HOUSE OF LORDS

Revised transcript of evidence taken before

**The Select Committee on Communications**

Inquiry on

# THE SUSTAINABILITY OF CHANNEL 4

*Evidence Session No. 2* *Heard in Public* *Questions 22 - 40*

TUESDAY 19 APRIL 2016

3.35 pm

Witnesses: David Elstein

Colin Browne and John McVay

USE OF THE TRANSCRIPT

1. This is a corrected transcript of evidence taken in public and webcast on www.parliamentlive.tv.

Members present

Lord Best (Chairman)
Earl of Arran
Baroness Benjamin
Baroness Bonham-Carter of Yarnbury
Lord Goodlad
Lord Hart of Chilton
Baroness Healy of Primrose Hill
Baroness Jay of Paddington
Baroness Kidron
Lord Sherbourne of Didsbury

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**Examination of Witness**

**David Elstein**

**Q22 The Chairman**: Welcome. We are very grateful to you for appearing before us again; this is beyond the call of duty. Your contributions are extremely helpful to us. If you would like to introduce yourself for members of the wider world, and if you have an opening statement that you would like to share with us before we ask questions, please feel free. As you know, we are looking at the future of Channel 4 and, in particular at this time, the question of privatising the channel.

***David Elstein***: Good afternoon. My name is David Elstein. I am a semi-retired broadcaster, producer and writer. I spent a large part of my life in broadcasting working to get Channel 4 to happen the way it did, to supply Channel 4 and to be a friendly critic of Channel 4 ever after, even when I was working for other broadcasters.

I spent a lot of time when I was director of programmes at Thames Television working with, and alongside, and supplying Channel 4. At BSkyB I had an interesting, but not entirely consensual relationship with Channel 4. At Channel 5 I offered to merge with Channel 4. They declined my offer, although subsequently they tried to buy Channel 5.

I have spent more months than I intended researching the chapter that I hope you have been supplied with, which is due to be published in June as part of the book, *What Price Channel 4?* I apologise for its extreme length. As Oscar Wilde said, “If I had more time, it would have been shorter”. Eventually, I will produce something more suitable for the general public.

What struck me in my research, having been a strong supporter of Channel 4, its independent status and its performance, was that I simply had not realised the extent to which the famous remit had been allowed to atrophy. At one time there were nine formal quotas for Channel 4 and there are now three. Meeting the so-called remit could be done very cheaply. I could probably do it for £40 million a year. For me, the notion that there is a tension between privatisation and the remit is misconceived. The concept of privatisation, or the plan to introduce a privatisation Bill, does set an opportunity to reverse the tide, to reinstate as many of the old hard quotas as possible that Channel 4 used to have to abide by, to invite Channel 4 to sign on for that much tougher regime, and if it cannot, or will not, to see if anybody else will.

In my view, Channel 4 has been allowed to settle into a state of comfortable middle age with reduced obligations, most of them verbal, not formal. If you read the Channel 4 report—there is another one due out next month—you will find 90 pages of verbiage on feel-good things and one page on what they actually did. In my view, this is the result of some misguided legislation in the 2000s. We cannot put that right at this Committee, but we can look forward to using the notion of privatisation as a way of opening up what we really want Channel 4 to do, how we get it to do it, and how we put enough steel into Ofcom to ensure that once there is a proper remit back in place, it will be observed and enforced. That is all I wanted to say.

**The Chairman**: Terrific. Thank you very much for that opening statement.

**Q23 Lord Sherbourne of Didsbury**: Can I follow up your opening remarks and ask you to amplify what you said in a more precise way in three questions? The first is in order to understand what you think lies behind the thinking of the Secretary of State considering privatisation, do you think that Channel 4 is failing in its remit? These are not mutually incompatible. Is there a worry whether Channel 4 is sustainable over a long period ahead? Either way, is the thought, whether it is doing well or not, that it could do better with privatisation? If that is the case, what precisely would privatisation help it do better?

***David Elstein***: Channel 4 could scarcely fail to meet its remit. The only formal remit it has is to broadcast four hours of peak time news per week, which it has done since the day it launched; to broadcast four hours of current affairs programming per week, half of it in peak time; and to ensure that 35% of its commissions come from outside the M25. That is all it has to do. There is no money attached to those obligations. Channel 4 spends £50 million a year on news and current affairs. If it spent less, nobody could do anything about it. If it cut it in half, nobody could do anything about it.

The remit is a fig leaf. It used to be really tough. There used to be seven hours of education, three hours of multicultural programming and 70% of the schedule had to be first-run origination. Amazingly, Channel 4 does not have to broadcast a single hour of new programming at all, if it does not want to, and it would still fulfil its remit. Of course, the news would look a bit strange, because it would be repeats.

Indulge me for a moment. If we allow the news to be new programming, all the current affairs could be repeats, and everything else. There is no requirement for first-run origination on Channel 4 any longer. It could do better. Anyone could do better on what the remit ought to be. That Channel 4 does pretty well—not nearly as well as it used to in my view—is reassuring. It is sustainable. How could it not be? It has £900 million of revenue and no cash spend obligation at all. It could go on for 100 years on that basis. For me, that is not the issue.

I do not have contact with Ministers, so I have no idea what is in the Minister's mind in talking about privatisation. I know that in 2001 the Conservatives in opposition—Peter Ainsworth was then the spokesman for this area—put out rather an impressive document advocating privatisation. If the Committee does not have a copy of that document I can make it available for copying, because it is an interesting historical document. I am afraid I keep these things. I know I should get out more. At the time I had ceased to run Channel 5, soon after I had proposed a merger with Channel 4, so I was very interested.

The notion was to release funding to support the arts generally, and to have a tougher remit. They were very explicit in their press statements saying, "We want to strengthen the remit", and that was the remit in 2001, which was hugely more demanding than the current remit, and they were going to top up the £1 billion, or whatever, that was generated from the sale with some money from the lottery and create a major arts support fund. It was all rather—can I say this—"unconservative". No, that would be unfair. It was an impressive piece of lateral thinking, given that the Conservative Government invented Channel 4 in the first place, improbably, against their own election manifesto.

