Submission to DDCMS's Consultation on a potential change of ownership of Channel 4 Television Corporation

pact.

September 2021

Introduction

1) Pact is the UK trade association which represents and promotes the commercial interests of independent feature film, television, digital, children's and animation media companies.

2) The UK independent television sector is one of the biggest in the world. Independent television sector revenues have grown from £1.3 billion in 2005 to just under £3 billion in 2020.[1] Like many other sectors impacted by the pandemic, the sector suffered its first decline since 2016 a 14% decrease year-on-year.

3) In 2020, Channel 4 spent £210 million on commissions from UK external producers[2].

4) Pact recognises the important role that Channel 4 plays in the UK television marketplace as a publicly owned public service broadcaster, with a unique remit to promote diversity and innovation both on and off screen – it plays a very important role in the British broadcasting ecology. The health of the UK TV production sector is closely interlinked with that of Channel 4.

5) For further information, please contact Pact's Head of Policy, Emily Oyama, at emily@pact.co.uk.

[1] Pact Census Independent Production Sector Financial Census and Survey 2021, by Oliver & Ohlbaum (O&O) Associates Ltd (2021)
[2] IBID

Overview

1. Channel 4's unique obligations have led to a booming UK independent TV production sector which has gone from strength to strength over the past four decades and is now a jewel in the crown of a world class industry. Channel 4's public service remit and its status as a publisher-broadcaster prevents it from making and owning its own programmes. This was one of the key founding principles when it was created by the Thatcher Government in the early 1980s. It is vitally important to the economic and cultural health of the UK that Channel 4 continues to be a publisher-broadcaster. It must retain its unique structure, remit and obligations, which ensures that Channel 4 works with a broad range of suppliers from across the country. There is no doubt that the media landscape has been changing with technology enabling audiences to pick whichever content they want, when and wherever they want, particularly with new content providers bringing further competition within the market. But much of the changes can be overstated by the Government. Broadcast TV accounts for the majority of viewing across all audiences and contributes the most revenue for the independent production sector. The Subscription Video on Demand (SVoD) providers operate with an entirely different business model and do not fulfil the same role as PSBs. SVoDs retain all rights and focus on content that appeals globally foremost with less room for genuine British stories across a range of genres.

2. Channel 4 still commissions more programmes from small production companies than other PSBs between 2015-2019 from across the UK.[3] This has enabled generations of creative entrepreneurs and small innovative start-ups to break into the UK broadcasting market and grow their businesses, initially working for Channel 4 and then supplying other broadcasters both domestically and internationally. Last year, Channel 4 worked with 161 independent production companies. Its risk-taking remit which breeds innovation and originality, and the creation of new IP, also provides much needed competition for the other PSBs which in turn benefits both viewers and the wider economy.

3. The diversity of supply and programming will be lost if Channel 4 is privatised and allowed to make and control its own programmes as the current slots and commissioning would move across to the in-house production arm. To enable Channel 4 to make and own its own programmes the new private owners of Channel 4 would need to cancel a range of productions made by both large and small companies to free up programme slots for its own production arm. Pact commissioned Oliver and Ohlbaum (O&O) Associates to estimate the potential impact of a Channel 4 ownership change, with an emphasis on the implications for the UK's international competitiveness and global profile. It estimated £80 million of content spend will be lost to a Channel 4 in-house production arm in the first year after an initial push to move content in-house. After five years O&O Associates have estimated that this would rise to £1billion.[4] This would not only damage the UK production sector but close the door on future generations of entrepreneurs and new businesses who use their self- sufficiency and self-motivation to break into the UK broadcasting sector. It would also become an opportunity cost of £3.7billion to the sector over a 10-year period and an inevitably this would be a direct transfer of value

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[3] Channel 4's impact on the UK's International Competitiveness and Global Profile, O&O Associates, p18 2021
[4] Channel 4's impact on the UK's International Competitiveness and Global Profile, O&O Associates, p60, 2021

from SMEs across the UK to privately owned shareholders.[5] Within the context of the pandemic this is a serious risk to the recovery of the sector as it grapples with just under £500 million losses in revenue which is the figure we have just published under our Annual Pact Census.[6]. This year we have also published a Covid impact Study to understand the full impact of the pandemic on the UK production sector and as predicted it shows that smaller companies have been spending considerable amounts of reserves thereby impacting R&D and skills budgets. It is unknown how quickly the sector will get back to its former growth trajectory and the Government's plans to change the ownership of Channel 4 in its current state puts at risk any shoots of recovery that we are seeing in the sector particularly for smaller independents. All our commissioned research has been annexed to this submission with a summary overview for each piece explaining why it is important in relation to the potential change of ownership of Channel 4.

4. Pact considers that the optimum model for Channel 4 and the whole ecology of UK broadcasting is one that allows for the continued remit as a publisher broadcaster which prohibits Channel 4 from making its own programmes, the Terms of Trade, a commitment to diverse programming, a 50% nations and regions quota and market access for start-ups to break into the UK commissioning market. This is especially important given the impact of the pandemic. Any change to this remit, would have drastic implications for the UK's world-leading independent film and TV sector, impacting businesses and the 10,000 jobs that have been created and sustained across the UK. If this optimum model is changed there will be considerable risks that would need to be mitigated:

5. **Government has also made several assumptions about the TV Broadcasting ecology and Channel 4's role within it that Pact challenges with supporting evidence:**

Governments' assumptions on Channel 4's status as publisher broadcaster and its lack of access to capital are misguided and wrong primarily because:

5.1 Channel 4 can already access capital by using deficit financing that producers can bring to any programme's production budget.

5.1.1 Through deficit financing independent producers have played an important role in protecting UK PSBs from the full impact of increased programming costs. They have invested their own profits into programme development and production. This was further shown most recently when Pact commissioned O&O in 2019 to carry out research on the impact of the iPlayer changes on the TV production market. In that report it showed the gap between the tariff provided by the UK commissioner (BBC) and the actual cost of the series. Excerpts from the market impact assessment are shown below.

