conventional broadcasting. This is felt to be especially necessary at a time when other content delivery media are becoming more attractive – and when personal video recorders (PVRs) are starting to have some impact on the effectiveness of spot advertising (see 4.5 below). Opponents question the potential for negative impact on editorial integrity and ultimately the viewing experience.
- 2.8 The final but fundamental contribution to Ofcom's analysis has been an assessment of the potential impact on viewers that the introduction of product placement into UK-produced programming might have. Specific research into viewer attitudes towards activities such as product placement was commissioned and an overview of this research is included at Section 5. The full report of this is being published alongside this consultation. In thinking about viewer attitudes we acknowledged that this is not a technique that is wholly new to viewers who have been exposed to its use in other audio-visual media for a number of years – most notably in feature films and imported drama series. We have also borne in mind that viewers also have access to a range of licence-fee funded BBC services which are free from advertising, sponsorship and other commercial involvement and which are not subject to the proposals outlined in this consultation.
- 2.9 Consideration of all of these factors has been incorporated into a high-level impact assessment which includes several revenue projection scenarios arising from rule relaxation and which can be found at Annex 5.
- 2.10 After considering this information, and having due regard to our commitment to removing unnecessary regulation, we recognise that the total prohibition on product placement in television programmes may no longer be proportionate to the potential detriment it seeks to prevent. This consultation document sets out the range of issues surrounding product placement and seeks views on whether the rules could be relaxed (assuming relevant changes to the prevailing European legislation). In addition we are consulting on the areas in which additional rules may be necessary to govern the use of product placement in programmes should the total prohibition be removed. These include:
- The genres of programmes in which product placement should be permitted if relaxation is pursued;
 - How to ensure transparency;

⁵ Art 10(1), Directive 89/552/EEC, October 1989, as amended by Directive 97/36/EC, June 1987

- Whether it is possible to retain the concept of undue prominence in a product placement environment;
- Whether additional measures regarding the type of products and services that can be placed and the way in which they can appear in programming are required; and finally
- What role, if any, Ofcom has in the commercial arrangements between broadcasters and independent producers.

2.11 Finally, whilst instinctively discussion about product placement focuses on its use in television programming it should be borne in mind that there is a similar prohibition on product placement in radio programming. There is however a fundamental difference in the regulatory regimes for the two media as there is no equivalent EU-level justification for the prohibition in radio of product placement as there is for television. In addition to seeking views from stakeholders on a degree of deregulation of product placement on television, Ofcom is also seeking views on whether, in principle, deregulation of product placement should also be considered for radio.

Section 3

Legal and global context

- 3.1 The Communications Act 2003 defines Ofcom's statutory duties which include a requirement to set, review and revise (as appropriate) standards for the content included in television and radio services. In setting these standards Ofcom is obliged to take into account the international obligations of the United Kingdom and specifically the requirements of European legislation as described by EC Directive (89/552/EEC), as amended by EC Directive 97/36/EC ("The Television Without Frontiers Directive").
- 3.2 The Ofcom Broadcasting Code, published in May 2005, lays out in detail the standards that television and radio broadcasters must adhere to. The Code includes a specific requirement to maintain appropriate separation between programme and advertising content giving effect to one of the key principles of the European framework, the 'separation principle' which states⁶:
- Television advertising and teleshopping shall be readily recognisable as such and kept quite separate from other parts of the programme services by optical and/or acoustic means.*
- 3.3 The Code also pays due regard to the need to maintain independent editorial control of programme content, as required by Section 319(4) of the Communications Act 2003.
- 3.4 The separation principle is designed to ensure audiences are not misled about the nature of the content – advertising or programming – they are consuming. It has governed commercial television since its inception in the 1950s and has allowed broadcasters to sell advertising (and in recent years, sponsorship) to advertisers whilst ensuring that broadcasters retained all responsibility and control for the programmes without further influence from those advertisers
- 3.5 Product placement is held to be the exemplar of a technique that breaches this separation principle.
- 3.6 Whilst any move to permit product placement would clearly be a significant step change from the principle of separation, its fundamental objective – of making clear to audiences the nature of content – could be maintained by adopting a principle of transparency. Such a move would recognise the increasing sophistication of audiences who are adapting to a more complex media environment and would allow them to identify commercial content and distinguish it from editorial.
- 3.7 This section outlines the current legal and regulatory frameworks governing the concept of product placement in the UK, and looks at attitudes to the technique in Europe and elsewhere in the world.

⁶ Ref 3 ibid

Ofcom Broadcasting Code

- 3.8 The Ofcom Broadcasting Code, published in May 2005, maintained the prohibition on product placement which is defined as⁷:

Product placement is the inclusion of, or a reference to, a product or service within a programme in return for payment or other valuable consideration to the programme maker or broadcaster (or any representative or associate of either). For the purposes of this rule, the following are not considered to be product placement:

- *References to products or services acquired at no, or less than full, cost, where their inclusion within the programme is justified editorially. On television, a brief, basic text acknowledgement of the provider of these products or services may be included within the end credits of the programme. This is permitted only where the identity of the product is not otherwise apparent from the programme itself.*
- *For television, arrangements covering the inclusion of products or services in a programme acquired from outside the UK and films made for cinema provided that no broadcaster regulated by Ofcom and involved in the broadcast of that programme or film directly benefits from the arrangement.*

EU Television Without Frontiers Directive

- 3.9 The basis for Ofcom's continuing prohibition on product placement is the TWF Directive's ban on 'surreptitious advertising', defined as⁸:

...the representation in words or pictures of goods, services, the name, the trademark or the activities of a producer of goods or a provider of services in programmes when such representation is intended by the broadcaster to serve advertising and might mislead the public as to its nature. Such representation is considered to be intentional in particular if it is done in return for payment or for similar consideration.

- 3.10 Some broadcasters have argued that if audiences are made aware of a product placement relationship in a programme (e.g. by explicit reference in credits) then viewers will not be misled and surreptitious advertising will not have occurred. The European Commission gave some credence to this view in its Interpretative Communication on the Directive in 2004⁹:

To be considered surreptitious advertising, the representation in words or pictures of goods, services, the name, the trademark or the activities of a producers of goods or a provider of services must meet three cumulative conditions: it must be intended by the broadcaster, it must be done to serve advertising and it must be capable of misleading the public as to its nature.

- 3.11 Critically, however, the European Commission has recently, and for the first time, stated that product placement is incompatible with the current TWF Directive¹⁰:

⁷ Rule 10.5, Ofcom Broadcasting Code, May 2005

⁸ Art 1(d), Directive 89/552/EEC, October 1989, as amended by Directive 97/36/EC, June 1987

⁹ Section 2.5, Commission Interpretative Communication on certain aspects of the provisions on televised advertising in the Television Without Frontiers Directive (COM (2004)) 1450 April 2004

¹⁰ Issue 4 Issues Paper for the audiovisual conference in Liverpool: Commercial Communications, European Commission, July 2005

The dual requirement of identification and separation implicitly has the effect of not authorising, within the current legal framework, recourse to product placement in programmes produced by broadcasters covered by the TWF Directive

- 3.12 In other words, although it may be possible to argue that product placement could be permitted in such a way that it does not conflict with the provision on surreptitious advertising (by making audiences aware of the placement); product placement still falls foul of the Directive as it breaches the separation principle. The Commission has now (December 2005) however published its proposals for a revision of the TWF Directive. These include proposals for a clear legal framework for product placement and associated viewer safeguards¹¹.
- 3.13 If the outcome of this consultation process is a consensus that product placement could be incorporated into the UK broadcasting environment in a limited and controlled way then stakeholders must be aware that we will need to take account of the progress towards a revised TWF Directive before we can identify our own timetable for reform. This means that the timetable for implementation of any changes suggested by the outcome of this consultation will be primarily determined by the timetable for review of the TWF Directive.

Other EU countries

- 3.14 Until the recent Issues Paper, the European Commission had never explicitly made clear whether product placement was incompatible with the Directive and clarifying the exact position on paid-for product placement across Europe is not easy. Many national regulators are silent on the subject, or claim prohibition whilst in fact there is a high suspicion that product placement takes place. Ofcom research suggests that relatively few countries explicitly ban product placement, although some may rely on the Directive's prohibition of surreptitious advertising.

The USA

- 3.15 The United States television market is widely recognised to have embraced the possibilities offered by product placement. According to PQ Media¹², television product placement in the USA is growing at a faster rate than any other media but still only represents just over 1% of advertising spend (\$1.87bn out of \$161bn). The combined value of product placement spend in television, films and other media grew by 30.5% to \$3.46bn. Advertising and marketing spending rose by just 7% for the year.
- 3.16 Programmes such as *The Apprentice*, *Survivor* and *Extreme Makeover* have made product placement so prevalent that reality shows accounted for about half of what was placed in television shows last year
- 3.17 PQ Media estimate that television placement spending will rise 30% in 2005 to \$2.44 billion, and will account for 57.5% of the total value of the product placement market, followed by films at 33.4% and other media at 9.1%. Marketers are seeing product placement as an integral part of a larger marketing package that includes traditional advertising and alternative marketing. Product placement is part of "branded entertainment", which includes event sponsorships and licensing.

¹¹ http://europa.eu.int/comm/avpolicy/regul/regul_en.htm#4

¹² Source: PQ Media, a US research and consulting firm serving the media and entertainment industries

- 3.18 Over half of product placement spending is found in four marketing categories: transportation, clothing & accessories, food & beverage, and travel & leisure. PQ Media expect these 4 categories to continue to lead in the next five years, but the fastest growing categories will be electronics & technology, toys & sporting goods and media & entertainment.
- 3.19 In terms of target demographics, PQ Media cite 18-34 year olds as a key audience for product placement due to their lack of brand loyalty and their light TV viewing (highest channel hoppers).
- 3.20 The Federal Communications Commission (FCC) does not prohibit product placement but does require on-screen disclosure of product placement arrangements. In practice this does not appear to be enforced and US consumer groups (e.g. Commercial Alert) have recently called for both greater enforcement and tougher regulations.

Section 4

Economic context

- 4.1 There is a more detailed discussion of the economic issues in the impact assessment attached at Annex 5.

What is the nature of the risk to spot advertising funded channels?

