

CONFIDENTIAL



1 March 2011

Rt Hon Jeremy Hunt MP
Secretary of State for Culture, Olympics, Media and Sport
Department of Culture, Media and Sports
2-4 Cockspur Street
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Colin Bowe
Chairman

Ed Richards
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Dear Jeremy

News Corporation / BSkyB proposed merger: further advice on revised UILs

We are writing as requested in your letter of 17 February 2011, to provide you with our advice on whether a revised set of proposed undertakings (UILs) provided by News Corporation on 28 February 2011 addresses the potential impact on media plurality of its proposed acquisition of the shares in British Sky Broadcasting Group plc (Sky) it does not already own, as identified in our report of 31 December 2010.

Background

In our previous report of 31 December 2010, we noted that the proposed transaction would result in Sky ceasing to be a distinct media enterprise from News Corporation. We considered both external and internal plurality and a range of measures to assess the effect of the proposed transaction, including:

- **Audience share and reach within individual platforms** - Following the transaction, News Corporation would be the only news and media provider present on all four media platforms at the wholesale level (TV, newspapers, online and radio). At the retail level, it would be one of three providers of UK-wide news and current affairs on three of four platforms (alongside the BBC on TV, radio and online and Northern & Shell on TV, newspapers and online).
- **Consumers' consumption of news** - We considered the parties' position in respect of their share of 'news minutes' consumed. This suggests that the proposed acquisition would see News Corporation consolidate its second place in terms of news consumption (rising from 14% to 24% including wholesale news provision). This compares to the BBC, which has news consumption of 44% of minutes and DMGT which is third with 9%.

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- **Primary research on consumers' claimed use of different media** - The proposed transaction would be a combination of the second and fourth largest providers based on our research into share of all references for news providers. For example, News Corporation's potential ability to influence would increase with the addition of Sky News, increasing its share of references from 12% to 22%. News Corporation's reach as a percentage of regular news consumers would increase from 32% to 51%.

By considering these measures, we concluded that the proposed transaction would result in an increase in News Corporation's ability to influence public opinion (through Sky News). This indicated a change in the concentration of media ownership which would be likely to affect sufficient plurality.

Our advice, based on the evidence and reasons set out in our report, was that we reasonably believed that the proposed acquisition may be expected to operate against the public interest since there may not be a sufficient plurality of persons with control of media enterprises providing news and current affairs to UK-wide cross-media audiences.

We therefore recommended a fuller second stage review of these issues by the Competition Commission to assess the extent to which the concentration in media ownership may act against the public interest.

On 25 January you announced that, following meetings with Ofcom and News Corporation, you intended to refer the merger to the Competition Commission, considering that it may be the case that the merger may operate against the public interest in media plurality. However, before doing so, you said that it was right that you consider undertakings in lieu (UILs) offered by News Corporation.

You requested Ofcom to advise you on the extent to which the proposed UILs address the potential impact on media plurality identified in our 31 December report. You separately asked the OFT to advise you on whether the proposed UILs would be practically and financially viable and effective, in relation to which we have, as requested, assisted the OFT in light of our sectoral expertise.

We wrote to you on 11 February 2011 with our views on News Corporation's UILs, which propose to separate Sky News into a new company – 'Newco'. In that letter, we detailed the importance of suitable governance measures being put in place as a result of the UILs given the fundamental commercial dependency of Newco on a merged News Corporation/Sky entity.

In our view, these UILs did not provide sufficient assurances on such governance arrangements to address our previously expressed concerns on the impact on plurality from the proposed transaction. However, we noted that the proposed UILs may represent a way forward in principle, subject to resolution of some key outstanding points and on further negotiation relating to the detail of the arrangements.

Following advice from Ofcom and the OFT, you received assurances from News Corporation that it was willing to address the outstanding concerns. On 17 February you asked us and the OFT to work with News Corporation on a revised set of UILs.

Following further discussion, News Corporation offered revised proposed UILs that are attached in full to this letter.

Revised proposed UILs

In our letter of 11 February, we had indicated that in light of Newco's commercial dependence on News Corporation, the following outline set of governance measures would be needed in addition to the measures offered in the original proposed UILs.