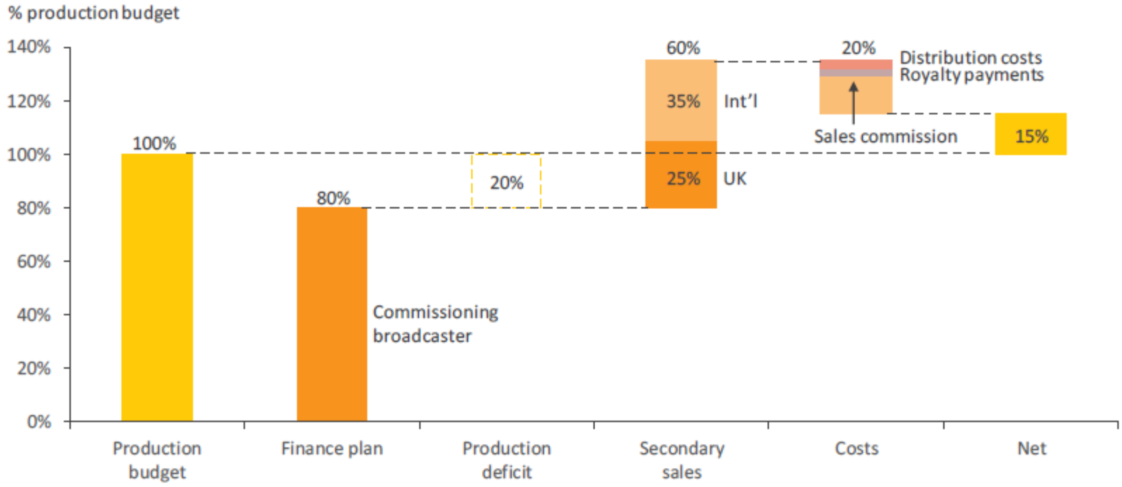
5.1.2 Figure 1 reviews the financing model for scripted content and comedy. This shows the gap finance that producers need to make up via their international sales in order to make the production budget and that in turn impacts their profit margin. It underlines the importance of secondary rights

[5] IBID

[6] Pact Census Independent Production Sector Financial Census and Survey 2021, O&O Associates, 2021

sales to the independent production sector's ability to complete the necessary finance for their productions. Research by O&O for Pact found that the UK's five main UK PSB networks (BBC1, BBC2, ITV, Channel 4 and Channel 5) have faced increased competition for audiences over the last 20 years, resulting in broadly flat revenues, and reduced real terms spending on original UK commissioning (a 13 per cent reduction in real terms between 2000 and 2018).[7] Despite this audiences have benefited as UK PSBs have been able to commission more high-quality original UK content at a lower cost because indies have bridged the gap in finance. During this period, there has been no lessening of the quality of UK content evidenced by its ability to win prizes, both at home and overseas.

Figure 1: Illustrative finance model for mid-range drama and comedy



Note: To protect commercially sensitive information, the programme titles used in the text are not necessary those provided to us by producers and may not be accurately represented by these finance model illustrations

Source: O&O analysis and estimates

5.1.3 By providing finance and taking on a greater share of the risk from broadcasters it reduces the cost of the primary licences to UK broadcasters. It is a cost-efficient way to access the global capital markets to ensure Channel 4 can access the capital it needs to commission high quality programming.

5.1.4 Industry estimates suggest that today only 55 per cent of BBC commissions are fully funded, with the remaining 45 per cent depending on co-production or deficit finance.

5.1.5 This willingness of independent producers to take more of the financial burden is not restricted to the large indies. Analysis of smaller indies in the UK suggests that on average they, as we have already identified, spend 4.5 per cent of their revenue on R&D, and only earn margins on UK production activity of around 2 per cent.[8]

5.1.6 Furthermore, it seems the Government already has the opportunity to increase the borrowing limit of Channel 4 as it is already within the gift of the Secretary of State to alter this limit. The Secretary of State and Government itself has decided to limit C4's borrowing capacity.

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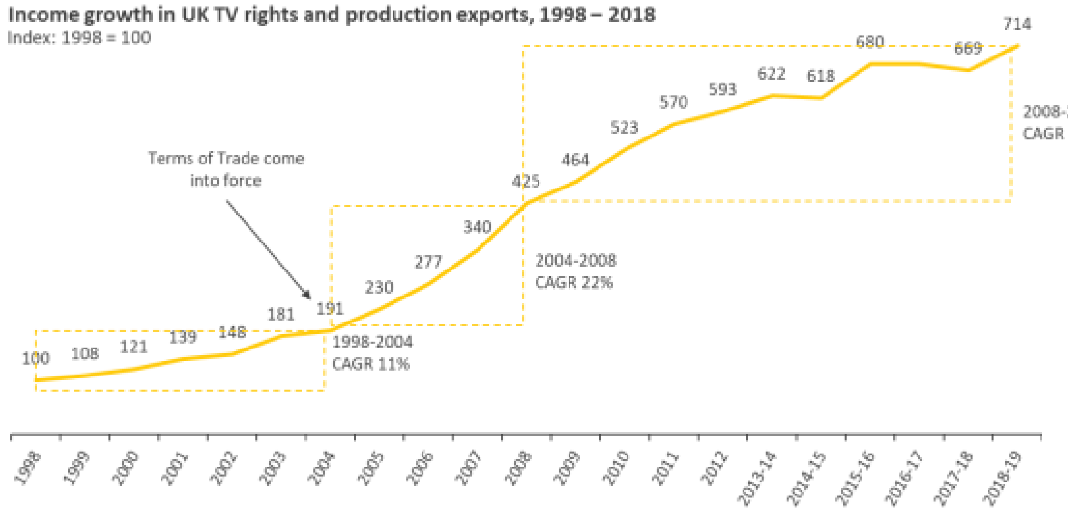
[7] Strengthening UK Culture and Creativity in a globalising TV marketplace, O&O Associates, 2020

[8] Call for Evidence PSBs and UK production sector, O&O Associates, 2021

5.2 Its status as publisher-broadcaster does not hamper its ability to keep up with a changing media landscape.

5.2.1 In a hits business it makes sense to source as many opportunities for success using a diverse supply.

Figure 2



Note: The reported periods in the source data changed from calendar to financial years after 2012 – the growth rate between 2012 and 2013-14 is therefore based on the restated 2012-13 equivalent
A change in methodology in 2016-17 used by Pact led to anomalous data
Source: BTDA, Pact, Oliver & Ohlbaum analysis

5.2.2 Independent producers are more incentivised to exploit their IP rights and there is a risk that Channel 4 would not know how best to exploit their own content. The table above highlights how after the Terms of Trade were introduced the revenues of indies began to increase by 22%. With rights under the control of producers it was in their own self-interest to push distributors to be more competitive with the terms they offered to secure the mandate to sell rights internationally. The previous five years before Terms of Trade were introduced there was half as much activity from the broadcasters. If Channel 4 were to make their own programmes there is a question mark whether it would have the tenacity and self-motivation equal to that of indies to exploit content rights.

5.2.3 Channel 4's status as a publisher-broadcaster also means it increases global format exploitation export revenue for the UK TV sector. Production companies have a greater focus on developing and producing local versions of formats with global appeal. By relying on the indie sector to source programming it also helps to keep overheads and programme costs to a minimum. With a shift away from the publisher- broadcaster model a decline in programme and format exports to the rest of the world is expected. This would be a lost opportunity to boost the UK's profile on the world stage as an open and confident nation, at a time when other states are investing in media to extend their soft power. As a proxy for the overall effect on the UK audiovisual sector, we can look at the GVA contributed by the sector before the introduction of the Terms of Trade in 2003. We might assume a gradual return towards this state, instead of the steady growth that has been seen. The ‘Film, TV, video, radio and photography’ sector had a GVA of £9 billion in 2001. In 2019, the ‘Film, TV and Music’ sector had a GVA of £21.7 billion (n.b. the methodology was changed in 2014).[9]

The advertising market is not broken and continues to survive - Government is overestimating the decline of free to air commercial advertising and has not accounted for the prospects of Total Video content advertising

5.3 Broadcaster TV remains the primary means of getting AV advertising seen for both 16-34s (77%) and all Individuals (91%)[10].