- 4.2 UK TV advertising achieved robust growth of 7.4% in 2004, rising to 17.4% in the multi-channel sector. Nonetheless there is considerable dispute about the future of the TV advertising market.
- 4.3 A detailed scenario exercise conducted for Ofcom in 2004 in the context of the Review of Public Service Broadcasting investigated the effect of a number of social, platform and technological changes on the main terrestrial channels¹³. Building on a research report by Price Waterhouse Coopers (PWC) that forecasted UK TV advertising revenue for 2004 – 2014¹⁴, the analysis developed a ‘steady state’ scenario as a benchmark and then a series of alternative scenarios reflecting a number of downside sensitivities.
- 4.4 The steady state scenario projected forward the current known trends as far as 2012 and assumed that the market environment remained broadly the same as it is today. It concluded that commercial PSB channels will face growing financial pressures and will have to manage their businesses with an increasing focus on the commercial realities of a sector approaching full switchover.
- 4.5 The alternative scenarios looked at the sensitivity of the outcomes of the steady state scenario to changes in key assumptions. The conclusion of the exercise was that the outcomes from the benchmark scenario were particularly sensitive to the assumptions relating to viewing share; that is, assumptions relating to factors which affected viewing share (such as platform distribution, the impact of PVRs, the share of total advertising budget allocated to TV spot advertising) would have a direct effect on net advertising revenues and this in turn impacted directly on the profitability of the commercial PSBs.
- 4.6 Taking into consideration the growth of digital TV platforms however, the increasing number of Freeview viewers over the last 18 months could indicate more positive prospects for advertising-generated revenues than anticipated by the report – particularly as the viewing of commercial analogue channels is higher in Freeview households than other multi-channel households.
- 4.7 This potential appears to be supported by the move of some channels away from subscription-based to advertising-based financing, relying on the expectation that advertising revenues might outgrow subscription revenues (e.g. the recent move of E4 to broadcasting unencrypted on the Freeview platform). There is a possibility that

¹³ ‘Looking to the future of Public Service Television Broadcasting’, 30 September 2004. This report incorporates the results of a report by Price Waterhouse Coppers entitled ‘Forecasting UK TV advertising Revenue 2004-2014’ concerning spot advertising. (www.ofcom.org.uk/consult/psb2/future/future.pdf)

¹⁴ The main conclusion of the report was that analogue and multi-channel Net Advertising Revenues (NAR) will grow at different rate, leading to a total NAR growth of about 2.5% in real term. Analogue channel NAR is expected to remain broadly constant in real terms whereas multi-channel NAR is anticipated to grow at around 9-10% per year in real terms.

the work undertaken in 2004 has underestimated the potential of DTT to help keep advertising revenues on the main terrestrial commercial channels as it was not as clear then how quickly the Freeview viewer base would increase compared to that of the multi-channels – a possibility that the report had highlighted in its sensitivity analysis. This would mean that the audience fragmentation effect identified in the report would not be as serious as suggested in some of the downside scenarios. This also indicates that the role of different television distribution platforms especially the development of Digital Terrestrial Television (e.g. Freeview) needs to be carefully monitored in order to accurately assess the risk to spot advertising funded channels.

What is the real threat from Personal Video Recorders (PVRs) and advertising moving to new media?

- 4.8 Recent evidence on the consequence of PVRs on impacts seems to indicate that several factors are at play including how many people have PVRs, how often are the ads fast forwarded, and how much viewing is watched non-live. By carefully anticipating how viewers use their PVRs and how viewers absorb fast-forwarded ads, strategies to maximise impacts could be effective at limiting the damage caused by PVRs. Depending on the combination of assumptions made for these three factors, it appears that the loss of impacts by 2012 due to PVRs could reasonably range between 8-9% and 12-14%, which is less than the rapid technological change scenario had assumed.
- 4.9 As outlined above, the share of the total advertising budget allocated to TV spot advertising is another important variable for the future funding prospects of commercial analogue channels. Since the studies referred to in paragraph 4.3 were published there has been growing evidence that broadband subscription is increasing at a sustained rate. This in turn could make it attractive for advertisers to spend higher amounts on internet and other broadband-based media. A diversion of advertising budget away from TV spot advertising to internet advertising is likely to materialise; however the rate at which this is going to occur and the magnitude involved are not yet clear.
- 4.10 The forecast future for television as described above reveals significant difference in growth between commercial terrestrial channels and multi-channels, with some difficult prospects for the former and a brighter perspective for the latter.
- 4.11 The main reason behind this growth rate difference lies in the increase in multi-channel audiences at the expense of analogue audiences, resulting from a combination of social, platform and technological changes. This audience fragmentation leads to an increase in the audience share of multi-channels and in the volume of impacts these multi-channels can deliver. This means that advertising on multi-channels becomes more attractive resulting in advertising prices increasing relative to those on analogue channels, which are not expected to augment much due to the increasingly competitive environment. As a result, the risk of a funding crisis appears less likely for multi-channels although the PWC report did highlight that multi-channel Net Advertising Revenues (NAR) was more vulnerable to changes in audience share and so would tend to be more volatile.

Revenue estimates of product placement

- 4.12 Faced with this potential threat to spot advertising, a number of broadcasters have argued there is a case for permitting product placement on UK television; a case which has been recognised by the European Commission (see 3.12).

- 4.13 It is however difficult to estimate the revenue contribution that permitting product placement would bring to commercial television. As noted in Section 3, product placement in the USA is growing at a faster rate than any other media but still represents just over 1% of advertising spend (\$1.87bn out of \$161bn). If this rate of growth was replicated in the UK, this suggests that product placement revenues might reach £100m.
- 4.14 However, pre-consultation discussions have suggested that the UK market is likely to be some what less than this, at least in the early years. Most observers expect at least some continued regulation of the market and, although £100m might be an eventual aspiration, most observers see the UK product placement market as being worth around £25-35m after five years or so (see Impact Assessment at Annex 5).
- 4.15 Many observers do note however that the related, and not unimportant, benefit of rule relaxation in this area is expected to be the additional flexibility that broadcasters and producers are likely to be able to provide advertisers in terms of access to audiences – which may in turn lead to advertisers retaining or spending more of their advertising budget on television.

Section 5

Viewer reaction

- 5.1 Audiences in the UK have been consumers of content incorporating product placement for many years most notably in feature films but also in US-produced drama series, as noted in paragraph 2.8. In order to gauge the likely opinions of UK audiences into more widespread use of product placement in broadcasting we undertook a short programme of qualitative research. The full report of this is being published alongside this consultation and can be found at www.ofcom.org.uk/research/tv/reports/. The research was primarily aimed at answering three questions:
- What do viewers think of the different ways that commercial television is funded at the moment?
 - What do they think about some other ways that are not allowed today, but may be possible options for the future, such as product placement?
 - Are viewers aware of the regulations in this area that are currently in place? How do they feel about them?
- 5.2 Six discussion groups were conducted in locations across England, Scotland, Wales and Northern Ireland during June 2005. Each group lasted four hours, and a total of 87 people took part. The high-level findings of the research relevant to the questions raised by this consultation document are presented below.

What do viewers think of the funding mechanisms in place today?

- 5.3 Programme sponsorship is the least disliked of today's funding mechanisms. Advertising is grudgingly accepted – though people do not like the idea of more being shown.
- 5.4 While participants felt that adverts have become slightly more intrusive over the last five years, they also felt the quality of television programmes had improved slightly.
- 5.5 Participants liked the realism that prop placement can give to programmes and found nothing to object to in this mechanism.
- 5.6 Pay interactivity was the most polarising of today's funding mechanisms. Middle-aged parents with children at home were the most disapproving. People worried that pay-per-view would lead to them "paying twice" for content – and possibly paying for content which is available free-to-view today.
- 5.7 Many of the issues that people raised in relation to the different funding methods were related to children – both in terms of protecting children themselves, and also protecting parents from the influence of advertising on children.
- 5.8 News & current affairs, religion and children's content were seen by respondents as 'no-go areas' for commercial activity. In contrast, sport was widely seen as the most commercial genre, followed by film, entertainment and drama. Attitudes towards sport may not be directly related to broadcasting but also include player/team sponsorship, tournament sponsorship, etc.

- 5.9 Little differentiation was made between the commercial PSB channels and multi-channel services in terms of the appropriateness of different mechanisms, though on the whole PSB channels were seen as less appropriate for the mechanisms than multichannel services. Mixed entertainment digital channels were seen as the most appropriate channels for pay-per-view and pay interactivity services.
- 5.10 A minority of participants thought that product placement already takes place pointing to the appearance of various car manufacturers in James Bond films, eBay and Apple in *Sex and the City*. They also cited examples, however, of current UK programming such as Cadbury's chocolate in *Coronation Street* and car manufacturers in *Top Gear* – which do not currently include product placement.

What do viewers think about potential future funding mechanisms?

- 5.11 When discussing future funding mechanisms with participants, product placement was generally well received when it enhances the realism of a programme, is relevant and is not too prominent. Background product placement was the most popular when ranked against the other means of funding.
- 5.12 Participants differed in their view of what is and is not prominent; they also recognised that achieving consensus could be difficult in practice.
- 5.13 Participants did not like the idea of being sold to by stealth – they preferred transparent disclosure of commercial arrangements. This suggests, echoing the European Commission's view, that transparency would be an important aspect of any regulatory regime governing product placement.
- 5.14 Respondents had concerns about advertiser-funded programmes because of fears about advertisers having too much editorial control.
- 5.15 As indicated earlier, participants were not comfortable with the prospect of more adverts on television.
- 5.16 Most people supported the principles that underpin the current regulations. A substantial minority (around 25%) had a particularly "purist" attitude to the integrity of programmes – these people tended to subscribe to the public service tradition of television and supported the status quo.
- 5.17 Participants were more inclined to relax the regulations when faced with a trade-off (i.e. in a world where money from traditional advertising was under pressure) – especially with regards to more spot advertising. However, they were sceptical about the premise that there could be a funding crisis in television.
- 5.18 The final rankings suggest that some potential new funding mechanisms (especially a limited form of product placement and possibly more minutes of advertising) could be preferred to some of today's mechanisms (especially pay interactivity and pay-per-view).

Section 6

Options and issues

6.1 This section sets out the options for change and the issues that we believe need to be considered in deciding whether to permit product placement. It should be read in conjunction with the analysis presented in the Impact Assessment and the results of the viewer research.