**Lord Sherbourne of Didsbury**: The question I asked was, what is your view today on how privatisation could improve Channel 4?

***David Elstein***: As I say in my chapter, the process of privatisation is the trigger here. In other words, if you start a privatisation process and say you are willing to look at the sale of Channel 4, what you create is a sale document, and I would hope the sale document would reinstate every last one of the original quotas, apart from the schools, plus several more, as I specify. Once you have that written out as your threshold—if you, potential buyers, are not willing to do that, go away—you talk to those who are willing to take on those obligations and see what their appetite for it is. If there is no appetite, and nobody is willing to do it, you know privatisation is not going to help you very much. If you start the privatisation process that way round, so that before you ever get to legislation you have willing buyers, a known process, a known outcome, and Channel 4 is given the option of taking it on itself and bearing rather more risk than it is currently used to, that is how you improve Channel 4 as a service, whether it stays publicly owned or becomes privately owned.

**Lord Sherbourne of Didsbury**: That is very helpful. Thank you.

**Baroness Jay of Paddington**: I do not understand what possible motive there would be for those putting forward this sale document to insist on that. You said earlier Channel 4 had drifted into rather cosy middle age. I do not see why there should be any motive.

***David Elstein***: For Channel 4?

**Baroness Jay of Paddington**: For the people who are putting up the sale document to have a retrospective determination that there should be all these other requirements.

***David Elstein***: As I understand it, the Government have said they intend to strengthen the remit of Channel 4. That is what they said in 2001 when they were in opposition. Both David Cameron and John Whittingdale are on record as saying that is the point of the exercise, so define "strengthen".

**Baroness Jay of Paddington**: That is a very long time ago.

***David Elstein***: 2001 or last week?

**Baroness Jay of Paddington**: 2001.

***David Elstein***: 2001 is a long time ago, but we had a strong remit, which was going to be strengthened. I am not sure how they were going to strengthen it, but I would love to see that remit still in operation. The issue now for the DCMS is to specify what it means by a stronger remit. Spell it out, nail it down and see if there is any appetite for it. If there is not, you are wasting everybody's time.

**Q24 Baroness Benjamin**: You argue that Channel 4 does not need rescuing, but it would be a better PSB in private hands with much tougher regulation.

***David Elstein***: I do not say it would be necessarily better in private hands. It would be better after a privatisation process, whether publicly or privately owned.

**Baroness Benjamin**: You have also said that savings could be made at the channel to allow more money to fund a more distinctive schedule. Am I correct?

***David Elstein***: Yes, we all know that.

**Baroness Benjamin**: Can you elaborate a little more on why you think Channel 4 would be a stronger PSB if it was to be privatised? Where do you think the savings could be made at the channel?

***David Elstein***: In my chapter I list the 808 jobs currently in operation at Channel 4. I know that any significant broadcaster—Viacom, Discovery, Liberty, Sky, whoever—would be able to save at least 500 of those jobs, if not 600, because most of them are already being done.

You would not need a separate building, and that is £85 million. You would not need any cash reserves, because you do not need them if you are a £20 billion a year company. That is £230 million that does not have to sit in a bank deposit.

My point is that when I was CEO of Channel 5 and approached Channel 4 in 2000 with the suggestion that we merge all our back office operations—accommodation, HR, advertising, engineering transmission—everything other than programming, and left the two programming teams alone to do what they were obligated to do under their licences, we would be able to save between £130 million and £190 million a year. That was 16 years ago. That is an awful lot of money that is not saved because Channel 4 is a narrowly based stand-alone broadcaster.

The fact that Channel 4 has twice tried to buy Channel 5 subsequently, and tried to buy the Living TV channels, also for £100 million, tells you all you need to know. This is a very narrow base from which to run any broadcaster. In my view, the merger savings that are available are of the order of £200 million a year. I can imagine some potential buyers saving a lot more because they will be able to do strange things with tax. Other buyers will do better because they will merge their airtime sales operations. It is certainly of that order. That is the money that is lying on the table because we let it. I think that is a public asset and it is incumbent on us to ask why we want to leave it lying on the table.

**Baroness Benjamin**: So you would spend it on more PSB content?

***David Elstein***: Absolutely.

**Baroness Benjamin**: Where?

***David Elstein***: Within Channel 4?

**Baroness Benjamin**: Yes.

***David Elstein***: My personal view is I would like to see some of the proceeds from a sale allocated to a public service broadcasting fund, which is more widely available than to Channel 4, but Channel 4 would be a primary applicant to such a fund. Education has vanished. It used to do seven hours of excellent programming on education every week. Naomi Sargeant, the head of education, was one of the most powerful people at Channel 4. That has gone. The Act says it must do educational and other educative programming. There is none. It has tried a little bit of children's programmes and that did not work. Channel 5 does 24 hours of children's programmes a week without being required to do so. Channel 4 does none. Channel 4's origination is far too low. It needs to commission a much higher proportion of its schedule as origination. It has drifted into 57% repeats.

**Baroness Benjamin**: Do you think the sale to a social enterprise, as suggested by Lord Burns, could achieve the best of both public and private worlds for the broadcaster?

***David Elstein***: I am not sure what Terry Burns had in mind. I am open to any would-be organisation taking over if it is willing to deliver. The key test here is we have lost the leverage to force Channel 4 to do what it ought to be doing. It was given up in the Communications Act 2003 and the Digital Economy Act 2010. Instead, all we have is a lot of feel-good language and no means of doing anything if Channel 4 falls short. If we had privatisation as a process, part of that would be to reinstate formal quotas. I would now apply cash sums to them. I would ring-fence the budget, the news budget, the current affairs budget. I would look for Channel 4 to commission a minimum number of programmes from small independent producers, independent producers employing ethnic minority producers and directors. All these can be put in place and we can have a much better, much more PSB Channel 4 than we currently have, if we had the courage to say, "That's how it has to be".

**Baroness Benjamin**: You did not include children.

***David Elstein***: Channel 4 has edged towards children's programming more than once. It then went to older children and failed with that. I would love to see them do good children's programming, but I have yet to see the desire. Certainly that should be on the table.

**Baroness Benjamin**: Thank you.

**Q25 Earl of Arran**: We are already circling around these questions. Under its present remit would it be a profitable investment? If the remit had to change to make it profitable, what changes would you consider necessary?

