Media Reform Coalition submission to House of Lords Communications and Digital Committee inquiry on the privatisation of Channel 4

Question 1: What, if any, developments over the last five years give cause to re-evaluate the ownership of Channel 4 Corporation?

1. Channel 4 faces three long-term challenges: increasing competition from subscription streaming services; the long-term decline of TV advertising; programming cost inflation.

2. The rise of subscription video on-demand (SVOD) services online is transforming TV and video viewing in the UK. Between 2017 and 2020, SVOD viewing increased as a share of total video viewing from 6% to 19%. The shift was driven by 16-34s, among whom SVOD viewing increased from 11% to 29%[1] and for whom SVOD viewing in 2020 accounted for more viewing minutes per day on average (91) than all live TV viewing (65), YouTube (72), games console use (33) or broadcasters' video-on-demand services (11). Given that the remit of the Channel 4 Corporation (C4C) is to 'provide content which appeals to older children and young adults', the rise of SVOD viewing among younger people in particular poses a clear challenge.

3. Channel 4 depends on advertising for over 90% of its revenue. TV advertising is in long-term decline, as Ofcom identified in its C4C review in 2020.[2] Channel 4 has only been able to manage the effects of this challenge on its operating surplus due to (a) overall growth in UK ad spending, and (b) stagnating and then falling content spend. Content spend was £695m in 2016, £660m in 2019 and then £522m in 2020, when it was heavily cut in anticipation of the effects of the pandemic on C4C's finances. Originated content spend fell from £501m in 2016 to £492m in 2019, and £370m in 2020. Taking inflation into account, between 2016 and 2019, content spend fell by 10.5% in real terms, originated content spend by 13.5%. In addition to competition from SVODs and YouTube, Channel 4 could face additional competition from advertising video on-demand (AVOD) services in coming years.[3] Although Channel 4 is, at present, financially sustainable, the rise of streaming does pose a threat to its future sustainability.

4. The rise of streaming services is also generating rampant cost inflation in key programming genres, particularly high-end drama and documentaries, as this Committee noted in its 2019

[1] Ofcom, *Media Nations: UK 2021*, 5 August 2021, p.42.
Total video viewing also increased, from 4 hours and 49 minutes per (4+) person per day in 2017 to 5 hours and 40 minutes in 2020. Viewing in 2019 was roughly the same as in 2017, indicating that the extra 51 minutes of viewing per day in 2020 was most likely an effect of the pandemic. Nevertheless, average SVOD viewing minutes have increased from 18 in 2017 to 65 in 2020; among 16-34s, the figures are 30 and 91.
[2] Ofcom, *Channel 4 Corporation's performance in delivering its media content duties 2014-2018*, 27 February 2020, p.10. TV advertising revenue fell from a peak of £4.3bn in 2015 to £3.8bn in 2018: a fall of almost 12% in three years.
[3] Ofcom, *Media Nations: UK 2021*, pp.46-7.

report on public service broadcasting (PSB).[4] Channel 4 told the committee its budget per hour for commissioned drama rose from £750,000 to £1.5m between 2013 and 2017, while the BBC's high-end drama budgets had risen by 60% over the previous five years. Netflix is intending to spend over $17bn (£12.35bn) on content this year, nearly 24 times Channel 4's content spend in 2020 and over 18 times its average spend in the four years prior.[5] As a result, the same amount of funding will go less and less far over time, as competition for the best talent, production resources and intellectual property continues to intensify.

5. While we accept Channel 4 faces major challenges, we completely reject the Government's argument that privatisation is the solution. The Government has offered no plausible reasons why a privatised Channel 4 would be better placed to meet the challenges outlined above, and we believe it would in fact be less able to meet them.

6. We think it is striking that – unlike this Committee – the Government has not even consulted on whether there are ways of addressing concerns about Channel 4's long-term sustainability *while keeping the channel in public ownershi*p. In our view, that demonstrates clearly that protecting Channel 4 and its ability to fulfil its important public service remit is not what is motivating the Government's enthusiasm for privatisation.

Question 2: If Channel 4 Corporation were privatised, what would be the benefits? What would be the risks and to what extent could they be mitigated?

7. There are three main sources of funding for TV and VOD content: advertising & sponsorship, subscription and public funding (e.g. the TV licence fee). To generate more revenue for content investment, a privatised Channel 4 would have to either generate more advertising revenue, or turn to subscription revenue.

8. We believe that subscription is antithetical to the public purposes of Channel 4 in particular, and PSB more generally, since it ought to be a key principle of PSB that content is available to the whole public, regardless of ability to pay. All4's £4-a-month, ad-free subscription service already erodes this principle, and a privatised Channel 4 may go further and introduce a more expensive, 'premium' subscription tier to fund high-end content.