Whether to permit product placement

6.2 As stated at paragraph 2.10, Ofcom is seeking views on whether product placement in commercial television programming should be permitted, subject to the results of this consultation and the evolving European legislative position. The reasons for this are set out in the following paragraphs.

6.3 The Communications Act 2003 requires Ofcom to ensure that a wide range of television and radio services of high quality and wide appeal are available throughout the UK. In doing so Ofcom is also obliged to have regard to the desirability of encouraging investment and innovation. It is an integral part of Ofcom's role to consider any potential threats to the revenue streams of broadcasters, particularly if those threats suggest that it may no longer be possible to maintain let alone increase the range and quality of programming available to UK audiences.

6.4 There is currently considerable discussion about the risks to spot advertising funded channels, as outlined in Section 4, which suggests that Ofcom must look seriously at the way in which regulation constrains the ability of broadcasters to maximise their revenue generating opportunities. It is however difficult to estimate the revenue contribution that permitting product placement would bring to commercial broadcasters. Whilst our analysis in Section 4 suggests a potential market of £100m, our pre-consultation discussions with industry stakeholders suggests that, in the early years at least, the market will be somewhat less than this at around £25-35m.

6.5 By way of context it is worth reflecting on the historical growth of the sponsorship market. From a low base in the early 1990s it has now grown to a point where it is contributing an important, if not huge, £114m (c. 3%) of commercial television total advertising and sponsorship revenues. Expectations of further growth have been encouraged by the recent relaxations in the Ofcom Broadcasting Code. Crucially sponsorship revenue is seen as relatively immune to the threat posed by PVRs.

6.6 The direct financial impact that product placement could have therefore, whilst not insignificant, is relatively small when compared to current spot advertising revenues. This simple quantitative observation does not however take into account the related, and not unimportant, benefit offered by product placement which is the additional flexibility that broadcasters and producers would then be able to provide advertisers in terms of access to audiences – which may in turn lead to advertisers retaining or spending more of their advertising budget on television.

6.7 In addition Ofcom, as a regulator committed to act with a bias against intervention, must also explore the views expressed by some stakeholders that an outright prohibition on product placement is now disproportionate to the detriment it seeks to prevent.

- 6.8 As outlined in paragraph 3.9, Ofcom's current prohibition gives effect to the TWF Directive's ban on 'surreptitious advertising'. By prohibiting the paid-for appearance of products or services in programmes the risk of confusing audiences about the nature of content is reduced to a minimum. It is clear however from the results of our audience research that viewers are not themselves wholly averse to the inclusion of commercial material within programming provided they are aware of its presence and that its inclusion adds to the realism of programmes. Indeed many viewers believed that product placement was already a part of the UK broadcasting ecology – as indeed it is, in imported programming.
- 6.9 In light of these factors, Ofcom is now examining whether there is scope for a limited and controlled relaxation of the current total prohibition on product placement on commercial television channels.

Question 1: Is the total prohibition on product placement no longer proportionate to the potential detriment it seeks to prevent?

Regulation of product placement

- 6.10 If there were to be consensus amongst stakeholders around the proposal to permit product placement in broadcasting, and the relevant legislative changes at European level reflect this, Ofcom would need also to consider whether any rules are required to govern its use and if so what they should be. Our pre-consultation discussions with stakeholders and our audience research revealed a number of concerns about the adoption of product placement. These included concerns about:
- The genres of programming in which product placement should be permitted;
 - Children's more limited ability to distinguish advertising from editorial content;
 - The way in which audiences are informed of its inclusion;
 - The challenge product placement poses to the concepts of undue prominence and editorial integrity.
- 6.11 Ofcom agrees that these concerns must be considered before any introduction of product placement could be contemplated and they are discussed in detail below. In our assessment of them we have been informed by the experience of the successful introduction of sponsorship into the UK broadcasting environment. This was characterised by strict initial rules, progressively relaxed over time by the respective regulators. This model of regulation, which allowed for a measured introduction of a significant alteration to the on-air experience, ensured a gradual evolution of the market. In the research undertaken to accompany this consultation sponsorship was rated by viewers as the least disliked funding mechanism in commercial television today.

Should product placement be allowed in all programming genres?

- 6.12 It is widely agreed that the programming genres most suitable for commercially successful product placement exploitation are sport, contemporary drama (including soaps), game shows and magazine programmes. These are genres which some viewers already believe contain product placement - possibly because they often have significant brand presence in their content e.g. team, vehicle or ground sponsorship in sport, cars in contemporary drama, products or services as prizes or review subjects (in accordance with the Broadcasting Code).

- 6.13 In contrast, Ofcom’s research revealed that viewers also believed that some genres were not appropriate for product placement, specifically news and current affairs, religion, and children’s programmes. Viewers’ rationale for rejecting product placement involvement in these programming genres was not related to commercial considerations but rather to the appropriateness of brand presence:
- News and current affairs were generally understood to rely on impartiality and some were concerned that brands may receive different journalistic treatment were they involved in some financial relationship with the broadcaster;
 - Strong views were expressed about religious programming which, whilst generally not considered personally relevant by respondents, was judged to be inappropriate for commercialisation;
 - In relation to children’s programming, the majority of research respondents felt that it was right to prohibit the use of product placement; Reasons cited included the need to protect children from commercialisation and the need to protect parents from “pester power”.
- 6.14 In relation to news and current affairs programming, Ofcom believes that any use of product placement as a funding technique risks damaging audience perceptions of editorial integrity and due impartiality – irrespective of the actual influence funding partners may or may not have on content. It is for these reasons that sponsorship of news and current affairs programmes is not permitted at present and Ofcom considers that similar restrictions would be appropriate on the use of product placement within news and current affairs.
- 6.15 Ofcom does not believe that the same rationale can be extended to religious programming. In respect of this genre of programming, as with all programming, Ofcom expects broadcasters to exercise appropriate judgement on the suitability of content for relevant audiences. Where viewer research suggests that audiences find a particular technique or creative treatment inappropriate, Ofcom would expect broadcasters to make responsible decisions about its use. Ofcom’s sponsorship rules do not prevent religious programmes being sponsored, leaving it to broadcasters to decide whether or not to seek sponsorship revenues around religious programming and Ofcom’s initial view is that a similar approach should be adopted for product placement.
- 6.16 The issues around children’s programming are different again and centre on a) the reduced ability of children to distinguish between commercial and editorial content and b) parents’ expectations that children will not be exposed to excessive commercialisation. As one of the fundamental provisos of any introduction of product placement will be the clear identification of viewers to its use, Ofcom accepts that there are unlikely to be ways in which transparency measures can be effectively applied to children’s programming. For this reason, it considers that product placement should not be used in children’s programming.

Question 2: Do stakeholders agree that product placement should not be permitted in:
a) news;
b) current affairs;
c) children’s programmes?

- 6.17 Ofcom would also welcome debate on whether there are additional genres of programming which initially at least may need to be prevented from incorporating product placement. These genres could include factual programming and drama

where viewers' relative unfamiliarity with product placement if combined with clumsy handling by broadcasters and/or producers may have a detrimental effect on the viewing experience and/or risk viewers perceiving that editorial integrity was being undermined.

- 6.18 In order to reduce this risk to a minimum, Ofcom is also considering whether product placement should also be prohibited in factual and drama genres, at least in the short-term. Stakeholder views on the merit and impact of this proposal are therefore also being sought.

Question 3: Do stakeholders consider that if product placement were introduced, a phased approach should be adopted that, in the short-term at least, prohibited product placement from use in:

- a) factual programmes;*
- b) drama;*
- c) any additional genres?*

Question 4: If product placement were permitted in these genres at the outset how feasible do stakeholders believe it would be for Ofcom to re-impose restrictions on these genres at a future date?

How to ensure audiences are aware of product placement

- 6.19 As discussed earlier in this document (see paragraphs 2.4 and 3.2) the use of product placement would present a risk to the historic principles of clear separation between editorial and commercial content. To overcome this risk, and to ensure that audiences are not misled about the nature of the content they are consuming, appropriate measures to deliver transparency would have to be adopted by broadcasters.

- 6.20 The European Commission in its recent Issues Paper argues that the presence of product placement in a programme would need to be made clear at the start of a programme¹⁵:

Explicit authorisation (for product placement) would be accompanied by the obligation, common to all forms of audio-visual commercial communications, to provide clear identification at the beginning of the programme concerned.

- 6.21 Our pre-consultation discussions with broadcasters revealed that there was some antipathy to this proposal with most broadcasters we spoke to believing that identification of product placement should be confined to the end credits. Ofcom has also considered the risk that including information about placements at the start of programmes may make advertisers keener to commercialise the disclosure message. Our audience research however, suggested that viewers would prefer upfront disclosure.
- 6.22 Whilst this aspect of product placement regulation may ultimately be determined by European requirements, it is Ofcom's initial view that, on balance, audiences would be better served by identification at the start of a programme than at the end. In addition to the simple fact that end identification would leave audiences unaware of the placement until the end of the programme, the current practice of broadcasters to run end-credits fast and/or shrink the screen to combine with an additional

¹⁵ See Ref 10 ibid

programme/channel promotion, could make it hard for a clear message about the inclusion of product placement to be given.

- 6.23 Taking into account these factors, and with reference in particular to our audience research which confirmed that viewers expected transparent disclosure of commercial arrangements, Ofcom is minded to insist on clear identification of product placement arrangements at the start of any programme.

Question 5: Do stakeholders agree with Ofcom's provisional view that the use of product placement in programmes should be:

a) clearly identified; and

b) clearly identified at the start of any programme in which it is contained?

Can the concept of 'undue prominence' be retained in a regulatory regime permitting product placement?

- 6.24 The Ofcom Broadcasting Code at rule 10.4 prohibits the giving of any undue prominence to a product or service in a programme:

'Undue prominence' may result from:

the presence of, or reference to, a product or service (including company names, brand names or logos) in a programme where there is no editorial justification; or the manner in which a product or service (including company names, brand names, logos) appears or is referred to in a programme.