***David Elstein***: The current remit is so flimsy that I could take on Channel 4 and make it highly profitable. I would do it with a kick-starter fundraise. To be serious, the only obligation is to spend somewhere in the region of £50 million a year out of £900 million of revenue. That is it. I cannot think of any commercial broadcaster that would not be able to deliver that. If that is all that is going to be asked for, we would be looking at £5 billion of sale and a really crummy Channel 4 to come out of it. I would much rather raise the barriers higher now, have a really demanding bill of sale and then see what the appetite is.

I would not say I know these companies well, but I have a pretty shrewd idea of how a Viacom, a Discovery, a Liberty Global, or even a News Corp, would approach an opportunity like this. It was interesting that when Viacom took over Channel 5—or Five as we must remember to call it—it volunteered to strengthen the licence conditions. Ofcom did not ask it to strengthen them; it offered to and signed on for a tougher remit. Not much tougher, but a little bit. It is not that these commercial companies have any resistance to putting out a strong Channel 4 schedule; they are balancing what that would cost against what the commercial opportunity for them would be.

The commercial opportunity is you have that £940 million of steady cash flow at the moment, and that is what it has been for the last five, six, seven years. How much of that could you save in costs? This is where I said the £200 million in answer to Baroness Benjamin. If you add on to that the £230 million of cash reserves and the £85 million of building value—let us put a six times multiple on it—that looks about £1.5 billion, and you are still going to be able to deliver a high-quality Channel 4. Your feet are going to be held to the fire much more than those of the current management because you are going to have a set of quotas and the cash fines that are written in the legislation, and which are pretty meaningless in relation to a publicly owned Channel 4, suddenly become real. If you miss this or that quota, it might cost you £5 million or £10 million. Nobody is going to take this on lightly, if it is done properly. There are some pretty shrewd people out there. We are sitting on unrealised value, and why should we?

**Earl of Arran**: In practice, do you think that the Government could be influenced by how much you could raise from a sale and be incentivised to relax the remit further?

***David Elstein***: There is nothing to relax. On a scale of 0 to 10, you are at 1. To go from 1 to 0 would be shameful. I would look at it exactly the other way round and take the Government at their word. You say you want to strengthen the remit; do so, name the strengthened remit, and then go about the sale process, otherwise you are inviting people to negotiate you away.

**The Chairman**: We have reached the halfway mark, but not in the number of questions that we have disposed of.

***David Elstein***: Sorry.

**The Chairman**: Not your fault. We will speed up, if we may.

***David Elstein***: I will be less verbose.

**Q26 Baroness Healy of Primrose Hill**: The Secretary of State has said that the public service remit of Channel 4, including news provision, will be protected in the event of privatisation. Would a privatised Channel 4 be able to keep certain parts of its remit, such as news? If so, for how long? I see what you are saying, that you put forward the remit and if the private companies go for it then that is workable, but if they say no it is not, we go back to the beginning. I still find it hard to see how these private companies would think that making an hour-long news programme every day is a good deal for them if they want to do anything else.

***David Elstein***: It is utterly trivial. On Monday to Friday at 7 o'clock your advertising revenue is probably half what it would otherwise be. That is five hours out of 168. In a heartbeat anyone would take that on. Even the Lebedevs would take that on. This is thin stuff, especially as at the moment there is no cash value attached to that one hour. Your budget is not specified. At the very least, the budget needs to be specified. I would not stick at one hour of news in peak time. Go back to the nine quotas. Why not? See what the appetite is. You have an opportunity. It costs nothing to set out a statement of intent and say, "Who's up for this?" What is the worst that can happen? Deafening silence? Okay, you retreat a little.

This is the whole point of opening up the books. I make the point in my chapter that Channel 4 is extremely coy about what it puts into the public arena. It will not say what its true costs are or what its breakdown of revenues is. You cannot keep that up in a privatisation scenario. Everyone gets to see everything, and then we can make really detailed judgments.

**Q27 Lord Hart of Chilton**: You have had a run-in with Ofcom in the past. I would like to ask you some questions about regulation. Do you feel that the regulator is tough enough in its regulation of Channel 4?

***David Elstein***: Ofcom is interesting. In many ways I am a big supporter of Ofcom. Some of what it does is very good. Its monthly programme bulletin is excellent, dealing with complaints. Baroness Benjamin has sat on that committee, so she knows how hard that job is. It is excellent at compiling information. Its annual communications market report is terrific, the best thing going. It is okayish on some competition issues. I thought its report on the BSkyB/News Corp transaction was terrible, and said so publicly repeatedly. I do not think there are many people at Ofcom now who would defend that document. It was all done in six weeks. You cannot judge a regulator on six weeks' work.

The problem with Ofcom in relation to Channel 4, Channel 3 and Channel 5 is that it lost a huge amount of expertise in 2003 when the merger took place. The way the IBA and the ITC, its successor, operated was very detailed, using expert people holding ITV licensees to very direct scrutiny. All that went. It was partly because Ofcom and the legislation went down the route of language rather than actual quantification, which I much regretted and was very critical of the whole idea of looking at the purposes and characteristics of public service broadcasting. It is like telling a horticulturist, "All you need to do is be able to smell the flowers". You need a lot more than that. You need expertise and design. The problem is that Ofcom does not seem to be able to do that particular job.

I will give you a well-known example. In 2009, still recovering from the severe advertising recession of 2008, ITV announced that it was going to chop its regional news and current affairs budgets. It said to Ofcom, "What we are going to do is either merge a lot of our reporting, so we will have super regions, or everything will be cut across the board. Take your choice". Ofcom felt it was Hobson's choice, each was bad, and it chose what it thought was the least bad option. Ofcom should have said, "Okay, until your profits recover you can do this. As soon as your profits return to £250 million a year"—they are now £840 million a year—"all this must be restored". It failed to do that.

What we have now is an immensely profitable ITV, which has been allowed to get away with a short-term measure to chop its obligation to news and current affairs regionally. Ofcom does not know how to intervene on Channel 4 to do better. It publishes triennial reports on public service broadcasting in which it bitterly regrets the collapse of key public service areas, such as arts, education, religion and so on, and does not say to Channel 4, "Come on, guys, put it right".