5.4 British advertising spend is set to increase by 18% to £27.7 billion with Broadcast TV continuing to play a significant part of this. TV ad spend is expected to increase by 15.1% in 2021 (a significant upward projection from the 8.8% forecast in April), reflective of increased activity during the Euros.[11]

5.5 ‘The total advertising spend market is growing at a rate of 5%[12] and the total video market (TV + Broadcaster Video on Demand (BVoD) + Online Video) is keeping pace with this and is forecast to grow at +5% per annum for the next five years and maintaining a share of total ad spend of 31% per year.’

5.6 TV advertising remains the medium of choice for big brands wanting to reach an audience quickly and at scale, with advertisers citing TV’s ability to drive both short-term sales and longer-term brand equity as a major advantage[13]

5.7 BVoD ad revenues grew by 15% year on year to £523 million, as broadcasters attracted more advertisers to these services. Commercial BVoD advertising now accounts for 13% of television advertising (excluding revenues from sponsorship and product placement) making up for the UK’s commercial public service broadcasters (including their digital portfolio channels) year-on-year decline of 14% in real terms in 2020, according to returns provided to Ofcom.[14]

Despite increased competition from VOD and VSPs resulting in a change in consumption habits Channel 4 is rising to the challenge and already has the tools necessary to build on its success

5.8 There is no denying that consumption habits are changing but the scenario that Government paints is not nuanced enough and risks overestimating the market forces that currently exist.

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[9] DCMS, *Sectors Economic Estimates*, 2019
[10] ThinkBox Research, 6th August 2021
[11] AA/WARC Expenditure Report, 2021
[12] WARC/AA Forceasts on AdSpend (£000s net.) (C4 response to PSB Review)
[13] Media Nations report, Ofcom, 2021
[14] IBID

5.8.1 Broadcast TV (live and on-demand) has the largest share of viewing across all audiences, and we expect this to continue as PSBs innovate and invest in their own VOD services. The total weekly reach of linear TV for individuals remains high at 85.5%.[2]

5.8.2 TV and BVOD viewing remains strong in lockdown (vs. pre lockdown) As time spent watching increases, TV and BVOD (combined) have seen an 11% increase in daily minutes from pre-lockdown.[3]

5.8.3 Among younger audiences, who favour on-demand, 'other online video' including social media is expected to outweigh SVoD towards the end of the decade. Again, such content is not generally in the same commissioning market segment as the PSBs such as Channel 4.

5.9 The Government has also already highlighted how Channel 4 is rising to this challenge by acknowledging: viewing amongst 16-34 year olds was 55% higher across the Channel 4 portfolio; that Channel 4 is the only PSB that attracts greater viewing amongst this age group and how Channel 4 has achieved a 26% increase in All4 views. And although viewing on the main channel has dropped to 5.9% from 11.9% in 2010 this has been relatively unchanged from 2013 when the initial decline in viewership occurred. Since then, Channel 4 has been able to adapt and continues to have the tools to meet the change in consumption habits. A key part of its recent strategy has been by agreeing a landmark content rights deal with our members to help it navigate this new digital era. Through the Terms of Trade Channel 4 managed to negotiate more royalty free uses in its own territory for a fixed term of three years. At the time of the negotiations Alex Mahon, CEO of Channel 4, commented that it would, 'For the first time, give us the full freedom to innovate with how the content created in partnership with indies appears across on-demand and channels.'[15] By negotiating with producers through the Terms of Trade it gives PSBs like Channel 4 the rights they need in order to attract audiences in the UK whilst rewarding producers for success and giving them long term sales revenue.

Growing production budgets across VOD platforms do not make it increasingly difficult for domestic players to access significant capital to support strategic investment to compete

5.10 As identified above PSBs like Channel 4 can access capital via third party funding which includes the independent production sector through deficit financing. PSBs like Channel 4 benefit from the higher budgets that SVoDs provide especially if they invariably co-produce content.

5.11 SvoDs are a relatively small commissioner compared to the PSBs and will remain so for the foreseeable future. PSBs spent £2.5 billion on UK originations in 2019, which is nearly nine times the £0.4 billion invested by SVOD. The PSBs delivered vastly more UK original content – over 32,000 hours in 2018, compared to 221

[2] ThinkBox Monthly TV viewing Report June 2021
[3] ThinkBox report based on IPA touchpoint data
[15] Pact press release, June 2019

hours of SVOD original productions made in the UK. We forecast that the PSBs will remain the most important source of commissioning for local, UK content for the foreseeable future. SVoDs also tend to source from larger indies with a turnover range of between £25-£50m and over £70m whilst Channel 4 has consistently sourced on average over 43% over five years of its content spend from smaller indies with a turnover of between £5m-£25m.[16] Crucially for indies starting out they are able to hold on to their IP rights with any Channel 4 commission whilst SVoD commissions tend to pay for rights outright. By holding onto their rights they are able to invest into skills, talent and idea development. Furthermore for smaller companies who lack a portfolio and deficit financing Channel 4 is more likely to be able to provide upfront financing compared to other PSBs for programming.

5.12 Co-production finance has become increasingly important as national broadcasters have sought to compete with the budgets available to global services.

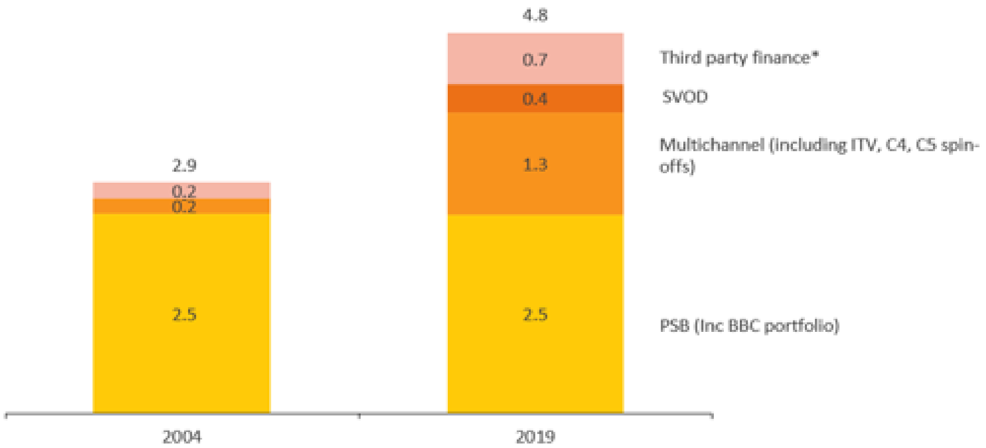
5.13 There are several different types of coproduction relationship, and these have become increasing complex in recent years.