- 6.25 There are two underlying rationales for the current position on undue prominence. First, the need to clearly distinguish between programme and advertising content as discussed elsewhere in this document. Second, to preserve editorial integrity and reduce to a minimum the risk that the independence of broadcasters is compromised. If, as discussed above, there are alternate ways to alert audiences to the nature of content then the only basis for retaining the undue prominence prohibition must be to preserve editorial integrity and prevent the distortion of programmes for commercial purposes.
- 6.26 Currently, undue prominence may arise where there is no editorial justification for a commercial reference or from the manner in which the reference is made (for example prolonged or repeated shots of a branded product). Some stakeholders have suggested to us in pre-consultation discussions that the concepts of undue prominence and product placement are incompatible. Not unreasonably advertisers, for instance, expect to get a significant return on their investment in terms of audience recognition if they are to pay sums approaching media value to have their products and services included in programmes.
- 6.27 Some broadcasters on the other hand believe that it would be possible to retain the concept of undue prominence were product placement to be permitted. This view arises from their belief that clumsy or heavy-handed integration of products and services into storylines risks alienating audiences, damaging editorial integrity and compromising their independence. It is therefore seen as being in their interests to ensure that product placement is only used in situations that have editorial justification, where pack shots or product references are incidental and where there are no scripted references to products or their attributes or calls to buy. Such an approach would go some way toward continued compliance with the prohibition of undue prominence but would undoubtedly mean that a lower value would be placed on the airtime by advertisers.

- 6.28 Not all broadcasters are likely to share these views of product placement and indeed views may vary within broadcasters as to the 'prominence threshold' that should apply to different types of content - contemporary drama versus magazine programmes for instance. It is also clear that there are already different views of what undue prominence means. If we refer to a US example, where product placement is permitted, some US observers believe that the Coca Cola involvement with *American Idol* was within acceptable limits whereas many UK observers would agree that the Coca Cola sponsored series represented fairly intrusive product placement.
- 6.29 There is clearly a need for substantive debate about the concept of undue prominence and its potential impact on editorial integrity (both real and perceived) before any relaxation of the prohibition on product placement can be introduced. Ofcom would welcome the fullest range of views on this issue before coming to any conclusions.

Question 6: Can the current concept of undue prominence be retained in a regulatory environment that permits product placement?

Question 7:

a) Is it sufficient to rely on the editorial responsibility of broadcasters to regulate the potential excesses of product placement?

b): Do stakeholders believe that Ofcom should, initially at least, apply regulatory constraints to the way in which product placement appears in programmes e.g. prohibiting scripted references to attributes of products, limiting the length of time products, logos, brand names etc can appear?

Question 8: Should 'calls to action' be permitted around placed products or services e.g. 'red button' interactivity, 'buy now' exhortations from presenters?

Are all products and services acceptable for product placement?

- 6.30 The Ofcom Broadcasting Code contains no prohibitions on the type of products and services that can appear in programmes as product placement, or the times or manner in which they are used, relying instead on editorial justification, context and audience expectations as a guide to broadcasters. In contrast there are prohibitions on the products and services that can be advertised on television, the ways in which they can be advertised and, in some cases, the times at which advertisements for certain product categories can be broadcast¹⁶.
- 6.31 Generally, products and services are restricted from advertising for reasons of legality e.g. prescription-only medicines and/or prevention of harm to vulnerable groups e.g. alcohol advertising in children's programmes. Product placement presents a route to advertising outside of the remit of the Broadcast Advertising Code which, if unchecked could see product placement of currently prohibited products such as firearms or prescription-only medicines for instance. This appears to Ofcom to be an unacceptable circumvention of the Advertising Code. If the relaxation on product placement proceeds we would propose to limit the products and services that can be promoted in programming time to those which are permitted to advertise.
- 6.32 In addition, there are some products and services currently prohibited from advertising in or around certain types of programme e.g. slimming products cannot

¹⁶ See <http://www.asa.org.uk/asa/codes/>

be advertised in breaks around programmes of particular appeal to children under 18. We believe that it would be appropriate to extend the application of advertising scheduling rules to relevant programmes for product placement purposes.

Question 9: Do stakeholders agree with Ofcom's provisional view that:
a) *products and services prohibited from advertising cannot be placed in programmes?*
b) *only products and services that would be permitted to advertise in breaks around a particular programme may be placed in that programme?*

Question 10: Are there additional products not currently prohibited from advertising that should be excluded from use in product placement e.g. over the counter medicines?

- 6.33 Finally, the Broadcast Advertising Code contains a number of provisions about the way in which certain products and services can be advertised. Both cars and alcoholic drinks for instance attract specific detailed guidance about the creative treatments that can be used. Typically these provisions are designed to prevent portrayals of product use that either excessively glamorise a potentially harmful product, which are dangerous or illegal, or which may lead to harmful emulation. The advent of product placement potentially opens up a number of programming scenarios that would be wholly unacceptable if used as advertisements e.g. cars in dangerous, high-speed pursuits. Whilst research has historically confirmed audiences' different expectations of programming and advertising material, Ofcom is concerned to ensure that by permitting product placement it does not fundamentally undermine the various protections that the advertising codes have in place.
- 6.34 In considering this issue, Ofcom is also aware of the anomalies that could arise were consistency with the advertising code principles to be insisted upon. If product placement scenarios were required to comply with advertising code rules, whilst a 'prop placed' sports car (where no fee for appearance had been paid) could be seen taking part in a dangerous high-speed car chase, the same car, were it to appear by virtue of product placement, could not be driven in a similar way. Alcohol, which attracts a range of advertising restrictions, would become particularly difficult to place in many programme scenarios.
- 6.35 No conclusions have been reached on this aspect of product placement and we welcome substantive views from all quarters to inform our decision-making.

Question 11: Are there other provisions of the Advertising Codes that should be extended to product placement e.g. creative treatments, substantiation of claims?

What role, if any, should Ofcom play in the commercial arrangements surrounding product placement?

- 6.36 In addition to the fundamentally deregulatory motives supporting calls to permit product placement are expectations that product placement will be a welcome revenue generating opportunity for broadcasters facing competition for advertising spend in an increasingly fragmented market. Allied to this, some independent producers have indicated that product placement will, for the first time, allow them to gain a direct share of advertising revenue. Ultimately this will depend on the complex negotiations between advertiser, broadcaster and independent production company – the key issue being who gets the revenue from placement.

- 6.37 Whilst independent producers are hopeful that they would receive some part of a revenue split, there is a concern that broadcasters would retain an upper hand. This fear appears to have some justification as both our pre-consultation discussions with advertisers and observations of the US product placement market suggest a preference on the part of advertisers to deal direct with broadcasters when entering into product placement arrangements. Additionally, broadcasters argue that responsibility for 'selling' product placement opportunities should lie with themselves as they are the ones best placed to deliver on audiences and argue that from a contractual point of view, product placement could be accommodated within the existing contractual relationships between advertisers and broadcasters. They also cite their ultimate compliance responsibility. This latter point presents an additional challenge to the independent production community who fear that they will be placed under undue pressure from broadcasters to accept particular products in programmes, affecting their editorial integrity. In the producers' view, the diversity and quality of television is generated by good production (more than by good broadcasting). Hence they argue that funnelling of funds directly to production companies will best ensure that television production remains diverse and of high quality.
- 6.38 Whilst Ofcom does not anticipate a significant level of commercial dispute arising from any introduction of product placement, it does recognise that in an emerging market there will inevitably be some disagreements as all parties look to extract maximum value from the new opportunities available to them. It is possible that both parties to a negotiation might approach Ofcom seeking to get a ruling in favour of one side or the other controlling the revenue from product placement: the broadcasters arguing from the point of view of their compliance responsibilities and independent producers arguing that they should have greater freedom to exploit other sources of funding. Ofcom does not consider that it has any clear locus to intervene to resolve disputes around revenue for product placement. It does however consider that it should be possible for both models of exploiting the opportunities offered by product placement to co-exist with an appropriate sharing of revenues.

Question 12: Is the market best placed to determine the commercial parameters that should govern product placement negotiations?

Treatment of product placement minutage

- 6.39 For the avoidance of doubt Ofcom would not propose to include product placement airtime in calculations of advertising minutage, unless it is required to do so by the evolving European regulatory framework.

Extension of deregulation to radio

- 6.40 Whilst instinctively discussion about product placement focuses on its use in television programmes, the current prohibition also applies to radio programming. There is however a fundamental difference in the regulatory regimes for the two media as there is no equivalent EU-level justification for the prohibition of product placement on radio as there is for television.
- 6.41 Stakeholders' views are therefore sought on whether, in principle, deregulation of product placement should also be considered for radio. Ofcom recognises that stakeholders' responses to previous questions may reflect their position on this specific issue.

Question 13: Should any deregulation of product placement apply as appropriate to radio broadcasting?

Section 7

Pre-consultation findings

Introduction

- 7.1 A key element of this project has been a series of interviews with a number of stakeholders in any future product placement industry. These include existing 'prop placement' suppliers, broadcasters, media buyers, advertisers and independent producers. Whilst the majority of points raised with us in pre-consultation discussions have been incorporated at appropriate points in the preceding sections of the document, comments of a more general nature are included below.
- 7.2 Inevitably the following is based on the small sample of representatives of each sector Ofcom has met so far. One of the principal aims of this consultation is to get a wider range of views across and beyond the sectors identified below.

'Prop placement' agencies

- 7.3 The existing rules do not prohibit the provision of products and services for programmes at no or less than full cost. As a result, a small industry (estimated at 12 companies in the UK) exists to provide film and television productions with 'props'.
- 7.4 The process of this 'prop placement' is as follows:



- 7.5 The existing 'prop placement' agencies have mixed reactions to the prospects of a paid-for product placement industry in television. Some see it as a significant threat to their businesses, others as a major opportunity. (Several have experience of the paid-for business via involvement in the feature film industry). Most expect that a paid-for business will result in advertisers seeking media value guarantees and editorial undertakings in return for investment and possibly a reduction in the availability of free prop provision as major opportunities become paid for. However,

the US experience suggests that 'prop placement' does remain, albeit at the bottom of the chain in terms of effectiveness and therefore investment.

- 7.6 It is important to note that currently prop placement retention fees are low compared to the potential media value that might be realised from the placement (annual fees start at £12,000 per annum per client).
- 7.7 Under the current system, the programme maker retains complete control over the product and the advertiser has no editorial influence and no guarantees concerning time and position of their products in a programme. The Broadcasting Code prohibition on undue prominence¹⁷ also applies.
- 7.8 'Prop placement' agencies are keen to stress the added value they bring to the process of placing products in programmes. This includes advice to advertisers on suitability and demand for product (and point of sale material and 'dummy' products), coordination, storage, fulfilment and monitoring. Some existing agencies believe that broadcasters advocating product placement have underestimated the financial administration/negotiation costs and that these may well outweigh the benefit to be gained from permitting product placement.