**Lord Hart of Chilton**: Do you think it needs to change its ethos and become more proactive?

***David Elstein***: Absolutely, but that has to be part of any legislation that goes forward. It then needs to significantly strengthen its content board. It has already made some new appointments. If we are going to go down a route of a much stronger Channel 4 remit, it needs to be told, "Enforce it".

**Lord Hart of Chilton**: Do you think it is going to be able to cope with this, having regard to its new likely responsibilities in respect of the BBC?

***David Elstein***: It is a different area. I do not think it would be able to do what it is possibly going to have to about the BBC unless it is strengthened, so the two things go together. If you are going to take over judging BBC impartiality and stuff of that kind, you are going to need more than quantification; you are going to need a lot of expert people who are not afraid to express their opinions. That is what we used to have with the ITC.

I ran the Thames Television licence for six years and our annual interview with the IBA, and then the ITC, was tough going. They did not hold back. Before the auction process took over, we all knew that if we did not perform we would be out at the next go round. They interrogated everything. I was responsible at the network level for adult education provision on ITV. I would send proposals to the head of adult education at the IBA or the ITC and they would come back and say, "It is not good enough. We are not going to validate that. You can transmit it, but it is not going to count. You will have to do something else as well or instead". It was back to the drawing board. They were not afraid to express their opinion, and it was a qualitative opinion. That is what I thought was important and what we have missed for the last 13 years.

**Lord Hart of Chilton**: If Channel 4 became part of a commercial group, is there a danger that the culture of Channel 4 would be lost? Perhaps you think there is not a culture.

***David Elstein***: There is definitely a Channel 4 culture. All kinds of commercial people have turned up at Channel 4: Michael Grade, John Willis. David Abraham, the current chief executive, worked in advertising, had never worked in programming or public broadcasting at all, but you learn the ethos and it is a strong one. It is a popular service. A lot of people really like it. It is one of these unusual broadcasters which attracts support from a lot of directions.

**Lord Hart of Chilton**: If it became part of a commercial group, do you think that would be damaging?

***David Elstein***: No.

**Lord Hart of Chilton**: It would survive?

***David Elstein***: It is a risk you have to think about. If I looked at a list of potential acquirers, no doubt there would be some where I would say "Really?" but others I would not have any anxiety about. I have worked for a lot of commercial operators and so-called moguls, and quality pays for itself.

**Q28 Baroness Kidron**: You have confused me because you said in your opening statement that you like the idea of using the notion of privatisation almost as a way of bringing Channel 4 to heel.

***David Elstein***: Yes.

**Baroness Kidron**: I can feel your fury that it has been let go. There seem to be a couple of risks involved in that. One is what makes you so certain that the Government are going to strengthen the remit before selling? What makes you so certain that the money you describe as lying on the table is not going to go to shareholders? I want to ask about the ecosystem of small providers and production companies that Channel 4 is so important to. We have had evidence from a number of people, both in the BBC inquiry and this one, about how it sustains them. I am not hearing anything about the risk of privatisation. You seem to be riding a little roughshod over the risks. Could you talk about that?

***David Elstein***: I am not persuaded by the argument about paying dividends to the new owners. This is not a private equity transaction. The dividend yield on ITV shares is 1%, News Corp 1%, Liberty Global 0%, Viacom 3%. This is not a case of acquiring an asset to strip out cash for dividends. You heard me right at the start. I see this notion of privatisation as an opportunity to strengthen the Channel 4 remit, whoever ends up operating it. If it stays with public ownership you have a different set of risks involved, because the cost of this tougher remit would add to the risk to sustainability of Channel 4 as it currently stands. Government would have to take a view, which is whether we want a very conservatively managed Channel 4 with a thin remit and £230 million in the bank, or a much higher quality

Channel 4 that spends a lot more of its reserve, but then might run into headwinds at some point in time which we would have to deal with.

My view is you should use this opportunity to see how high you can raise the bar of quality in the public service content areas that are important, including the number of independent companies that you commission from, and see who drops out at which point. I was one of the first independents to supply Channel 4. I was one of their big eight. The company I established, Brook Productions, lives on in Brook Lapping Productions, delivering “Inside Obama’s White House” and who knows what, to British broadcasting.

In 1982 when Channel 4 started, it represented virtually all independent production revenues, well over 90%. Now it is 10% of independent production revenues. In 2002, Channel 4 dealt with 414 independent producers. Last year it was 207. The world is changing around us and we need to redefine what we most want from Channel 4.

I have added in my chapter various things that have never been part of Channel 4’s remit because in the current age those are important. This Committee, and its equivalent in the other place, has the opportunity to say to the Government, “If you are serious about strengthening the remit, be specific. Ideally, we would like to have this shopping list. These are the things that ought to be there”.

**Baroness Kidron**: Do you consider it a risk that that remit may not be strengthened in the course of this process? Do you accept there is a risk that Government will not upgrade the remit but go ahead with the privatisation?

***David Elstein***: I hope then everyone would oppose the sale. I would oppose the sale. That seems to me absolutely philistine.

**Q29 Lord Goodlad**: You referred earlier to Channel 5 making an offer for Channel 4. Is there an optimum size for a global media organisation in a smallish country such as this? If so, what sort of size?

***David Elstein***: ITV is a £6 billion organisation in equity value. The BBC is a £5.5 billion a year turnover organisation. I have lost track of how much Sky’s turnover is, I think it is nearly £7 billion a year these days, but not just as a broadcaster, it has many other businesses, telephony and so forth. BT has a turnover of £20 billion a year running a few channels.

I would look at it the other way round: is there a survivable size as a small broadcaster? When I launched Channel 5 it had 220 employees and within four years it was worth £1 billion, because it was incredibly tightly run and managed. At the time that I pitched to Channel 4, they had nearly 1,200 employees—do not ask me why. It is not the actual size, it is how you manage your overhead and avoid duplication of services you do not need.