5.14 The nature of the arrangement can vary significantly depending on the national or international footprint of the coproduction partner in question.

5.15 SVoD services are also experimenting with co-productions in exchange for UK secondary rights and global distribution (i.e. rights in all other territories). For example, Netflix co-produced Troy (produced by Kudos / Endemol Shine), and Black Earth Rising (Drama Republic) with the BBC, in exchange for distribution rights for all international territories and a reduction of the holdback period. Similarly in a Pact-commissioned report by O&O Associates they found that Channel 4 has also proved it can be competitive in the market through securing co-production deals and acquiring high profile content. Recent Channel 4 co-productions include It's a Sin with HBO Max and The End of the F***ing World with Netflix.. O&O goes on to note that 'independent producers have turned to third party financing and co-productions to make up the deficit from PSB financing, rather than moving away from PSB commissions.' Figure 3, shows how third party financing has grown at almost twice the rate of SVOD commissions between 2004 and 2019.

[16] Based on analysis from Pact Census

Figure 3 Total UK TV production investment, 2004-2019, £ billions nominal terms



*Note: Includes news, but excludes sports rights and inward investment (e.g. spending in the UK by US Studios on programmes made primarily for the US market). *2018 value*
Source: Ofcom, COBA, Oliver & Ohlbaum estimates and analysis

Illustrative characteristics of co-production deals might include:

- Share of production budget from UK commissioner: The primary UK commissioner, such as Channel 4, might contribute between a quarter and a half of the production budget in exchange for UK broadcast rights and potentially some BVoD rights for All4.
- Share of production budget from an SVoD co-producer: global SVoD services will sometimes offer significant financial incentives upfront, in exchange for global rights. This might include covering up to 75 per cent of the production budget.
- Other sources of finance: tax credits

5.16 The financial terms offered by global SVoD services can be attractive to producers. These services typically integrate the total perceived value of a programme into their up-front payment. This means producers can receive very high payments from SVoDs compared to broadcasters; removing much of the risk associated with content production. This, however, is at the expense of retaining the IP, which is either lost permanently, or for extended licence periods.

Channel 4 is already seizing the opportunities that technological changes bring to adapt and invest

5.17 As already identified through the recently negotiated Terms of Trade, Channel 4 now has the flexibility to utilise longer content windows across all its platforms. If Channel 4 wishes to expand into international markets and increase the hours of content available, the Terms of Trade are flexible enough to negotiate any new terms that require changes in a fair fashion. Channel 4 have also identified ways to build on the success they have achieved by : Setting a target to double All 4 viewing by 2025; investment in more in youth-skewing content to drive digital viewing, using deeper audience insights to find shows that drive streaming; the roll out personalisation features on All 4, including smarter recommendations; building on current partnership network and forge new arrangements to reach the right audiences; 4Studio to produce more original shorts and grow branded digital entertainment and the launch of the Global Format Fund to invest in new content formats with global potential.

C4's public service remit does not limit its ability to respond to the challenges outlined by Government

5.18 Channel 4's remit contains several things set out in legislation:

- *to provide a percentage of programming to be made in the Nations and Regions*
- *to not make its own programmes*
- *to provide programming for teenagers and children*
- *to meet its 25% indie quota*
- *a statutory public service remit which is the provision of a broad range of high quality and diverse programming which, in particular—*

   a) *demonstrates innovation, experiment and creativity in the form and content of programmes;*

   b) *appeals to the tastes and interests of a culturally diverse society;*

   c) *makes a significant contribution to meeting the need for the licensed public service channels to include programmes of an educational nature and other programmes of educative value; and*

   d) *exhibits a distinctive character.*

None of these obligations currently prevent Channel 4 from meeting the Governments' wider aims and priorities for PSB.

5.19 Channel 4's status as publisher-broadcaster and the indie quota means 100% of its programming can be sourced from independent producers with smaller producers also having a role in providing programming. Thereby ensuring a wide range of high-quality programming is provided to audiences which the Government has outlined as one of the objectives of a Public Service Broadcasting system.

5.20 Channel 4's obligations to provide programming from the Nations and Regions shows how it is contributing to this wider PSB aim of contributing to the cultural, economic and democratic life of the UK at home and abroad. O&O has also noted Channel 4 'is the only lever that can provide creative competition to the BBC in its own efforts to decentralise operations and production, so that both can drive and inspire the other in delivery of their public remits.' It also found that, 'ITV aims to keep the maximum of seventy-five per cent of commissioning in-house, while Channel 5 has a much lower Nations & Regions quota at the moment, at ten per cent. Non-PSBs have no such obligation at all, which has resulted in SVODs focusing UK investment in London and the surrounding areas in the south of England.'[17]

5.21 Channel 4's recent move to Leeds and its commitment to spend up to 50% of its commissioning spend out of London has a considerable impact in meeting Government's wider aim of using the PSB system to impact the wider creative economy.

5.22 Furthermore, the obligations do not stop PSBs like Channel 4 from rising to the challenges of large international players like Netflix and other SVoDs taking audience share. In 2020, Channel 4's main channel share grew by 7% year-on-year amongst 16-34-year-olds (to 8.6%), its highest figure since 2011, which is more than any other PSB. Share in the peak time hours of 7–11pm was 10.7%, the highest figure since 2007 amongst this demographic.

5.23 It's likely that if Government wanted to get rid of these remits it would mean their wider aims and priorities on PSB would not be met and be severely hampered by the false need to keep up with SVoDs.

[17] Channel 4's impact on the UK's International Competitiveness and Global Profile, O&O Associates, 2021

Consultation questions

Question 1. Do you agree that there are challenges in the current TV broadcasting market that present barriers to a sustainable Channel 4 in public ownership? Please provide supporting evidence.

Yes

No x

Not sure

1.1 Pact acknowledges that there continues to be technological changes in the UK audio-visual market. Audiences want to be able to access content whenever they like, wherever they are. That said, the changes should not be overstated. As a Pact commissioned report by O&O noted, 'Broadcast TV still accounts for the majority of viewing across all audiences and contributes the most revenue for the independent production sector – Channel 4 is at the heart of this. And it would be hasty to draw conclusions about the future of Channel 4 and other UK broadcaster revenues. Channel 4 has many levers it can pull under its current model and should be allowed to prove itself.'[18] Share of PSB viewership continues to be just under 50% of all hours watched by all adults in the UK whilst SVoDs represent 19% of viewing based on the last Ofcom Media Nations Report.[19]

1.2 The arguments set out in the Government's consultation overlook that fact that commissioning spend for UK producers predominately comes from PSBs and that SVoD commissions only account for 9% of indies' revenues.