Broadcasters

- 7.9 There have been a number of public declarations by leading UK broadcasting broadcasters concerning product placement. At the EU Audiovisual Conference in Liverpool, Charles Allen, Chief Executive, ITV plc, urged the EU to remove the restrictions on product placement in its forthcoming review of the TWF Directive. By contrast, at the recent RTS Cambridge Convention, Channel 4 Chief Executive Andy Duncan argued that it might be "the thin end of the wedge" as advertisers sought to influence broadcasters to show their products in a favourable light. On balance, Ofcom's pre consultation findings seem to suggest that a majority of broadcasters would favour the introduction of product placement.
- 7.10 One of the issues Ofcom explored with smaller/niche broadcasters was whether they felt they would be crowded out by larger broadcasters if product placement rules were liberalised. This was not felt to be the case – such broadcasters have a lower point of entry for advertisers and also have strong relationships with advertisers using their channels.
- 7.11 In terms of the effect on channel commissioning, some broadcasters recognise that there is a possible danger that the range of genres will be affected as some programmes have little if any potential for product placement. However, broadcasters are also keen to stress that they recognise that product placement is likely to be a modest contributor to their businesses and that it will not be in their interest to damage their channel brands by commissioning in this way. In particular, broadcasters state that poor placement could turn away viewers leading to reduced impacts for spot advertisers. The most likely areas for successful exploitation are seen to be sport, contemporary drama (including soaps), entertainment, game shows and magazine programmes.
- 7.12 Broadcasters also note that existing product placement in acquired programmes attracts little concern from viewers. In addition to this they point out that sophisticated advertisers are recognising that brands placed in US programmes are likely to benefit from UK exposure and that this is revenue that is being lost to the UK production sector.

¹⁷ Rule 10.4, Ofcom Broadcasting Code, May 2005

- 7.13 Most broadcasters also recognise that product placement will be an expensive media product to administer. In addition to the commercial negotiations, they mentioned:
- Delivery of the product placement deals including defining and measuring the exact presence of a product/service in a placement arrangement. In the US, media measurement agencies including Nielsen and VNU have developed systems to measure the exposure delivered by product placement, including the type and prominence of each brand appearance recorded, visual and verbal dimensions, character interaction, time duration, brand visibility and exclusivity, and level of plot integration.
 - The logistics of delivering, coordinating and removing product from set.

Advertisers

- 7.14 Generally there is agreement in principle amongst advertisers about deregulating product placement. Broadly though, those advertising products targeted at expensive audiences (e.g. mobile phones, cars to 16-34s/ABC1s) are more enthusiastic about the technique than those targeting less costly demographics (e.g. FMCG (fast moving consumer goods) to housewives).
- 7.15 FMCG advertisers believe there is little research to support the effectiveness of product placement and believe that a five second pack shot has little value when a viewer is concentrating on a programme. The key to successful product placement is integration with the story line – and this is difficult with, for example, a packet of washing powder. They believe that broadcasters need to protect their programmes and that overt product placement will lose viewers and ultimately damage television production.
- 7.16 In addition, advertisers targeting more expensive demographics (16-34s, ABC1s) traditionally have a stronger predisposition to risk and innovation in marketing. Many of these brands have a history of significant product placement activity in the feature film industry and as a result are more likely to be interested in exploring opportunities in the new market that commercial television offers.

Independent producers

- 7.17 Independent producers have mixed views on product placement. For some it is welcomed as a first opportunity to break the stranglehold broadcasters currently have on revenue from advertisers (i.e. for advertising spots and sponsorship). Like broadcasters, most independent producers recognise that a negotiation would need to take place on the revenue split, although there is some concern that broadcasters would have the upper hand.
- 7.18 However, some independent producers feel that product placement will lead to undue pressure from broadcasters to accept particular products in programmes affecting editorial integrity. Some producers feel that the choice of a brand of product should be driven by the script rather than the brand that was prepared to pay for the placement.
- 7.19 Some also believed that the involvement of an advertiser in a programme was likely to add to the administrative burden of the production process.

Annex 1

Responding to this consultation

How to respond

Ofcom invites written views and comments on the issues raised in this document, to be made by **5pm on 13 March 2006**

Ofcom strongly prefers to receive responses using the online webform at http://www.ofcom.org.uk/consult/condocs/product_placement/form, as this helps us to process the responses quickly and efficiently. We would also be grateful if you could assist us by completing a response cover sheet (see Annex 3), among other things to indicate whether or not there are confidentiality issues. This response cover sheet is incorporated into the online web form questionnaire.

Responses may alternatively be posted or faxed to the address below, marked with the title of the consultation.

Julia Snape

Floor 5
Content and Standards
Riverside House
2A Southwark Bridge Road
London SE1 9HA

Fax:020 7981 3806

Note that we do not need a hard copy in addition to an electronic version. Ofcom will acknowledge receipt of responses if they are submitted using the online webform but not otherwise.

It would be helpful if your response could include direct answers to the questions asked in this document, which are listed together at Annex 4. It would also help if you can explain why you hold your views, and how Ofcom's proposals would impact on you.

Further information

If you have any want to discuss the issues and questions raised in this consultation, or need advice on the appropriate form of response, please contact Julie Myers on 020 7981 3470.

Confidentiality

Ofcom thinks it is important for everyone interested in an issue to see the views expressed by consultation respondents. We will therefore usually publish all responses on our website, www.ofcom.org.uk, ideally on receipt (when respondents confirm on their response cover sheet that this is acceptable).

All comments will be treated as non-confidential unless respondents specify that part or all of the response is confidential and should not be disclosed. Please place any confidential parts of a response in a separate annex, so that non-confidential parts may be published along with the respondent's identity.

Ofcom reserves its power to disclose any information it receives where this is required to carry out its legal requirements. Ofcom will exercise due regard to the confidentiality of information supplied.

Please also note that copyright and all other intellectual property in responses will be assumed to be licensed to Ofcom to use, to meet its legal requirements. Ofcom's approach on intellectual property rights is explained further on its website, at www.ofcom.org.uk/about_ofcom/gov_accountability/disclaimer.

Next steps

Following the end of the consultation period, Ofcom will review responses and outline its next steps in light of the timetable for the TWF Review.

Please note that you can register to get automatic notifications of when Ofcom documents are published, at http://www.ofcom.org.uk/static/subscribe/select_list.htm.

Ofcom's consultation processes

Ofcom is keen to make responding to consultations easy, and has published some consultation principles (see Annex 2) which it seeks to follow, including on the length of consultations.

If you have any comments or suggestions on how Ofcom conducts its consultations, please call our consultation helpdesk on 020 7981 3003 or e-mail us at consult@ofcom.org.uk. We would particularly welcome thoughts on how Ofcom could more effectively seek the views of those groups or individuals, such as small businesses or particular types of residential consumers, whose views are less likely to be obtained in a formal consultation.

If you would like to discuss these issues, or Ofcom's consultation processes more generally, you can alternatively contact Vicki Nash, Director, Scotland, who is Ofcom's consultation champion:

Vicki Nash
Ofcom Scotland
Sutherland House
149 St. Vincent Street
Glasgow G2 5NW
Tel: 0141 229 7401
Fax: 0141 229 7433
Email: vicki.nash@ofcom.org.uk

Annex 2

Ofcom's consultation principles

A2.1 Ofcom has published the following seven principles that it will follow for each public written consultation:

Before the consultation

A2.2 Where possible, we will hold informal talks with people and organisations before announcing a big consultation to find out whether we are thinking in the right direction. If we do not have enough time to do this, we will hold an open meeting to explain our proposals shortly after announcing the consultation.

During the consultation

A2.3 We will be clear about who we are consulting, why, on what questions and for how long.

A2.4 We will make the consultation document as short and simple as possible with a summary of no more than two pages. We will try to make it as easy as possible to give us a written response. If the consultation is complicated, we may provide a shortened version for smaller organisations or individuals who would otherwise not be able to spare the time to share their views.

A2.5 We will normally allow ten weeks for responses to consultations on issues of general interest.

A2.6 There will be a person within Ofcom who will be in charge of making sure we follow our own guidelines and reach out to the largest number of people and organisations interested in the outcome of our decisions. This individual (who we call the consultation champion) will also be the main person to contact with views on the way we run our consultations.

A2.7 If we are not able to follow one of these principles, we will explain why. This may be because a particular issue is urgent. If we need to reduce the amount of time we have set aside for a consultation, we will let those concerned know beforehand that this is a 'red flag consultation' which needs their urgent attention.

After the consultation

A2.8 We will look at each response carefully and with an open mind. We will give reasons for our decisions and will give an account of how the views of those concerned helped shape those decisions.

Annex 3

Consultation response cover sheet

- A3.1 In the interests of transparency, we will publish all consultation responses in full on our website, www.ofcom.org.uk, unless a respondent specifies that all or part of their response is confidential. We will also refer to the contents of a response when explaining our decision, without disclosing the specific information that you wish to remain confidential.
- A3.2 We have produced a cover sheet for responses (see below) and would be very grateful if you could send one with your response (this is incorporated into the online webform if you respond in this way). This will speed up our processing of responses, and help to maintain confidentiality by allowing you to state very clearly what you don't want to be published. We will keep your completed cover sheets confidential.
- A3.3 The quality of consultation can be enhanced by publishing responses before the consultation period closes. In particular, this can help those individuals and organisations with limited resources or familiarity with the issues to respond in a more informed way. Therefore Ofcom would encourage respondents to complete their cover sheet in a way that allows Ofcom to publish their responses upon receipt, rather than waiting until the consultation period has ended.
- A3.4 We strongly prefer to receive responses in the form of the online web form at http://www.ofcom.org.uk/consult/condocs/product_placement/form.
- A3.5 Please put any confidential parts of your response in a separate annex to your response, so that they are clearly identified. This can include information such as your personal background and experience. If you want your name, address, other contact details, or job title to remain confidential, please provide them in your cover sheet only so that we don't have to edit your response.

Cover sheet for response to an Ofcom consultation

BASIC DETAILS

Consultation title: Product Placement

To (Ofcom contact): Julia Snape

Name of respondent:

Representing (self or organisation/s):

Address (if not received by email):

CONFIDENTIALITY

What do you want Ofcom to keep confidential?