I cannot pass it on to you—I am under an inhibition, having signed an NDA when I left Channel 5—but this was the document I presented to Channel 4 listing every area of operation and opportunity to save money as between the two organisations. That was O-level maths: two similar broadcasters doubling up on a whole set of activities which they did not need to. It was entrenched inefficiency. I would not say that Channel 4 needs to be part of a £5 billion, £20 billion or £100 billion organisation. All I know is there is a lot of wastage in the way it is run at the moment. Anyone would be able to dig that wastage out.

**Lord Goodlad**: Do you see the possible privatisation of Channel 4 as part of a wider relaxation of restrictions on broadcasting in this county?

***David Elstein***: I see it as a fantastic opportunity to tighten up our PSB ecology. I do not see any need to deregulate or relax this, that or the other. In any event, most of what would apply here would fall under competition issues. For instance, if Sky bids for Channel 4, I am confident that the competition authorities would say, "Sorry, in the advertising marketplace you are going to be too large. That is an unacceptable merger". To be honest, I do not know what is in the Secretary of State's head when he is advocating privatisation. As one analyst has put it, it might be insane. It might be ideological dogma. I prefer to attribute good sense to Ministers and say, "I am going to take you at your word. You want to have a stronger remit for Channel 4, do so and we will support you".

**Lord Goodlad**: If the decision was taken to privatise Channel 4, who would you see as the likely buyers? Do you think ITV, BSkyB or Sky should be allowed to bid, or should it be an IPO?

***David Elstein***: I cannot see an IPO working. I do not see a private equity deal functioning, because private equity does need to take dividends out. I see it as four, five, six almost certainly US and EU companies which would find the opportunity irresistible. I do not think ITV would be allowed to merge with Channel 4 because of the impact on the advertising marketplace. I think Viacom would be allowed to, because Channel 4 and Channel 5 is a well-known, acceptable combination. Liberty Global does not have any particular broadcast assets in the UK, but owns Virgin Media. That looks a very acceptable home. News Corp rather than Sky is a possible. Discovery is the most obvious of all the potential partners, not least because it has a big portfolio of pay-TV sports rights, which require free-to-air expression at some level, so partnering up with a free-to-air channel would make sense. There are three or four European companies I could imagine. Elsewhere in the UK, maybe BT would like to take part.

**Lord Goodlad**: Why do you think an IPO would not work?

***David Elstein***: You are basically selling what you have already. It is the inefficiency in what you have already that creates the opportunity for a third party to come in and make the savings. An IPO simply locks those inefficiencies in. I do not say it is impossible but I think it is improbable.

**Q30 Baroness Jay of Paddington**: I am pursuing the whole issue of who might buy and what that impact might be. Several of the companies you have speculatively mentioned are either directly foreign companies, or at least international. You have mentioned News Corp and I gather Scripps International has announced that it could have some interest, which already has a stake in UKTV. Do you think there is any reason to be concerned about who buys it, those international or foreign investors?

***David Elstein***: It is generic more than specific. I would want to look hard at the quality of guarantees that an organisation was putting forward. As I say in my chapter, I would contemplate a retrieval mechanism.

**Baroness Jay of Paddington**: Can you expand on that? Everybody in this room is familiar with international guarantees that governments and regulators try to impose on foreign bodies, and they are rarely successful.

***David Elstein***: It is a bit like a golden share, taking back the spectrum, the EPG slots, the things that are specifically in the gift of government and regulator, in the event of A, B, C or D.

My modest experience of dealing with these international organisations is that what they most like in life is high-quality content. That is what they are looking to make. That is what works for them internationally. Discovery does very high-end wildlife programming. I am sure it would be delighted if it owned Channel 4 to discover that here was an outlet for its very high-end wildlife programming in the UK.

**Baroness Jay of Paddington**: Let us focus on news. You said news was trivial in the context of the overall programming.

***David Elstein***: The cost.

**Baroness Jay of Paddington**: The cost against the amount of broadcasting involved. Are you sanguine about the prospect of, for example, News Corp using that as a platform to develop something like Fox News on Channel 4?

***David Elstein***: Given that News Corp, instead of developing Fox News developed Sky News, which is a hugely valuable part of our news coverage in this country, I would not be worried about that at all. Fox News is available in the UK. It has a trivial viewership. Sky News has a much bigger viewership, but not as big as BBC News. I do not think so.

**Baroness Jay of Paddington**: You do not feel there are any particular concerns? People speculate in a slightly exaggerated way that you could get interest from Russia or China, but you do not feel that anyone should be, as it were, even theoretically concerned about who might own the channel?

***David Elstein***: Keep something in your back pocket on quality control. For the most part, I do not think anyone is going to try and buy Channel 4 who is not going to be instantly acceptable, because they would not want to go through a process of rejection. Russia Today is not going to bid, nor is Al Jazeera or Iranian TV or France Today. I do not see those as realistic propositions. We are becoming speculative.

**Q31 The Chairman**: Earlier you said, rather in passing, with what you regard as the current rather feeble remit, the value of Channel 4 might be £5 billion because of the savings that could be made and that if a much tougher remit was put in place, we still might get £1.5 billion. As you said it rather briefly in passing, are those the sorts of numbers that are in your mind?

***David Elstein***: I would always trade quality of service for cash. In other words, if you could get a maximal remit commitment from a buyer and only £800 million cash, that is better than a not very good remit and £1.5 billion, because that is selling yourself short, disposing of the family silver unnecessarily. I hope the object of this exercise is to end up with the strongest remit that Parliament can agree upon as a condition of sale. It is a terrific opportunity to get our collective minds going and saying, “What do we really want from Channel 4?”

I started my research four months ago thinking, “Oh yes, the wonderful remit. Terry Burns is right, you can have privatisation or the remit, but you cannot have both”. This is really sad. I have all the old Channel 4 reports from the 1990s and the 2000s. I started reading them and was astonished at the transformation that has taken place and nobody seems to have noticed. It is like Topsy; it just happened. Here is our chance to put right everything that has gone wrong over the past 13 years.

**The Chairman**: Thank you very much. That is a very powerful message. We are extremely grateful to you for putting it to us very clearly. Thank you.