1.3 Channel 4 continues to perform successfully, generating £985 million in 2019 and £934 million in 2020, only a 5% decline despite the challenges presented by Covid-19.[20] Channel 4 also saw increasing digital advertising revenue to a record £161 million, as a result Channel 4 was able to record a £74 million surplus in 2020, proving its ability to adapt to new market conditions.

1.4 Channel 4 has proven time and time again to meet the challenges of market dynamics and will continue to do so. For example, it is forecast to generate over £1billion in revenues in 2021. It has a robust plan via the Future4 strategy to:

- Double All 4 viewing by 2025
- Digital advertising to be at least 30 per cent of total revenue by 2025
- Non-advertising to be at least 10 per cent of total revenue by 2025

1.5 Channel 4 is already meeting the need to modernise through the flexible Terms of Trade. The current PSB framework including the Terms of Trade, has shown to be flexible and adaptive enough to cater to these new preferences by agreeing to new

[18] Channel 4's impact on the UK's International Competitiveness and Global Profile, O&O Associates, p21, 2021
[19] Media Nations Report, Ofcom , 2021
[20] Channel 4, *Annual Report*, 2020

Terms of Trade that will allow PSBs to utilise content in longer windows. As identified above Channel 4 recently signed up to a landmark deal with Pact and producers across the industry to increase the window for content on their platform. That said, distribution is not the sole challenge to be faced by PSBs. Pact considers that the issues that face PSBs are focused on editorial and content in a more competitive market for audiences - especially younger viewers - which has accelerated due to the COVID-19 crisis.

1.6 One of the main things Government can do to help PSMs like Channel 4 is increasing the prominence of PSBs within a smart TV envrionment and this has been an issue that Government has delayed for some considerable time. That said, we welcome the news that this will be imminently legislated for under the Broadcasting White Paper and we hope it will outline in detail how PSBs including Channel 4 will benefit from more prominence and under what terms.

1.7 Ofcom has also not directly raised any concerns in their PSM statement. Pact considers that if there were any significant challenges that Ofcom would have noted this in their report on Channel 4 and made recommendations. While there are challenges for all PSBs, including C4, Channel 4 has shown they can adapt to market changes and maintain a healthy balance sheet. For example, on advertising Commercial PSBs are making up for the decline in linear advertising by seeing an increase in BVoD advertising.

Question 2. Would Channel 4, with a continued public service broadcasting licence and remit, be better placed to deliver sustainably against the government's aims for public service broadcasting if it was outside public ownership? Please provide supporting evidence.

Yes

No x

Not Sure

2.1 Pact considers that the answer to this question depends on what the Government deems is the PSB licence and remit for Channel 4. Under the current remit it would seem that public ownership is the best way to sustainably deliver the Government's aims for PSB.

2.2 Channel 4 is already accessing high quality programming by commissioning production companies who utilise the markets to bring additional finance to programme budgets.

2.3 In their recommendations to Government regarding the future of PSM, Ofcom stated the importance of supporting the creative economy/indies and recommended that a new PSM remit should include 'a new objective to support the UK's creative economy.' Channel 4 are already doing this and privatising C4 would likely weaken their support for the creative economy. Maintaining the current remit is unlikely to work with privatisation and elements would either completely be removed or severely curtailed.

Question 3. Should Channel 4 continue its contribution to levelling up the regions and nations of the UK through retaining a presence outside London and a strengthened regional production remit? Please provide supporting evidence.

Yes x

No

Not sure

3.1 Pact considers that a full impact assessment must be outlined to understand what a strengthened production remit would do to the market. Pact notes that the shift to commissioning 50% of Channel 4 commissions outside of London by 2023 is making a noticeable difference to jobs and the economy quota. Channel 4 commissioned EY to look at the impacts of Channel 4 spending across the UK and found that it is already making progress on this commitment: spend for its main channel on commissions from the Nations and Regions was 47% in 2020.[21] Furthermore the spend within the Nations and Regions has a GVA contribution of £274m.

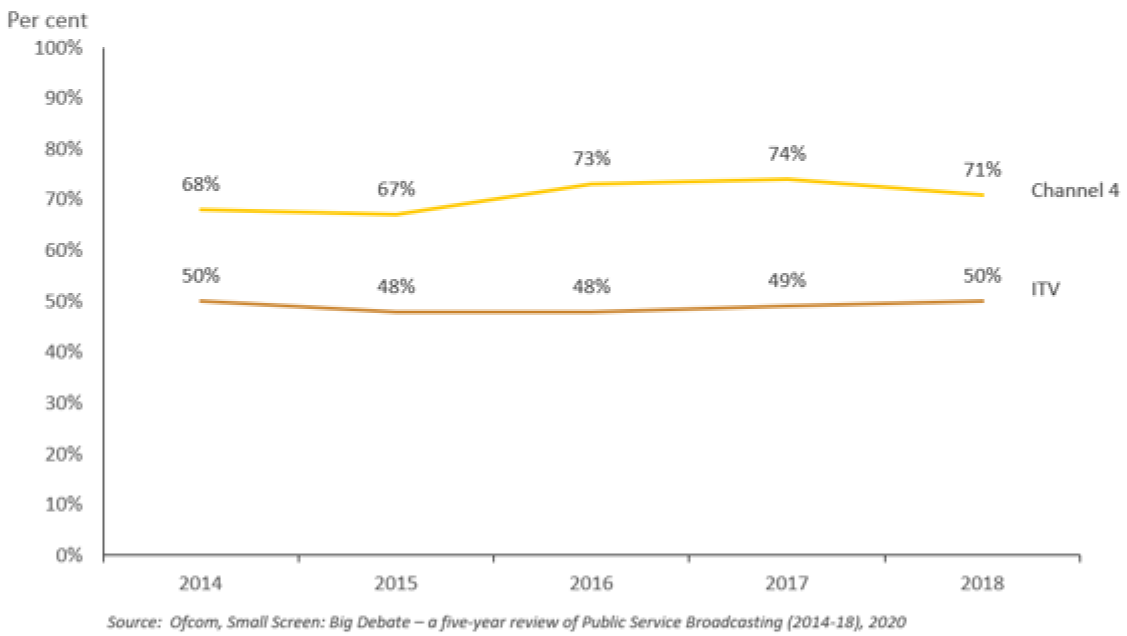
3.2 Channel 4's investment in N&R indies and their growth in the last decade alone stands at over £1.5 billion on content spend within the Nations and Regions. Most recently it has also committed in its '4 All the UK' strategy a voluntary commitment to increase its content spend in the Nations and Regions by up to £250 million by 2023. Channel 4's move to Leeds is also a considerable investment that the area and wider region will reap the benefits.. As part of its '4 All the UK' strategy, Channel 4 relocated its National HQ to Leeds and they have created regional creative hubs in Bristol and Glasgow, as well as an advertising sales house in Manchester. It is estimated that Channel 4 will deliver £1 billion in Leeds over the next 10 years and create 1,200 jobs.[22] A range of commissioners from key genres including Daytime, Drama, Factual, Specialist Factual and Sport will be based in Leeds. Channel 4's Emerging Indie Fund, Indie Growth Fund and 4Studio, which commissions and produces content for social media, will also be based in the city. Other TV companies are also following Channel 4's lead and opening offices there, including independent producers The Garden and Wise Owl/All3Media, Pact and Sky Studios, as well as the UK's first Centre of Screen Excellence. True North has also expanded its post-production facilities in Leeds.