Nothing	<input type="checkbox"/>	Name/contact details/job title	<input type="checkbox"/>
Whole response	<input type="checkbox"/>	Organisation	<input type="checkbox"/>
Part of the response	<input type="checkbox"/>	If there is no separate annex, which parts?	

If you want part of your response, your name or your organisation to be confidential, can Ofcom still publish a reference to the contents of your response (including, for any confidential parts, a general summary that does not disclose the specific information or enable you to be identified)?

DECLARATION

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Name

Signed (if hard copy)

Annex 4

Consultation questions

Question 1: Is the total prohibition on product placement no longer proportionate to the potential detriment it seeks to prevent?

Question 2: Do stakeholders agree that product placement should not be permitted in:

- a) news;*
- b) current affairs;*
- c) children's programmes?*

Question 3: Do stakeholders consider that if product placement were introduced, a phased approach should be adopted that, in the short-term at least, prohibited product placement from use in:

- d) factual programmes;*
- e) drama;*
- f) any additional genres?*

Question 4: If product placement were permitted in these genres at the outset how feasible do stakeholders believe it would be for Ofcom to re-impose restrictions on these genres at a future date?

Question 5: Do stakeholders agree with Ofcom's provisional view that the use of product placement in programmes should be:

- a) clearly identified; and*
- b) clearly identified at the start of any programme in which it is contained?*

Question 6: Can the current concept of undue prominence be retained in a regulatory environment that permits product placement?

Question 7:

a) Is it sufficient to rely on the editorial responsibility of broadcasters to regulate the potential excesses of product placement?

b): Do stakeholders believe that Ofcom should, initially at least, apply regulatory constraints to the way in which product placement appears in programmes e.g. prohibiting scripted references to attributes of products, limiting the length of time products, logos, brand names etc can appear?

Question 8: Should 'calls to action' be permitted around placed products or services e.g. 'red button' interactivity, 'buy now' exhortations from presenters?

Question 9: Do stakeholders agree with Ofcom's provisional view that:

- a) products and services prohibited from advertising cannot be placed in programmes?*
- b) only products and services that would be permitted to advertise in breaks around a particular programme may be placed in that programme?*

Question 10: Are there additional products not currently prohibited from advertising that should be excluded from use in product placement e.g. over the counter medicines?

Question 11: Are there other provisions of the Advertising Codes that should be extended to product placement e.g. creative treatments, substantiation of claims?

Question 12: Is the market best placed to determine the commercial parameters that should govern product placement negotiations?

Question 13: Should any deregulation of product placement apply as appropriate to radio broadcasting?

Annex 5

Impact assessment

Introduction

- A5.1 Impact assessments (IAs) provide a valuable way of assessing different options for regulation and showing why the preferred option was chosen. They form part of best practice policy-making and are commonly used by regulators. Generally we have to carry out IAs where our proposals would be likely to have a significant effect on businesses or the general public, or when there is a major change in Ofcom's activities. In producing this IA, Ofcom has had regard to such general guidance as it considers appropriate, including related Cabinet Office guidance in accordance with Section 7 of the Communications Act 2003 ("the Act").
- A5.2 When read in conjunction with the rest of this consultation document, this Annex represents an Impact Assessment (IA) as defined by Section 7 of the Act. Respondents should send any comments on this IA to Ofcom by the closing date for this consultation. All comments received will be considered by Ofcom before deciding whether to proceed with our possible proposals.
- A5.3 This IA is focussed on the likely key consequences of permitting product placement. It does not address any detailed modifications that might be required to the Ofcom Broadcasting Code to authorise product placement. In conducting this review, Ofcom has taken into account the current position and likely evolution of the UK TV production and broadcasting sector and considered the likely reaction of viewers.

Basis for Ofcom involvement and alignment with mission

- A5.4 The Communications Act 2003 at Section 6(1) requires Ofcom to keep the carrying out of its functions under review in order to ensure that regulatory burdens are not maintained or imposed which are unnecessary. It is in within this context that Ofcom is reviewing the current prohibition on product placement in order to assess the extent to which the restriction is still necessary.
- A5.5 In reviewing the current restrictions on product placement, Ofcom has also had regard to other relevant provisions of the Act. These include:
- Securing the availability of a wide range of television and radio services of both high quality and wide appeal;
 - Maintaining a sufficient plurality of providers of television and radio services;
 - Having regard to:
 - The desirability of encouraging investment and innovation;
 - The vulnerability of children; and
 - The opinions of members of the public. .
- A5.6 When looked at in conjunction with Ofcom's other substantial regulatory reviews in the broadcasting sector such as the Public Service Broadcasting Review and the recent review of the Broadcasting Code, this review should be seen as another step

by Ofcom in continuing its efforts to operate with a bias against intervention and to seeking the least intrusive regulatory mechanism to achieve its TV broadcasting policy objectives.

A5.7 The remainder of this paper is organised around four sections;

- a summary of the regulatory context;
- a description of the present broadcasting market context;
- a discussion of the options considered; and
- an assessment of the impact of those options.

A5.8 In light of the uncertainty around the impact of a relaxation of the current restrictions on product placement, the assessment is necessarily high-level in nature. The paper concludes by comparing the options and indicating which one appears to best support Ofcom's mission and objectives.

Regulatory Context

A5.9 The Ofcom Broadcasting Code, published in May 2005, contains a prohibition on product placement at Rule 10(5). The rationale for the prohibition on paid-for product placement derives from European Television Without Frontiers Directive's ban on 'surreptitious advertising' and ensures that there is separation between advertising and editorial material.

A5.10 By contrast, 'prop placement' - the of placing of branded goods in television programmes at no, or less than, full cost - is permitted on the grounds that it would be neither realistic nor appropriate to remove all references to brands and trade marks in television programming. The willingness of manufacturers to offer props at less than full cost also helps to reduce programme production costs. It is worth noting that whilst manufacturers typically offer their products to producers for free, they do not have any guarantee that their products will be featured.

A5.11 At present, the regulation concerning product placement:

- prohibits paid-for product placement;
- restricts the visibility of branded goods to 'no undue prominence';
- seeks to protect editorial integrity.

A5.12 During the 2004 review of the Ofcom Broadcasting Code, several stakeholders argued that the existing product placement regulation was not only restrictive and burdensome but also a barrier to potential additional revenue sources for the production and broadcasting sector. Some stakeholders suggested that the prohibition may also undermine the credibility of the viewer experience.

A5.13 As evidence to support their arguments in favour of relaxing product placement rules, proponents made reference to the commercial benefits delivered to the US television and feature film industry resulting from their use of product placement. They also pointed to the anomaly of the current 'dual regime' in which UK-produced programmes without product placement co-exists on-screen with imported programming which does feature product placement.

- A5.14 Some stakeholders also suggested that some programme production takes place outside the UK in order to avoid the production placement prohibition. We do not have any evidence of the scale of any such activity.
- A5.15 At a more practical level, some programme producers also complained that the need to assess whether or not any references to trade marks or branded goods infringed the undue prominence rule unnecessarily added to filming time. They also suggested that in order to abide by the existing rules they sometimes had to refer to non-existent trade names or brands in a way that detracted from the realism of the production and hence the quality of the viewer experience.
- A5.16 Those putting forward these concerns argued that the deregulation of the current restrictions on product placement would constitute a first step towards alleviating some of these disadvantages and generate additional revenues for programme production.
- A5.17 Further discussions with industry indicated that the attractiveness of paid-for product placement was likely to depend on:
- The degree to which the ‘no undue prominence’ rule is lifted or amended; and
 - Whether product placement could be combined with other forms of advertising around the same programme, such as sponsorship or advertising spots.
- A5.18 The next section sets out a brief description of the market context in which the issue of product placement is being considered, particularly as it relates to the main commercial terrestrial channels.

The Market Context

- A5.19 A detailed review of the television broadcasting sector was undertaken as part of Ofcom’s Review of Public Service Broadcasting (PSB)¹⁸. This review analysed the general trends affecting television in the UK going forward and was supported by two pieces of research: **Forecasting UK TV advertising Revenue 2004-2014** and **Looking to the Future of Public Service Television Broadcasting**¹⁹. Key aspects of that analysis as related to the issue of product placement are summarised below.
- A5.20 Television is currently undergoing significant change at three levels: society, platform and technology – each of which has implications for viewers and broadcasters.
- A5.21 At the societal level, important developments include the growing affluence of individuals, the fragmentation of the traditional family unit, the growing diversity of UK society, changing attitudes towards membership of communities and other social networks, and the rise of a culture in which service users have rights independent of their wealth or status. These changes have an impact on the purposes and characteristics of television, as explained in the PSB review. Of particular relevance to the product placement debate is the increasing fragmentation of programme audiences. This is exacerbated at a platform level by the continued growth of digital television (including the development of free to view digital options such as Freeview and FreeSat from Sky) and the progress towards full digital switchover in 2012. These factors contribute to the proliferation of channels and subsequent audience fragmentation. Given that audience is a key driver of the revenues raised by

¹⁸ http://www.ofcom.org.uk/tv/psb_review/

¹⁹ See Economic Analysis of TV Advertising Market www.ofcom.org.uk/research/tv/reports

advertising and sponsorship, its fragmentation is expected to have a tangible effect on the traditional sources of revenues for broadcasters. This effect will be reinforced by changing attitudes towards, and consumption of, broadcasting.