### Examination of Witnesses

**Colin Browne**, Chairman, Voice of the Listener and Viewer, and **John McVay**, Chief Executive Officer, Producers Alliance for Cinema and Television

**Q32 The Chairman**: Welcome, and thank you very much indeed for joining us. As you know, we are looking at the possible privatisation of Channel 4 and other aspects. We are very grateful to you for joining us. Would you like to briefly introduce yourselves, perhaps you first, John, and say where you are coming from, and if you want to make an opening statement about Channel 4, please do that for us at the outset as that would be helpful?

***John McVay***: I am John McVay, the chief executive of Pact. Pact is a trade association that represents the interests of film, TV, children's, animation and digital producers. We are probably as old as Channel 4. In fact, we were set up round about the same time and so we have a very close and intimate relationship with Channel 4. As with a lot of intimate relationships we do not always get on. When families meet at Christmas they might fight over the turkey. We do not do that and are staunch supporters of Channel 4, but we take a view about its current activities and its future.

**The Chairman**: Thank you very much, John. Colin.

***Colin Browne:*** I am Colin Browne, the chairman of Voice of the Listener and Viewer. We think this is the only consumer organisation in the UK that is wholly dedicated to the interests of listeners and viewers. It was founded originally in the 1980s as the Voice of the Listener and we added the "Viewer" bit later. We promote and lobby for public service broadcasting, specifically for quality and diversity.

Picking up John's point, obviously we have a close relationship with the BBC and Channel 4, but we regard ourselves also as critical friends of these organisations. We are a charity. We are funded by our members, who pay £30 a year because they believe in public service broadcasting in Britain and believe that we can help support it.

**The Chairman**: Thank you very much. Lord Sherbourne.

**Q33 Lord Sherbourne of Didsbury**: Can I ask each of you a separate question, at least to start? We are trying to understand the thinking behind the decision to consider privatisation. The question for Mr Browne is, do you think the remit of Channel 4 is satisfactory and satisfactorily monitored and maintained? The question for Mr McVay, which we have been discussing in previous sessions, is what is your view on the long-term sustainability of Channel 4 under the present regime?

***Colin Browne:*** To start on the remit, I could not help hearing what David Elstein said at the end. We have looked at the remit from the original 1980 Broadcasting Act, through to the Communications Act 2003, the Digital Economy Act 2010, and subsequently, and it seems to us that the remit has been strengthened at each stage. We believe the remit is pretty good, but there is an issue with delivering it. How do you measure a remit which is, to a large extent, quality driven rather than quantity driven? Clearly, one can have a debate about that. What you have to do is to look, ultimately, at the output on screen and what audiences say. The research from Ofcom and our members shows that Channel 4 broadly meets the remit which is set out for it. We are a bit reluctant to go down a more quota-driven/numbers-driven measurement of output. We think that is rather difficult in a channel such as Channel 4, and indeed in broadcasting generally. That requires intelligence on the part of the regulator, which in this case is Ofcom, and requires organisations such as ours to be alert as to the standards and quality of the broadcasting that is provided by Channel 4. Nothing is ever perfect, but broadly I would say we are content with the remit and, by and large, the reports from Ofcom hold Channel 4 pretty well to account, and certainly our own research suggests that there is a good level of consumer satisfaction.

***John McVay***: I would like to touch on the remit at some point, so I hope some other member of the Committee might prompt me on that. From the research and data that have come out over the past few years, we think that Channel 4 is not in rude good health but is in good health. Advertising over the past decade has grown by 12% in real terms and, in spite of the effects of the recession, Channel 4 is still doing remarkably well. In fact, last year was one of the best years ever for commercial free-to-air television in NAR. Channel 4 has recovered its reserves since the recession and, as Mr Elstein pointed out earlier on, has reserves of about £230 million in the bank and generated revenues of about £1 billion a year in 2014. It is making investment in content, which is what it should do, not only for its public service purposes but to remain commercially competitive. We live in a world where distinctive and quality programming is what wins audiences. Channel 4's demographic remains one of the most highly valued in our sector. Its CPTs are the highest in the sector. We would not say the model is bust at all.

Yes, there are people migrating to watching television online, on tablets and on phones, but we have to bear in mind that net TV viewing across the past decade means that people are watching four hours more television, so that is more eyeballs and more availability for Channel 4 to monetise. In various agreements we have reached with Channel 4, we have helped it to launch 4oD, All 4 and its secondary digital channels. If you look at Channel 4's total media real estate that it can monetise to advertisers, it has grown over the past six or seven years. That has enhanced its ability to generate revenues and reinvest as much of those revenues as possible back into its public service purposes, and, overall, we do not see a financial crisis.

I appeared before this Committee when the chief executive was Andy Duncan, where Channel 4 was asking for a large chunk of the BBC licence fee or a bailout from government. I do not think those conditions were true then and I do not think they are true now.

**Lord Sherbourne of Didsbury**: Would I be right or wrong to infer from what you have both said that if it ain't broke don't fix it?

***John McVay:*** I do not think it is broken or that the models that exist in our very carefully balanced broadcasting ecology are dysfunctional. If we look at investment in original British programming and the quality of that for our audiences, you might say that system is generating the right level of creative and commercial competition to drive value back to the public, and, indeed, advertisers and the commercial sector. Things can always be improved and you can always get efficiencies. In certain areas of Channel 4's remit there could be some tweaks, but, overall, we think the current model is working pretty well and we do not draw the conclusion from all the research that it is a broken model.

***Colin Browne:*** That would also be our conclusion. Looking at the overall ecology of British broadcasting, which we think is delivering good broadcasting and services for the consumer—and we come at this purely from the point of view of consumers, viewers and listeners—those who propose change have to be able to demonstrate the reason for change and that it would produce something better. It is not clear to us how that could happen. To characterise it, we would say that, in a sense, the Government here appear to be looking for a solution without having defined the problem.

**Q34 Baroness Benjamin**: The Secretary of State, John Whittingdale has argued that Channel 4 is being restrained by not being privatised, which means it has less deep pockets. The former boss of Channel 4, Lord Grade has said: "The current settlement for Channel 4 is no longer fit for purpose and puts a risk on the public purse ..." Other critics of the status quo say that if Channel 4 were to be privatised, it would be better able to withstand commercial threats. What do you see are the pros and cons of this argument?