- The Board of Newco should consist of a majority of independent directors, "independent directors" being directors who have no other News Corporation or News Corporation associated interest;
- The Board of Newco, including the independent non executive directors, should have a combination of both senior editorial and business experience/expertise;
- The Chairman of Newco should be an independent non executive;
- There should be a sub-committee of the Board of Newco to oversee editorial independence and integrity of Newco's services ("the Board Editorial Committee").

In addition, we noted that the OFT had a number of remaining concerns relating to the practical and financial viability of the initial UILs. These concerns were relevant to our plurality concerns, and in our view would also need to be satisfactorily addressed in any final UILs.

Taking each of these points in turn, the revised UILs, received in final form on 1 March 2011, now propose as follows:

- a majority of the Newco board of directors will be independent, being directors who have no other News Corporation or News Corporation associated interest (UILs 3.1(iii) and 10.4);
- the Chairman of the Newco board will be an independent director (UILs 3.1(iii));
- the articles of association of Newco will provide that the board of Newco and its committees shall have the appropriate balance of skills, experience, independence and knowledge of Newco to enable them to discharge their respective duties and responsibilities effectively and that at least one Independent Director must have senior editorial and/or journalistic experience (UILs 3.1(v));
- the articles of association of Newco will provide that Newco's Sky News TV, radio and any closely related services (irrespective of the platform on which such service is distributed) will abide by the principle of editorial independence and integrity in news

reporting and, where appropriate, will comply with the Ofcom Broadcasting Code (UILs 3.1(ii)). The reference to closely related services is to ensure that the provision of text content alongside audiovisual content does not provide a mechanism for editorial influence that could affect the editorial independence and integrity of Newco news services; and

- Newco shall have a Corporate Governance and Editorial Committee, key points of whose terms of reference are defined in the articles of association. This committee would oversee and report to the full board on compliance with the principles of editorial independence and integrity in news reporting and compliance with Ofcom's Broadcasting Code (UILs 3.1(viii)).

Under the revised proposed UILs, the provisions in the articles relating to independent directors and the editorial committee would no longer apply if News Corporation acquired more than 50% of the shares in Newco (even though News Corporation might not have the 75% control of voting required to amend the articles of association of Newco).

However, News Corporation's share in Newco would be limited to 39.14% and it would require your prior approval to acquire any more (UILs 6.1).

In offering our advice in relation to the revised proposed undertakings we assume that you or any successor would consult both publicly and with Ofcom and the OFT before agreeing to any change which proposed to permit News Corporation to increase its shareholding above 39.14%.

We understand that if you are minded to accept these revised proposed UILs you will consult on them (as would also be required by statute for any future changes to or termination of the UILs). If you decide, subject to the outcome of the public consultation, to accept the UILs, we consider that further negotiation with News Corporation may be necessary on the precise terms of contracts outlined within them which require your prior approval. It is important to note that the financial and practical viability of the revised proposed UILs and their effectiveness in addressing our plurality concerns will depend on the detail of the arrangements.

As you are aware, the revised proposed UILs effectively run for a 10 year period. As we set out in our letter of 11 February 2011, we have advised the OFT that we consider that a carriage agreement of a 10-year term in the context of market dynamics in this sector is long term. This is because we consider that there is likely to be significant evolution of the market and consumers' use of news and current affairs over the next decade. As a result, the situation with regard to plurality may be significantly different in 10 years time.

However, in this context, we would like to restate and emphasise our advice, set out in our report of 31 December 2010 and our letter of 11 February 2011, that the Government should consider undertaking a wider review of the statutory framework to ensure plurality in the public interest in the longer term. We believe that the current system is deficient in failing to

provide for intervention to be considered where plurality concerns arise in the absence of a corporate transaction involving media enterprises.

Our advice

We have seen a draft of the OFT's further advice to you in relation to the financial and practical viability of the revised proposed UILs. We agree with the OFT's position.

In conclusion, and with reference to the points set out above, we consider that the revised proposed undertakings would address the plurality concerns identified in our report of 31 December 2010.

Yours over,



Colette Bowe



Ed Richards

Enc

cc. *Clive Maxwell, Executive Director, OFT*