3.3 Pact notes that any private owner would want to change any of these obligations, and it can't be guaranteed that these opportunities for investment would remain or increase once the ownership is changed. This is especially the case if the new owner sought new profit-maximising incentives by finding cost synergies and reducing broadcaster competition in the case of a merger. A Pact-commissioned report by O&O Associates found as shown in Figure 4, ITV's content spend as a proportion of broadcast and online revenue has consistently been lower than

[21] Channel 4's contribution to the UK, EY Report for Channel 4, April 2021
[22] Channel 4, *4 All the UK Case Studies*, 2020

Channel 4. Therefore, they have assumed these two forces will offset each other and the overall content spend will remain flat if that.

Figure 4 Programme spend as a proportion of broadcast and online revenues, Channel 4 and ITV



Question 4. Should the government revise Channel 4's remit and obligations to ensure it remains relevant in an evolving broadcast market? If yes, what changes should be made (which could include new freedoms or changes to its obligations)? Please provide supporting evidence.

Yes

No x

Not sure

4.1 considers that despite the changing media landscape Channel 4 is well equipped to navigate the changes and already narrowed the gap it has seen in linear advertising by shifting its efforts on a digital first strategy. This has seen impacts on its revenues as BVOD advertising has increased by 11% on 2019 this year. It is the most successful youth skewering VOD platform in the world and it continues to be relevant– on-demand viewing increased by 26% in 2020 and up >30% over 2021 Year to Date.

4.2 Channel 4's remit and obligations are what make it so popular – it has a commitment to taking risks, innovation and diversity and not to shareholders. This is still important.

4.3 As we have outlined above the obligations and remit of Channel 4 do not stop it from continuing to meet the challenges of the dynamic market. The obligations found within the Terms of Trade in particular have shown to be enough for Channel 4 to agree terms which enables them to make the most of the content it commissions.

Question 5. Should the government remove the publisher-broadcaster restriction to increase Channel 4's ability to diversify its commercial revenue streams? Please provide supporting evidence.

Yes

No x

Not sure

5.1 If Channel 4 were to set up a production arm this would remove opportunities from the smallest of producers in the UK. Slots would be freed up to suit its own production arm. Not only would this impact those producers who would ultimately lose out on those slots, but it would come with a considerable weakening of the wider audio visual ecosystem within the UK. The delicate balance of legislative and regulatory interventions has led to the creation of a broadcasting ecology here in the UK which is internationally recognised as one of the most dynamic, innovative, creative and diverse in the world. A range of organisations with different business models, incentives and sizes within the UK mean that there is strong competition between the PSBs and between PSBs and commercial operators. This combination of public and commercial forces is essential due to the UK's comparatively small home market. Changing any part of the ecosystem and upsetting its balance is a huge risk. As O&O noted in a Pact-commissioned report, 'Channel 4 invests c.70 per cent of its revenues from broadcasting and online in content, while ITV reinvests around c.50 per cent (pre-Covid).[23] While the proportion that Channel 5 reinvests in content is higher than ITV's, its overall revenues are around a third of Channel 4's and so its ability to drive the sector forward is reduced. We also understand that its upfront investment in programmes is lower than Channel 4's, requiring the independent to plug the funding gap. This is less feasible for newer or smaller independents in particular, which can't spread risk across a portfolio of projects.'[24]

5.2 Channel 4 would also likely have to cut back on investment to make programmes, production is a hit driven business and hits are not guaranteed. BBC Studios/ITV Studios have an advantage already and Channel 4 would not have the decades experience of in-house production that the two entities have amassed along with a back catalogue. It could take many years to get a hit, and this would likely be at the expense of the indie sector.

5.3 In the report Pact commissioned O&O to produce it also found that Channel 4 does not have the same function in the market as other commercially owned and commercially funded PSBs. O&O argue that although some consolidation within the market is helpful for some broadcasters as in the case of ViacomCBS and Channel 5 it does not mean that the same should follow suit for Channel 4. It found that a move to consolidation would in fact weaken the current fulfilment of the Government's policy objectives for PSB and that it is the very fact that Channel 4 has no internal conflicting incentives between in-house studios and supporting the

[23] Ofcom, *Small Screen: Big Debate – a five-year review of Public Service Broadcasting (2014-18)*, 2020
[24] Channel 4's impact on the UK's International Competitiveness and Global Profile, O&O Associates, 2021

indies sector through access to IP through the Terms of Trade that allow it to fulfil the government's policy objectives.[25]

The indie development and production cycle with Broadcasters

5.4 Through owning their intellectual property (IP) rights, indies are able to invest in the development and production cycle at several key stages. Alongside investment in R&D, producers also invest in the training and recruitment of new and existing employees as their businesses scale-up and grow. This also benefits broadcasters like Channel 4 as these employees often go on to work for them and bring in the skills and expertise learned at production companies. Ensuring the sector has a suitable supply of highly skilled workers in a range of genres to meet demand is vital for the whole broadcasting ecology in the UK. Which is why producers, and the broadcasters, contribute to training schemes such as the high-end TV skills fund, animation skills fund, children's TV skills fund, and the TV skills fund all run by ScreenSkills.[26] The high-end TV skills fund, for example, has raised over £17 million since it was established in 2013, and productions such as *The Crown, Killing Eve,* and *Sex Education* have all paid into the fund.

Development

5.5 The first stage of the production cycle is in research and development (often referred to as R&D). It is extremely expensive and time consuming to invent, research and develop programme ideas to a stage at which they might be commissioned. For example, high-end drama, which requires scripts and talent attachments to the project can cost an estimated £297,000. Whereas comedy, which often requires a pilot script or episode outline, can cost an estimated £223,000.[27] Independent producers invest millions of pounds in R&D each year, which brings considerable benefit to the UK PSB ecology. Very little of this is ever recouped, with many projects developed and never commissioned.

5.6 If a broadcaster is interested in a project, it might put some money towards the cost of funding development. Channel 4's upfront investment is usually higher than Channel 5, which helps smaller producers who may lack a wider portfolio to spread risk. This investment in effect locks the producer out of the market in terms of preventing the idea being taken elsewhere while the original broadcaster is considering it.