***Colin Browne:*** The argument that is being made there is that it would somehow be stronger and in a financially strong position to withstand competition. The detailed analyses I have read from people such as Ernst & Young and Enders Analysis, and indeed from Ofcom, seem to indicate that, in the view of all those bodies, the Channel 4 model is sustainable. Certainly, when Lord Grade was chief executive he was pretty confident that the model was sustainable.

Obviously the world changes around Channel 4, but if you look at privatisation as an alternative, it seems to us that it is always possible to get greater efficiencies out of an organisation, and that clearly needs to be looked at, but if you have a different form of ownership, somehow you are going to have to serve the interests of the shareholders, because that is why they are investing in that organisation. Inevitably, one can argue against this by saying it will all be sorted out by the remit as long as the remit is fine, but a remit gets eroded over time. Shareholders will put pressure on over time to get a greater share of the funds. You would have to take a fairly big leap in the dark to say that greater efficiency was somehow generating more funds than you would end up having to pay shareholders to reward them for their investment. On the basis of the studies we have seen, we think it is unlikely that privatisation would leave Channel 4 in a stronger position than it is at the moment.

***John McVay:*** They could be right regarding the purpose of Channel 4. If we were saying we want Channel 4 to be the biggest, most successful commercial media company on the planet, the current model clearly does not deliver that. It is where you are coming from in your analysis. If you want Channel 4 to be a commercially driven public service broadcaster, with a remit to serve the public purposes set up by Parliament for social goods, Channel 4 does not have to be a huge, off-the-leash commercial beast to do that. It needs to be highly efficient, to monetise as much as it can, but it needs to meet its primary purposes. I look at other large, commercial global media companies and Channel 4 is not like them. However, it was designed not to be like them because of its purpose. They are two different things.

Channel 4 may need access to more capital in the future to invest in more technology and to take more opportunities. Technology is very expensive. We can recall the iPlayer cost the BBC hundreds of millions of pounds to be a world-class VoD service. Allowing Channel 4 more ability to borrow might help it navigate its commercial future. To a point, if you take away its public purposes and make it fully commercial regardless of the remit, the remit will be eroded. I do not think it would necessarily damage the programming spend, because why would you buy something and then damage the product you are monetising on? However, I think it would change the mix of that programming spend and the type of programming, and that may not deliver the same public service outcomes that everyone would seem to desire from it.

**Baroness Benjamin**: Those who argue for privatisation believe that if Channel 4 were more efficiently run—and we heard from David Elstein about savings of £200 million a day—as part of a larger group with economies of scale, it could spend more, not less, on programmes. How do you react to that criticism?

***John McVay:*** Representing producers, any broadcaster which will spend more on programmes gets my vote. However, you have to carefully consider why and how. If it was spending more money on British programming, but it was to the detriment of our overall system, you would want to be careful about that. If it was spending more money on low-value programming that had very limited international appeal which might generate good commercial returns, that may be commercially sensible, but I would be nervous about that for the long-term value of British IP and exports. We are the second largest exporter in the world. We have a positive balance of trade with Europe. All those things are partially driven by Channel 4 investment.

***Colin Browne:*** I would make the additional point that my experience—and I have worked in both the public and private sectors in different forms of ownership—is that the culture of any organisation inevitably reflects the way in which it is funded. If you become to some extent a profit-driven organisation, your incentives change. There is a clear link between, as I said, the way you are funded and your incentives. We believe that over time the public service remit would be eroded in the way I have described. It might not happen overnight, but the culture would change, the output would change, and, ultimately, we do not necessarily believe we will end up with more money to spend on programmes.

***John McVay:*** As a corollary, we are pro profit maximisation in commercial companies and I represent private enterprise. However, Channel 4 is clearly publicly owned and has public purposes, and whether it is run efficiently and delivering the best value at the best price for public purposes is a matter for its board, the non-executive directors and, indeed, your good selves and our friends in the Commons. Every business can be more efficient. That is what we have learned since the recession. Clearly everyone in Channel 4 wants to make sure that it sweats every pound it earns to deliver value to audiences and to the advertisers.

**Baroness Benjamin**: Some in the industry, such as David Elstein, feel strongly that the remit of Channel 4 has been diluted, especially in the case of the arts, education and perhaps children’s content. What is your opinion on this?

***John McVay:*** We are very active in our campaign to try to persuade the Secretary of State to look again at the requirement for commercial retail broadcasters concerning children’s programming. There was an oversight in the Communications Act. It used to be a requirement for PSBs to commission original children’s programming. That has been diluted since that Act came into force and further exacerbated by the introduction of the HFSS restrictions on advertising around children’s programming.

Channel 4 is the only free-to-air commercial broadcaster that still has a remit requiring it to make children’s programming. It is split into two areas: one is called older children, for 10 to 14 year-olds, and the other is young adults, for 14 to 19 year-olds. Those of us who have children—I have three boys of 20, 18 and 15—know they watch up and watch adult programming. It is up to us as parents to moderate that, or at least know what they are doing. We would say that 14 to 19 year-olds are being well served and there is a range of programming there. However, we do not recognise any programming that is specifically commissioned by Channel 4 for, say, 10 to 12 year-olds. Ten to 12 year-olds are at a very different developmental stage compared to 14 to 19 year-olds. We do not see any programming commissioned by Channel 4 that addresses their needs for drama, factual programming or documentary programming that engages with the lives of that age range. Other than watching programming on the BBC—the only broadcaster still commissioning children's programming—that age range is watching American-acquired programming on other channels.

We think there is an opportunity for Channel 4 to strengthen its remit by producing or commissioning shows for younger children, and to build audience. If it was looking to engage 10 to 12 year-olds, it would be building its audience of the future. We all remember shows when we were children which we loved and made sure we got back from school to watch. We think it is a missed opportunity and would encourage the debate about Channel 4 and its future remit and its requirement to do more to stimulate more original children's programming.

We also think it is unhealthy if we only have one buyer of children's programming, the BBC, because the BBC has a particular editorial view of the world, which is right and proper. Channel 4 is meant to have a different editorial view of the world as part of its requirements. We think it would generate new writers, new actors and more diversity, which is clearly part of Channel 4's current view about its remit, and it would be a positive thing for Channel 4 to do.