- A5.22 Key technological developments include increasingly sophisticated electronic programme guides (EPGs), personal video recorders (PVRs), second generation interactive services, the rolling-out of DSL across the UK and the increasing numbers of households subscribing to broadband. Further into the future, the emergence of on-demand television and mobile broadcasting are all developments expected to have an impact on viewer behaviours which in turn will influence advertising revenues. Potential behavioural impacts of these developments include:
- Increasing ad avoidance i.e. viewers choosing to fast forward through advertising or to skip advertising altogether;
 - Changes in the way in which consumers organise their viewing;
 - Diversion of audience away from TV, e.g. more time spent on internet.
- A5.23 As a general point, although there is broad agreement about the threats and opportunities posed by these various developments, it is far from clear how long these influences will take to get established and how significant any changes might be.
- A5.24 The impact of these social, platform and technological changes on the main PSB channels was investigated by means of scenario analysis exercise set out in the **Looking to the Future of Public Service Television Broadcasting** document in 2004. That analysis developed a 'steady state' scenario as a benchmark and then a series of alternative scenarios reflecting a number of downside sensitivities.
- A5.25 The steady state scenario projected forward the current known trends as far as 2012 and assumed that the market environment remained broadly the same as it is today. It concluded that commercial PSBs will face growing financial pressures and will have to manage their businesses with an increasing focus on the commercial realities of a sector approaching full switchover.
- A5.26 The alternative scenarios looked at the sensitivity of the conclusions of the steady state scenario to changes in key assumptions. The outcome of the exercise was that the conclusions from the benchmark scenario were particularly sensitive to assumptions relating to viewing share; that is, assumptions relating to factors which affected viewing share (such as platform distribution, the impact of PVRs, the share of total advertising budget allocated to TV spot advertising) would have a direct effect on net advertising revenues and this in turn impacted directly on the profitability of the commercial PSBs.
- A5.27 It is worth noting that since this analysis was carried out Ofcom has announced a substantial reduction in licence fees for ITV and Five (in June 2005) and has granted the permission to ITV to reduce some of its PSB programming obligations (fewer hours of regional and religious programming) (also June 2005)²⁰. In addition recent evidence on the growth of digital platforms (especially that of Freeview) and on the consequences of PVRs already contradicts some of the more pessimistic assumptions used in these scenarios. This would seem to suggest that the impact on the main broadcasters from these factors might be more muted than suggested in some of the downside scenarios.

²⁰ see <http://www.ofcom.org.uk/media/news/2005/06>

- A5.28 It is also worth noting that the projections for the television sector indicate a significant difference in growth between commercial terrestrial channels and digital only channels, with some difficult prospects for the former but improved possibilities for the latter. The risk of funding difficulties appeared less likely for multi-channels, although the supporting research indicated that that multi-channel NAR was more vulnerable to changes in audience share and so would tend to be more volatile.
- A5.29 The next section identifies the options available to Ofcom when considering the extent to which product placement might be deregulated.

Options to be considered

- A5.30 In developing this IA we have identified a benchmark option of the status quo i.e. that the existing regulation remains unchanged (Option 1). Against this we consider the option of allowing product placement within programming (Option 2).
- A5.31 Clearly the potential impact of Option 2 will depend on the degree of rule relaxation permitted. As described in A5.17 above, for instance, the degree to which undue prominence rules are maintained or relaxed could have an important effect on the impact of any product placement introduction.
- A5.32 At this stage however Ofcom does not consider it appropriate to distinguish and evaluate options depending on the extent to which the undue prominence criterion is relaxed. Our initial contacts with stakeholders and viewers have revealed significant differences of opinion about perceptions of prominence and we do not believe we have sufficient clarity on this point to evaluate in any meaningful way how varying degrees of prominence might generate different impacts.
- A5.33 The programme genres in which product placement might be permitted could also affect the impact of any relaxation both in terms of viewer reaction and attractiveness to advertisers and broadcasters (see discussion in Section 7). In the context of discussing the impact of Option 2 we will discuss the issues around allowing product placement on a more limited range of programming i.e. maintaining a prohibition on product placement in news, current affairs and children's programming. However, in light of the uncertainty about the impact of allowing product placement in general, we do not propose to evaluate this as a separate option.

Assessment of the impact of the options

- A5.34 The following analysis has been carried out at a high level in order to identify the key impact of relaxing the rules on product placement. As explained above this analysis does not include detailed assessment of the impact of permitting varying degrees of prominence. There would however be an expectation that the greater the degree of deregulation i.e. the greater the degree of prominence permitted, the greater would be the attractiveness of product placement to advertisers and thus the greater the potential revenues generated.
- A5.35 It is expected that under the status quo option, the industry would develop along the lines anticipated in the analysis developed as part of Ofcom's Review of Public Service Broadcasting as set out above. That is, in broad terms, there would be continued growth in digital television, increased use of devices such as PVRs and various societal factors which would lead to increasing audience fragmentation. The combination of these factors would tend to work to the benefit of digital channels and

put increasing pressure on commercial PSBs to manage their businesses with an increasing focus on the commercial realities of a sector approaching full switchover.

A5.36 The impact assessment below analyses more systematically the likely consequences of the deregulatory option, Option 2, on:

- Broadcasters and producers;
- Prop supply agencies;
- Viewers;
- Ofcom;
- Broadcast competition in general.

Broadcasters and producers

A5.37 There is a general consensus among stakeholders that allowing paid-for product placement might open up new ways of attracting additional funds to television.

A5.38 By relaxing the product placement rules, broadcasters and producers are likely to be in a position to provide advertisers with more flexibility in terms of access to audiences. For their part, advertisers are reported to be keen to get better access to audiences, especially as advert-skipping and fast-forwarding diminish their control on their traditional routes to audiences and are looking to experiment with product placement to test its effectiveness. If it proves effective, advertisers are expected to respond positively to product placement by retaining or even spending more of their advertising budget on television. How much more they will be prepared to invest will depend on how much commercial impact they obtain through product placement as well as on how much competition develops amongst advertisers to get their products or services placed in programmes.

A5.39 Informal pre-consultation interviews with broadcasters and production companies revealed an expectation that paid-for product placement – if permitted in UK produced programming – would be most likely to start as cautious ‘background type’ product placement until advertisers, broadcasters and producers developed a better understanding of audience reaction. Under such a scenario, in the early years at least, product placement might not be expected to yield significant revenues. If, however, there was fierce competition between advertisers to get products placed in specific, well-known programmes, then the growth in product placement might be expected to be higher. The value of even this limited product placement might also increase over time if it develops as an alternative way to reaching audiences to compensate for the loss of impacts due to ad skipping and fast-forwarding.

A5.40 Pre-consultation discussions with stakeholders also suggested that money put into product placement could come from within existing marketing budgets, but all hesitated to be more precise. This suggests that some monies might be diverted from the current spot advertising budget but the extent to which product placement revenues might cannibalise spot advertising revenue would probably be limited.

A5.41 The above observations, gathered during informal pre-consultation interviews, have guided the development of scenarios considering the potential for product placement to generate new funding. It should be noted that the status quo option of retaining the product placement prohibition will obviously not generate any additional revenues.

A5.42 Since product placement is not permitted at the moment, Ofcom has had to develop proxies to build up an indication of how much funding is likely to be generated by allowing product placement. For the purposes of this analysis, Ofcom considers that the experience of the development of the UK sponsorship market could provide a useful benchmark in terms of considering how quickly revenue from product placement might grow. The experience of product placement in the US could also provide an indication of the potential financial impact that product placement might achieve overall.

A5.43 Sponsorship is an area of the Broadcasting Code that has been progressively deregulated since the late 1980s, as the sector and audiences have grown more familiar and confident with the technique. The progressive evolution of the concept and of its implementation translates into a source of revenues for broadcasters that have risen over time.

Table 1: Total Industry Sponsorship revenues (£m, 2004 prices)

	1998	1999	2000	2001	2002	2003	2004
Total Industry	50.7	69.2	71.1	90.9	87.0	107.2	113.8

A5.44 The table below shows how sponsorship revenues have evolved since 1998.

Source: Ofcom, PSB review work.

A5.45 It is worth noting that sponsorship has been allowed since 1988. It therefore took about 10 years for sponsorship to generate £50m a year, and another five years to reach slightly over £100m. In part the growth rate has undoubtedly been influenced by advertisers and broadcasters “feeling their way” with the rules on sponsorship and also audience reaction. In pre-consultation discussions it was also suggested to Ofcom that – because of this gradual approach - the growth in sponsorship revenues has not cannibalised existing TV advertising budgets but has been incremental revenue.

A5.46 The table also shows a degree of volatility in the growth of revenues from year to year. But, over the whole 1998-2004 period, sponsorship revenue growth has been significant, more than doubling overall. From other (confidential) data available to Ofcom, it is clear that Five and the cable and satellite channels have seen rapid growth in sponsorship revenues, reflecting the growth of their audience shares. However, the most recent data might indicate that the growth rate of sponsorship revenues might be beginning to slow – at least for the main terrestrial channels – in that most programming which is amenable to sponsorship is now being sponsored.

A5.47 It is also important to put these sponsorship revenues into perspective in order to derive an indication of their importance to broadcasters. In 2004, spot advertising revenue generated £3.5bn at the industry level, of which £2.8bn was earned by the commercial terrestrial channels. This means that at the industry level sponsorship revenues represent about just over 3% of the spot advertising revenues.

- A5.48 If product placement were allowed, then it could be argued that it would probably experience more rapid growth because it would be able to build on the regulatory experience developed with sponsorship and prop placement. However during pre-consultation discussions, stakeholders pointed to factors that could potentially seriously affect the take-up of product placement. Of particular importance among them were issues around the practical implementation of managing and controlling product placement e.g. in terms of the initial uncertainty around the interpretation and implementation of the separation principle; issues around sharing the revenues among broadcasters and producers etc.
- A5.49 In the context of assessing the financial impact of relaxing the restrictions on product placement, Ofcom has considered three scenarios for the development of product placement revenues.
- A5.50 The first scenario assumes that many small to medium advertisers prefer to keep the prop supply type of agreement to start with and it is only the large advertisers – already used to product placement abroad – that embrace the new opportunities offered by rule relaxation. This translates into small initial product placement revenues (£5m) that increase rapidly (50% per annum) as a broader range of advertisers begin to experiment with product placement.
- A5.51 The second scenario assumes that a significant proportion of advertisers currently engaged in prop placement switch to product placement in return for some form of guaranteed impact or visibility. These advertisers' initial enthusiasm is perhaps then dampened by the mixed results generated by these early product placement trials – some of which are successful, others are not. As a result, the rate at which product placement expenditure grows is smaller. This scenario translates into an initial product placement expenditure of £20m i.e. initially higher levels than in Scenario 1 that are then followed by a more conservative growth rate of 20% per annum.
- A5.52 The third scenario assumes that there is some interest in product placement across a range of advertisers so that product placement immediately draws £10m the first year. It also assumes a high rate of annual growth (50%). These growth rates are in line with what has been observed in the USA.
- A5.53 The table below sets out the development of product placement revenues for these three scenarios for the period 2006-2010 assuming that product placement is allowed from early 2006.