5.7 If a producer accepts development funding from a broadcaster before it receives a commission, this opens the door to further dialogue with the commissioner, which is valuable to the production company. However, pilots and other forms of development are often expensive, and it is extremely rare for the producer only to use the broadcaster's money in development. In order to try to win a commission in this highly competitive industry, the producer will often add their own investment into funding further development. If the project is commissioned, it is likely that they

[25] Channel 4's impact on the UK's International Competitiveness and Global Profile, O&O Associates, 2021
[26] Further information on ScreenSkills funds and training can be found here: https://www.screenskills.com/industry/

[27] From Pact discussions with distributors

will be able to recoup. However, if the idea is not commissioned, the producer is liable for the full costs of the development and must also repay the broadcaster who originally put in the development funding if their idea is commissioned at a later date by a different broadcaster. It is unlikely that the new broadcaster would pay the full cost of the earlier development, thereby leaving the producer out of pocket for the money which they invested, even if the programme is eventually commissioned.

Production

5.8 Moving from development to the production process, it is becoming increasingly rare for a UK PSB to pay for the whole cost of producing a television programme. For example, in a commissioned piece of research O&O found that ‘Industry estimates suggest that today only 55 per cent of BBC commissions are fully funded, with the remaining 45 per cent depending on co-production or deficit finance.’[28]

Distribution Exploitation

5.9 The commissioning broadcaster will often pay for a percentage of the programme budget – the amount varies widely, depending on the genre – and the producer will fund the deficit through presale agreements and by investing money which it calculates it will be able to make back from finished programme sales. Distributors often invest a certain percentage of the production budget as part of presale agreements.

Question 6. With reference to supporting evidence, what would the economic, social and cultural costs and benefits of Channel 4 moving out of public ownership be on:

a. overall audience experience?
b. the Channel 4 Television Corporation itself?
c. investment in the independent production sector?
d. investment in the independent film sector?
e. the TV advertising market?
f. investment in the creative industries sector more widely?
g. competition between Channel 4 and other PSB and non-PSB channels?
h. the regions and nations of the UK?

6.1 Pact considers that this is difficult to answer without knowing what the full terms of moving Channel 4 out of public ownership would entail. In its current status with its current remit and obligations any move towards changing the ownership of Channel 4 would entail costs. Pact has focused on those costs that it is most concerned about below.

Economic costs

[28] IBID

6.2 Any change of ownership would be a threat to our world leading production sector:

6.3 The opportunities for emerging indies to break into both domestic and international commissioning market will be curtailed.

6.3.1 With any move to private ownership and with a subsequent loss of publisher broadcaster status and the shift toward in-house production would lead to less opportunities for the independent production sector. As already outlined, we would see an economic impact on the independent production sector amounting to £3.7 billion loss over a ten-year period starting with an initial £80 million of value lost in the independent production sector.[29]

6.3.2 Channel 4 is one of the few network broadcasters that can take risks on emerging UK talent that have no network credits thus creating the opportunity for new indies to break into the domestic broadcasting market. This is because risk taking, and innovative content, sit at the heart of Channel 4's public service remit as set out in the Communications Act 2003. This initial break into the domestic market then can be built upon by small businesses who through their own self-motivation can use the network credits to gain international commissions.

6.3.3 The seed funding by way of commissions from Channel 4 will be lost impacting the long tail of opportunities that this investment represents. A Pact-commissioned report by O&O Associates found that Channel 4 had many of the features that are commonly associated with the Government-led initiative called 'sandboxes' which are used to drive innovation and risk taking through the use of developing and testing new products and services within the private sector. Whilst Channel 4 is not a regulatory sandbox it has been driving innovation and experimentation by operating as a seed fund to take risks on programming. For example, O&O have estimated that, 'between 2006 and 2019, 195 new production companies became successful businesses following initial commissions from Channel 4,' and that they now are estimated to 'generate around £380 million in revenue per year across both PSB and non-PSB commissions.' The O&O report commissioned by Pact also found that Channel 4 commissioned seven of the top 25 best selling formats internationally in 2019. One of which 'Come Dine with Me' has generated over £40m of revenue over the lifetime of the programme. This comes back to further fund future jobs and projects back in the UK TV market.

6.3.4 O&O also found that Channel 4's focus on commissioning from small businesses and start-ups in particular drives the economic cycle of the sector. They noted that 'all PSBs and other UK commissioners then benefit in terms of lower commissioning costs, access to deficit funding by independents and increased investment in R&D and skills and training'.[30] It is unlikely that a private owner would continue to take the kind of sustained risks that Channel 4 maintains in supporting the indie sector.

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[29] Channel 4's impact on the UK's International Competitiveness and Global Profile, O&O Associates, 2021

[30] IBID

6.4 A change of remit is a threat to jobs and the Government's levelling up agenda, not only production jobs but also freelancers, locations, caterers, post-production houses etc.

6.4.1 Channel 4 contributed £992m to the UK economy in 2019 including £274m to the regional economy representing 30% of Channel 4's indirect and induced GVA contribution to the UK. This supported around 10,600 jobs across the UK in 2019, of which nearly 3,000 related to jobs supported by Channel 4 in the Nations and Regions.[31]

6.4.2 It also generated £65m of GVA in the devolved Nations (Scotland, Wales and Northern Ireland), representing 24% of the indirect and induced GVA it generated in the Nations and Regions.[32]

6.4.3 The Government has not signalled any firm commitments to maintain the current Channel 4 remit on Nations and Regions. Take this remit away and the GVA wealth that we currently see cannot be guaranteed. If this remit were to impede a sale it is most likely that any Nations and Regions remit would be watered down or abandoned. Pact considers that this goes against the Government's wider objectives on Public Sector Broadcasting and particularly its agenda to support the wider creative economy. This would also abandon the previous investment of public money and the many partnerships with public and private sector which have enabled the sector to flourish under the policy. Under a privatisation Channel 4 may choose to buy the kind of companies like BBC/ITV/Sky etc have chosen to do – which may lead to a more consolidated marketplace and loss of Terms of Trade for indies. Given Government's focus on levelling up and SMEs, this likely consequence would mean it would be harder for the Government to deliver on its levelling up policy objectives.