9. If Channel 4 is privatised, it will still be dependent on TV advertising revenue, which is in long-term decline, as the Government and Ofcom recognise. Under private ownership, Channel 4 would be required to increase profit margins for its shareholders. The two most obvious ways of doing this are by (a) cutting the content budget and/or (b) seeking to 'game' or dilute its remit. According to a report by the consultancy Ampere Analysis, the cuts to its content budget under such conditions would likely be of the order of 40-50%.[6]

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[4] House of Lords Communications and Digital Committee, *Public service broadcasting: as vital as ever – 1st Report of Session 2019*, 5 November 2019, pp.37-38.
[5] Channel 4 content spend was £522m in 2020 and averaged £673m in the four years prior.
[6] Mark Sweney, 'Channel 4 privatisation "could shut up to 60 production companies"', *Guardian*, 14 September 2021: 'the [Ampere Analysis] report argues that a new owner would aim to cut 40% to 50% of Channel 4's programming budget to boost its roughly 8% margin closer to the level of commercial peers across Europe, which operate at about 15% or higher. … A reduction in spend on original productions could jeopardise 50 to 60 small production companies … And potentially more if a buyer is particularly risk averse and looks to commission more from larger producers.'

10. Under private ownership, it would be the fiduciary duty of Channel 4's corporate leadership to find ways of circumventing the less profitable parts of the corporation's PSB remit.[7] That might be achieved by minimising what Channel 4 spends on the sorts of content required by its remit and by lobbying the Government to dilute or abolish the remit.

11. We would point out how difficult it is to define some of the concepts in C4C's media content: 'a broad range of high-quality content that appeals to the tastes and interests of a culturally diverse society'; the promotion of 'alternative views and perspectives'. There is considerable scope for a shareholder-focused Channel 4 leadership, or corporate owner, that is not committed to 'game' it by creating content that fulfils the letter but not the spirit of the remit.[8]

12. At present, Channel 4 effectively operates a cross-subsidy model, where programmes that attract lots of viewers at relatively low cost are used to fund more expensive programmes that better fulfil Channel 4's PSB remit, such as news and current affairs programmes. Privatisation would lead to the reverse: a for-profit Channel 4, whether independent or acquired by a larger, commercial, media conglomerate (probably from the United States) would make the minimum of PSB content it is required to, while focusing on maximising advertising revenue.

13. It is widely acknowledged that a remit imposing extensive PSB requirements would depress the sale value of C4C. It stands to reason that those most confident they will be able either to get around the remit, or get the Government to dilute or abolish it over time, will be most prepared to pay more for the channel and win out in any competition to buy it.

14. The Government's own case for privatisation highlights the long-term decline of TV advertising due to declining live TV viewing. What the Government does not explain is, if this is the case, why would a forward-looking media conglomerate buy C4C and invest heavily in it? The far more plausible scenario is that C4C is squeezed to produce a short term profit by cutting costs (mostly from its content spend), leading to a longer term decline in viewing, which then entails a new round of cost cutting. There is a clear precedent to hand for this kind of downward circle of cost cutting and audience decline: the collapse of commercial news publishers in the UK, particularly in the local and regional press.

Question 3: If Channel 4 were to remain in public ownership, what would be the benefits? Insofar as they are valid, how could concerns about its long-term viability be addressed?

15. Were Channel 4 to remain in public ownership it would be better placed to meet the future challenges outlined above in paragraphs 1-4, and to address concerns about its long-term viability. While a privately owned Channel 4 would be subject to considerable commercial pressures, creating an incentive for its remit to be less substantively met, for regulatory requirements to be weakened and for content production to be cut, Channel 4's current ownership structure to some extent mitigates these pressures. As such, its public ownership

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[7] That is, assuming the Government does not decide to abolish, or substantially dilute, Channel 4's channel remit or C4C's media content duties in order to maximise the value of the sale.

[8] This is not only our view, but that of the media consultancy Enders Analysis in their report on the issue: 'We believe that it will be difficult to maintain the remit with a new buyer paying any more than a meagre sum, and even if that happens, a profit-oriented buyer will have incentive to game the obligations.' Enders Analysis, *Channel 4: Privatisation, here we go again*, 22 June 2021, p.1.

structure is fundamental to Channel 4 substantively meeting its remit and regulatory requirements.