Table 2: Product placement – Revenues projections if rules are relaxed (£m, 2004 prices)

	2006	2007	2008	2009	2010
Scenario 1	5	7.5	11.2	17.0	25.3
Scenario 2	20	24	28.8	34.6	41.5
Scenario 3	10	15	22.5	33.7	50.6

Source: Ofcom calculations

- A5.54 As might be expected, the first scenario generates the lowest level of new funding whereas the third one generates the highest level. However, the key aspect of these scenarios is to illustrate that the overall impact of product placement – even assuming that it all represents additional revenues – is likely to be relatively modest in terms of the overall funding of commercial television. This might also suggest that product placement is less likely to cannibalise existing spot advertising revenues.
- A5.55 It is also the case that all three scenarios generate revenues that are consistent with the indications provided by the stakeholders during pre-consultation interviews and an industry seminar. These informal discussions have indicated that stakeholders consider that product placement would not generate significant new funds for TV production and estimates of the overall revenue from product placement ranged from £30m up to £50m after a few years (i.e. on a par with levels of sponsorship after a few years).
- A5.56 It is worth contrasting these figures with what can be observed in the United States where product placement is not regulated. According to PQ Media research, TV product placement amounts to about 55% of total USA product placement; it reached \$1.87bn in 2004 (a 46.4% increase compared to 2003) and is expected to reach \$2.44bn in 2005 (that is, a 30% increase compared to 2004). However TV product placement revenues are still small compared to traditional TV advertising spot revenues (worth about 3.3% of spot revenues).
- A5.57 If the US situation were to be replicated in the UK (that is, if TV product placement was to generate revenues worth about 3.3% of TV spot advertising after a few years), then on that basis product placement might be expected to have the potential to reach about £120-125m based on today's prices. This would exceed what stakeholders suggested was the likely potential for product placement (i.e. around £100m).
- A5.58 Based on the above scenarios and the comparison with the more mature US market, it seems unlikely that allowing product placement would provide significant new sources of funding for television production unless product placement experienced dramatic growth rates. Indeed, the amount of potential funding appears relatively small compared to today's NAR.
- A5.59 As with sponsorship, however, the real significance of product placement may well be the additional flexibility it gives to advertisers in terms of adding to the ways in which they can use television to communicate with viewers and thus help to keep funds within television. Broadcasters, producers and advertisers are all keen to explore this possibility in order to continue to exploit all potential benefits of the medium.
- A5.60 At the same time, it is appropriate to consider the amounts quoted above as a reasonable proxy for a first stage of deregulation, in which product placement remains constrained by a 'no undue prominence' rule. Indeed there seems to be an inclination among stakeholders to proceed with deregulation in a cautious and progressive manner in order to help the sector and the audience to adjust to the change.
- A5.61 In this context, if the existing prohibition on product placement were to be retained for certain programme genres such as news, current affairs and children's, we do not consider that this would have a material impact on the revenues generated. This is because we expect stakeholders to be cautious in implementing product

placement including being less inclined to trial product placement in programmes where market research indicates that audience resistance is likely to be greatest.

Prop supply agencies

- A5.62 Pre-consultation discussions with prop supply agencies suggested that they are not sure about the extent to which allowing product placement might affect their business. Some expressed concerns that production companies and broadcasters would step in and appropriate a significant proportion of their revenues. Others believe that they might have a first mover advantage with their experience of the logistics and detailed practical requirements of prop/product placement. Further, some agencies are also inclined to think that these practical requirements might make getting involved in product placement less attractive to broadcasters and production companies.
- A5.63 Ofcom considers that the impact on prop supply agencies of allowing product placement will be mitigated by the fact that a significant proportion of prop supply volume is expected to remain free i.e. not all products are likely to be suited to a 'paid for' product placement model. This view came out in the course of discussions with the industry. In addition the experience and preparedness of prop supply agencies is believed to provide some first-mover advantages, providing a potentially powerful spring board for entry into the paid-for product placement business. Ofcom does, however, acknowledge that prop supply agencies are likely to face increased competition and that there could well be a degree of rationalisation in this area as a result.

Viewers

- A5.64 In terms of the impact on viewers, the market research carried out by Ofcom indicates that viewers are already familiar with the concept of product placement and are relatively sympathetic to the idea of background product placement. The viewer research also considered the transparency aspects and revealed that viewers claimed they would be more accepting of product placement if its use in a programme was clearly signalled to them.
- A5.65 In terms of the quality of programming available to viewers, Ofcom does not consider that relaxing the rules on product placement in a cautious and controlled manner is likely to have an adverse impact on the quality of television programming. As indicated above, revenue from product placement is not expected to cannibalise other sources of television funding and Ofcom is therefore minded to believe that TV programming and viewers' experience could even be improved by the additional funds attracted as a result of a controlled relaxation of the product placement rules. This is especially so as viewers have indicated that background product placement is likely to increase the realism of programmes for them.

Ofcom

- A5.66 The impact on Ofcom of allowing product placement could mean an increase in overall compliance activity in the short run. Ofcom anticipates that in the early years of product placement there would be some additional costs in relation to implementation and monitoring: e.g. amending the Broadcasting Code, providing guidance to parties wanting to explore development of product placement options; and also dealing with complaints.

Impact on broadcasting competition

- A5.67 The relaxation of product placement rules is not aimed primarily at stimulating or promoting competition in TV broadcasting. However it is part of the impact assessment to discuss the impacts of options under consideration on competition between different broadcasters.
- A5.68 Competition among channels using more UK production and channels importing foreign productions could in principle be affected to some extent by the deregulation of product placement. Channels using UK production would be able to capture a new source of revenues (assuming they get a share of it) whereas the latter would not see much difference as the product placement revenues relating to foreign productions are captured abroad. This is likely to advantage PSB channels compared to multi-channels, because the former invest significantly more in UK originated programming than the latter. Even among the PSB channels, some might benefit more than others because they import less and produce more in-house e.g. ITV1. However given that the amounts at stake are relatively small, Ofcom is of the view that this impact on competition is likely to be negligible.
- A5.69 Similarly competition between different channels could in principle be affected because product placement is expected to generate revenues for some genres more than for others. Depending on the genres a broadcaster specialises in, allowing product placement might advantage some channels more than others. Informal pre-consultation contacts with the industry suggest that unsurprisingly (contemporary) dramas, soaps, sitcoms, sports, reality TV programmes are more likely to be preferred genres for product placement compared to historical dramas, documentaries, news and current affairs.
- A5.70 This should mean in turn that channels showing more of the former programme genre would benefit to a larger extent from product placement than channels showing more of the latter programmes. As above, given the small size of the forecast product placement revenues, Ofcom considers that the impact on competition between channels can reasonably be expected to be insignificant in the initial years.

Conclusions

- A5.71 The analysis in this high-level impact assessment, when read in conjunction with the earlier sections of this document, is intended to provide the context for a debate on the prospects for deregulating product placement. It considers: the impact on relevant stakeholders, including viewers; provides estimates of the potential revenue generated by relaxing restrictions on product placement; and considers broadcast competition impacts. It does not however address the detail of any specific Code modifications or guidance that might need to accompany any degree of deregulation.
- A5.72 After considering the analysis presented above Ofcom has drawn a number of conclusions about the impact of the following two high-level options included in this IA:
- Option 1 - keep the existing prohibition on product placement;
 - Option 2 - deregulate to allow product placement.
- A5.73 In addition to contributing to a deregulatory agenda, Option 2 is expected to provide broadcasters and producers with greater flexibility to carry out their business when compared to Option 1. Indeed allowing product placement is expected to enable

broadcasters and producers to provide advertisers with better access to audiences, which could in turn lead to the development of new types of programmes as well as providing access to a new source of funding – factors to which Ofcom is obliged to have regard under the Communications Act Section 3(4). To the extent that the new source of revenue contributes to ensuring the plurality of providers and the availability of a wide range of high quality and wide appeal television services, Option 2 would also help Ofcom to meet its general duty under the Communications Act Section 3(2).

- A5.74 This impact assessment explored the likely magnitude of the revenues that product placement could generate in its early years. By using the example of the development of sponsorship as a benchmark and assuming that product placement revenues are likely to grow faster as a result of the regulatory experience derived from sponsorship and prop placement, Ofcom developed three scenarios to project product placement revenues ahead for an initial five-year period. The forecast generated by this exercise is that, after five years, product placement revenues might be expected to be extremely modest compared to traditional spot advertising i.e. in the order of £25m-£50m.
- A5.75 Ofcom is of the view that at this stage there is not likely to be a significant difference in the revenues generated under Option 2 whether product placement is permitted across all programming types or whether the current prohibition on product placement is maintained for news, current affairs and children's programming. This is because stakeholders are expected to proceed slowly at the beginning, experimenting carefully with the implementation of product placement without alienating their audiences. Our initial market research suggests that a significant percentage of the audience is ready to see some product placement to take place provided that it remains of a background type; is not allowed in children, news and current affair programmes; and is transparently implemented.
- A5.76 Our pre-consultation discussions indicate that there are likely to be a number of issues around implementation of product placement on whatever basis. There is not only a question of magnitude of the benefits for the various stakeholders but also an issue of their distribution among these stakeholders. The pre-consultation interviews revealed significant differences in perceptions of how the financial gains of product placement should be split amongst broadcasters, producers and advertising and placement agencies.
- A5.77 Other costs that a deregulation of product placement might generate relate to prop agencies and to competition in the broadcasting sector. This impact assessment reveals that the overall impact on these stakeholders is likely to be relatively modest compared to the benefits from offering new degrees of freedom to broadcasters/producers in carrying out their activities.
- A5.78 The results of this high-level impact assessment appear to favour relaxation of the prohibition on product placement for three main reasons. First, such a move is deregulatory in nature, removing rules preventing broadcasters from maximising their revenue opportunities. Second, permitting product placement would reflect some viewers' preference to see the realism of programmes enhanced - providing concerns regarding the types of programmes in which product placement appears are addressed. Third, it adds to the variety of media products that broadcasters are able to offer advertisers. This could encourage them to remain committed to television as an advertising medium at a time when other content delivery media are becoming more attractive and when PVRs are starting to have some impact on the effectiveness of spot advertising.

A5.79 Taking these points into consideration and on the basis of the initial evidence it has accumulated during the pre-consultation period Ofcom is of the view that the benefits deriving from allowing product placement are likely to be higher than the costs resulting from it.