6.4.4 We understand that based on a Channel 4 commissioned report by EY the Nations and Regions could also be disproportionately affected by privatisation, particularly if Channel 4's regulatory quota for content made in the Nations and Regions is not increased to reflect its current levels of spend in the Nations and Regions. The report found that 'Channel 4's contribution to GVA through its supply chain 8 in the Nations and Regions could reduce by 43% (£1.2bn) over a ten-year period. Similarly, we estimate that jobs supported by Channel 4 in the Nations and Regions each year (both directly and in its supply chain) would reduce by 60% (2,300 fewer jobs supported each year) compared to a scenario where Channel 4 is not privatised.'[33]

Cultural costs

[31] IBID
[32] EY Report for C4 2021
[33] Assessing the impact of a change of ownership of Channel 4, 2021

6.5 A change in ownership would also be a considerable threat to the diversity of programming within TV and film seen within the UK and the skills development that Channel 4 contributes to the sector:

6.6 Channel 4's requirement to commission 'distinctive content' has meant shows that are culturally reflective of the UK but not necessarily fitting the editorial themes of the BBC or ITV have found a home at Channel 4. Channel 4 has taken on risks on new and upcoming indies. Channel 4 commissioned more small production companies (those with a turnover of less than £10 million) than the other PSBs over a five year period between 2015 and 2019.[34] The data also shows that Channel 4 commissioned more than twice the number of small production companies at ITV.[35]

6.6.1 This is also further evidence of the healthy competition that exists within the UK PSB Broadcasting ecology whereby production companies and broadcasters compete with each other to get the best possible ideas on screen. As a result UK audiences currently enjoy a varied and rich array of content across the PSBs. Channel 4 plays a key part in this competition. O&O's research on Channel 4 found that, 'Depending on who a future owner is, reduced competition and reduced variety in the UK broadcaster ecosystem, including in terms of incentives and remits, could gradually lead to lower total content investment and more homogenous output across UK broadcasters over time.'[36] In turn O&O found that a decline in the independent production sector would deprive any Channel 4 in-house studios of their source of creative renewal through acquisition and investment in indies. 'This creates the risk of production for UK broadcasters focusing on low and mid-range content for local audiences, while the high end is global and doesn't genuinely reflect values, culture and voices from across the UK.'[37]

6.6.2 Innovative, distinct and edgy content that is directly relevant to those in the UK would be lost especially if commissioning had to cater to shareholder demands. Channel 4's requirement to commission 'distinctive content' has meant that programmes which are culturally reflective of the UK (but not necessarily fitting into the themes of the BBC or ITV) have found a home on Channel 4. Shows such as *It's a Sin* and *The Undateables* have been popular whilst also promoting underrepresented voices across the UK. Commissioning shows such as these has given Channel 4 a long-standing reputation for commissioning shows that tackle subject matters that others won't. This was acknowledged by Andrew Mitchell, Conservative MP for Sutton Coldfield in a debate on Channel 4, ''Channel 4 caters for minority tastes and diversity in modern Britain… It aids inclusivity.'[38]

6.6.3 Commissioning programmes that reflect UK life and culture has had a positive impact on C4 viewers. Viewing amongst 16–34-year-olds was 55%

[34] Channel 4's impact on the UK's International Competitiveness and Global Profile, O&O Associates, p16, 2021
[35] IBID
[36] Channel 4's impact on the UK's International Competitiveness and Global Profile, O&O Associates, 2021
[37] IBID
[38] Andrew Mitchell, Parliament debate on *Channel 4: Privatisation*, 2021

higher across the Channel 4 portfolio; that Channel 4 is the only PSB that attracts greater viewing amongst this age group and how Channel 4 has achieved a 26% increase in All4 views. And although viewing on the main channel has dropped to 5.9% from 11.9% in 2010, this has been relatively unchanged from 2013 when the initial decline in viewership occurred. O&O have found that, 'By taking risks to commission programmes that feature challenging subject matters and promote underrepresented groups, Channel 4 puts important issues at the centre of the public eye and helps to normalise subjects that were previously considered controversial. This then promotes the UK on the global stage as a forward-thinking country that is creatively and culturally ahead of the curve.'[39]

6.7 A move to privatisation would also have considerable costs to the UK film industry. Channel 4 has been a champion and crucial part of the British film sector providing early backing for many films that would not have happened had it not been for Channel 4 seeing the potential. Much of this is because of Channel 4's remit which has a duty to make, broadcast and distribute high-quality films, intended to be shown to UK audiences, and broadcast and distribute films (including third party films) that reflect cultural activity in the UK to audiences (a requirement that is satisfied by the activities of Film4).

6.7.1 Films supported by Film4 often showcase the diversity of contemporary life in the UK and represent different aspects of UK culture to the rest of the world. If the Government choose to water down the remit to suit a buyer's preference, it will mean losing the £114m investment in films shot predominantly in the Nations and Regions since 2013, comprising 20% of the full production budget for these films.[40]

6.7.2 A channel 4 commissioned report by EY in April also noted that, 'Talent supported by Film4, who have gone on to have globally-recognised careers, can also be recognised as UK exports, representing the UK to the rest of the world as a diverse creative hub. Some examples of globally-recognised UK talent directly supported by Film4 and Channel 4 throughout their careers include Steve McQueen, Andrea Arnold, Martin McDonagh and Daniel Kaluuya.'

6.7.3 Whether the creative risk taking associated with Film4 would carry on under new ownership remains to be seen especially if shareholders demand a set target on investments. It is likely that private ownership would change Channel 4's approach to risk and thereby cut back on its backing of innovative risky ventures involving under represented groups and focus more efforts on more established talent. This would be a detriment to the cultural fabric of the UK film industry.

6.8 Channel 4 has invested in hundreds of independent production companies over the nearly 40 years of its existence, enabling and improving access, skills, international activity and diversity.

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[39] IBID

[40] Channel 4's contribution to the UK, EY, April 2021

6.8.1 At a time when our sector is busier than ever, we need to attract new, diverse talent for the future and a broadcaster that is committed to continuing to commission new voices and ideas as a principle of its remit.

6.8.2 Channel 4 plays a key role in developing talent and investing in skills and training. Many producers or other talent start their careers at Channel 4, who have the capital to invest in skills and training on a wider scale than some smaller indies themselves. Producers then take the skills they have learnt and often go to set up their own production companies, creating jobs and helping to stimulate investment in the local creative economy.

6.8.3 A report commissioned by Channel 4 by EY has recently noted ' Since its inception, the Indie Growth fund has made 25 investments and there are now 15 companies in the portfolio'. [41] Furthermore, 'The Alpha Fund invested £385,000 per year in Nations and Regions production companies in 2018 and 2019. This investment included six companies in Scotland in 2018 (total investment of £90,000) and seven companies in Scotland in 2019 (total investment of £97,000).[42]

6.8.4 Other examples of Channel 4's investment into training schemes to support the development of talent across the Nations and Regions in particular include:

- **4skills** – launched in 2020 to provide entry-level opportunities to people from across the Nations and Regions to break into the TV industry, , including the relaunched Channel 4 Production Training Scheme, Channel 4 Apprenticeships, 4Studio Placements, and the Aspiring Solicitors partnership
- **Production Training Scheme** – paid placements for people from backgrounds that are currently underrepresented in the TV industry at production companies across the Nations and Regions (jointly paid for by Channel 4 and the production company)
- **Apprenticeship Scheme** – apprenticeships for people to spend 14-24 months attached to a Channel 4 department in Leeds or Manchester.

Again whether a private owner would continue this level of support remains to be seen but there is a great risk that this infrastructure would be lost if Channel 4 were to be privatised.

[41] IBID
[42] IBID