16. If Channel 4 remains in public ownership, there is the option of replacing declining TV advertising revenue with alternative forms of public funding that could strengthen its capacity to meet its remit in an increasingly competitive market, commissioning programming that is both popular *and* high-quality. For example, we propose funding Channel 4 with a new 5% tax on advertising spending in the UK. In 2020, total UK advertising spending was £23.5bn, despite the pandemic. A 5% tax would raise in the region of £1-1.2bn - more than Channel 4's total pre-pandemic revenue. A tax on all forms of advertising would be equal across formats, and spread across a range of parties (including Google and Facebook, who accounted for 80% of online ad spending in the UK last year), as well as giving Channel 4 a source of funding that is guaranteed to increase in the future.[9]

17. In addition, this small tax could be supplemented by a tax on Pay-TV and SVOD services. These services – including Sky – currently have no obligations to produce public service programming. In lieu of imposing obligations on them to do so, they could be taxed, with the revenue used to increase the budgets and capacities of the UK's public broadcasters. Ofcom estimates that in 2020 online subscription entertainment and audio-visual services generated revenue of £3.4 billion in the UK (although this includes music streaming services like Spotify). A tax on this and the roughly £13 billion in annual revenue that Sky, the UK's main Pay-TV operator, generated in 2020, could provide a further source of funding to support UK PSB production.

18. If these proposals were implemented, Channel 4 could become an ad-free TV channel and streaming service. Ofcom research has found majorities or pluralities of viewers unhappy with the amount of advertising on Channel 4, ITV1 and Channel 5,[10] and criticisms of advertising on its channels and platforms feature in Ofcom research on Channel 4's remit.[11] Research for the DCMS on viewers attitudes to the BBC, meanwhile, found not only that 'adverts were largely disliked' by television viewers, but that the iPlayer was preferred to the streaming service of commercial rivals because it is ad-free.[12] Since the lack of advertising is a major part of the appeal of Netflix and other SVOD services, an ad-free Channel 4 would be much better placed to compete online with the US streaming giants.

19. Our proposed new public funding model would mean that (a) Channel 4 would have a larger annual budget, and (b) by eliminating the operating costs created by having to sell advertising, would also be able to spend more of its budget on programming. The result would be greater investment in UK-originated programming made by the UK's independent production sector, and in the UK's film sector, with much of that investment occurring outside London, in the UK's nations and regions. The same scale and pattern of investment would be highly unlikely under private ownership. It is for this reason that the Government's proposal has been met with scathing criticism from many figures in the UK's film industry.[13]

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9 Total UK ad spending was £15.5bn in 2010, according to AA/WARC data, meaning the ad market has grown by 51.6% over the past decade.
10 Ofcom, *Cross Platform Media Tracker 2017: Audience Attitudes to Programme Standards*, pp.71-2.
11 Ofcom, *Channel 4 Corporation Remit: Research report produced for Ofcom by Kantar Media*, 12 July 2017.
12 GfK Social Research, *Research to explore public views about the BBC: For the Department for Culture, Media and Sport*, 2016.
13 Geoffrey MacNab, '"Incredibly short-sighted": UK industry reacts to possible privatisation of Film4', *Screen Daily*, 21 July 2021.

Question 4: Should the regulation and/or remit of Channel 4 be changed, irrespective of its ownership? What would be the risks and benefits of any such changes to the UK Public Service Broadcasting System?

20. Channel 4's regulatory requirements and remit should be kept under review. However, we do not see any reason for fundamental change to either. There remains a strong case for the sort of innovative, risky and creative programme making that commercial operators will usually not support, and for producing freely available content that fully reflects the diversity of the UK, with a particular focus on content that represents marginalised and underserved communities and that appeals to older children and young adults. Any decision on, or policy discussion around, the future of Channel 4 and its remit (including the present debate on its ownership structure) ought to involve proactive efforts to consult with these groups, as well as those in the independent TV production and film industries whose livelihoods are most likely to be affected. The Government's brief public consultation on its proposal is not, in our view, enough.

21. Insofar as there are any changes to Channel 4's remit, these should in our view involve strengthening existing requirements. The shift towards more geographically distributed programme production, for example, should continue, and should be accompanied by changes to how funding is distributed, and with what conditions. Alongside geographical requirements there should be requirements to promote higher labour standards in the TV and film production sectors. Independent production companies commissioned to make programmes for Channel 4 should be required to provide the local living wage, to commit not to use unpaid interns, and to ensure diversity in recruitment and promotion. Commissioning should focus on small and medium-sized enterprises (SMEs) and less on the 'super-indies' (defined by Ofcom as companies with turnover of over £70m), that are concentrated in the south-east of England and many of which are not even UK-owned.

22. Another important area for regulatory change is the current role of the Government in appointments to the board of Channel 4. There is a serious risk of these powers of appointments being abused to attempt to exert control over Channel 4 for political reasons, which could undermine its independence, and its ability to meet its remit. Appointments to the Channel 4 board should therefore no longer be subject to approval by the Secretary of State.