**Baroness Benjamin**: What about the arts and education?

***John McVay:*** The arts is a broad subject. I think Channel 4 has been very good on that, but it may not be someone going around an art gallery to stimulate the arts. It takes a broader Channel 4 view about that.

***Colin Browne:*** As I said earlier, we think the overall remit as broadly defined has been strengthened rather than weakened over the years. Where there are gaps—and I agree there are some gaps as we have heard—those can be addressed by regulation. It does not require a change of ownership to address that kind of issue. I think they are two different issues.

**Q35 Baroness Kidron**: I think you have answered some of my question, but I would like to ask you very specifically about news. The Secretary of State has said that he will protect the remit as it stands. Do you think it is reasonable to think that a private owner will protect the news as it is currently?

***Colin Browne:*** I come back to our underlying point that a remit can say so much and it is then down to the way in which that remit is regulated and the efficiency and strength of the regulation. Over the years you would see, as you have seen in other circumstances, the licensee going back to Government and saying, "I know we said we would do this, but I have a financial problem here and my shareholders are asking for a bit more money. Is it really sensible I should be doing that if the BBC is doing that anyway?" It gets eroded in that way. The remit is important and regulation of the remit is very important, but I do not think it is enough. I go back to what I was saying earlier; the character and nature of an organisation are affected by the way in which it is funded and incentivised, and I would worry about remit erosion.

***John McVay:*** I would echo slightly Mr Elstein's comments to you earlier about news being part of your brand and something you should be doing as a mainstream broadcaster. Sky does not have to do news, yet it makes some of the top award-winning news programming. I do not think it would stop doing news. Depending on who owns it, it may change the tone or style of the news, but it would still do news. Of course, we pride ourselves in the UK on having independence and impartiality in news, but we also pride ourselves on having different tones and styles of news. Channel 4 is doing news in a particular way now because of its editorial view, and that itself may change over the next few years. It is quite hard to anticipate what a new owner, depending on their particular perspective, may or may not do. I do not think it would get rid of the news but it may change how it is done. Channel 4 has changed its news programming over many years.

**Baroness Kidron**: The thread of David Elstein's evidence, if you like, was saying that privatisation is an opportunity to make the remit stronger, to make the regulation of the remit stronger, and that is the purpose of it. He ended up saying let us not do it unless we can make the remit stronger. Do you share that view or are we going the wrong way about this? Is privatisation the wrong way to get to the same destination? You both look confused.

***John McVay:*** No, I get David's point, but the journey of British broadcasting through regulation and legislation over the past two decades or more has been to become more flexible and more able to let broadcasters with public purposes interpret that. We see that the days of ITC or IBA tick-boxing have been consigned to history. You would have to go back to that if you were going to hold a private owner's feet to the fire. It might say, "That is fine, but I am competing against ITV and it is not getting its feet held to the fire to the same degree. It doesn't make children's programming any more. It doesn't do all these other things you are asking me to do." I think that is a problem. If you are going to have regulation, particularly for competing companies that are commercially driven—although one is currently publicly owned—regulation has to be fair for everyone. It would seem to be that, yes, you have an opportunity to toughen up the remit. I would say you could toughen up the remit anyway for commercial broadcasters if you were so inclined, but, whatever you do, it should be fair and equitable for everyone—advertisers, commissioners, shareholders, ITV as a plc, the pension funds invested in that—and there is a whole range of things that you have to be fair about.

***Colin Browne:*** What we know on the news specifically is that "Channel 4 News" at 7 o'clock in the evening does not generate remotely enough advertising to pay for that programme. If it was privately owned/shareholder owned you would have to ask whether that cross-subsidy would still be permitted. There would be some fairly large questions about that.

I was working at BT at a senior level when it was privatised and I think there the situation was entirely different. You could hold that organisation to account in very specific ways. Are you delivering telephones within a certain amount of time? Are you repairing faults within a certain amount of time? Your prices will be RPI-minus X. That was good, strong quantitative regulation. It is very difficult to apply that to a privatised broadcaster.

***John McVay:*** News does not make anyone any money. It does not make Sky money. You lose money doing news, but you are doing it for a range of other purposes. I would go back to my earlier comment about children's programming. Making more children's programming would probably lose Channel 4 money, but it is part of the PSB compact that there are certain things we require as a trade-off for the benefits the PSBs receive, to give us content that is otherwise not supplied by the market, or not sufficiently supplied by the market. That is why I would ask Channel 4 to do more children's programming, because that is part of its PSB and it should maintain news. If it was privatised, I do not think we would get the children's programming, but we may still have news.

**Q36 Baroness Healy of Primrose Hill**: John, regarding the people you represent, I have a question on the importance of this to the British economy. In 2014, Channel 4 worked with 338 suppliers and spent £430 million on original UK content. What effect could a change in ownership of Channel 4, such as privatisation, have on your members? Would these effects be consistent across all your members? For example, Channel 4 is particularly valuable to smaller indies, but I understand bigger companies are also working in the market.

***John McVay:*** Yes, we have tested out some of those numbers and it has actually been working with fewer smaller companies over the past few years. Leaving that aside, the principle is that Channel 4 was set up with the purpose of stimulating the independent production sector to create more competition, more diversity and more innovation. It is a very important buyer from independent producers across the UK. Obviously we work closely with Channel 4 to make sure that new companies are able to get access, build their businesses, and get commissioned and recommissioned by Channel 4. My producers would always like a lot more work, but it is a competition, and that is fine.

The publisher broadcaster model that Channel 4 has is the model that many other broadcasters have adopted around the world. Channel 5 until recently, although it was not required under regulation, was a publisher broadcaster. It has a tiny in-house production unit which does not really perform that well. The publisher broadcaster model is the most efficient way to generate the most ideas at the best price and the best competition for you as a broadcaster. Would a private buyer seek to set up their own in-house production? Yes, it may, but it would normally be driven by its desire to retain and own and control intellectual property rights. It would not be very efficient because it would have a huge fixed cost and it might not generate the hits to give the money back. In fact, in the current negotiations on the charter, the BBC is in discussion with us and government about reducing BBC Studios' in-house production to make it more competitive and provide more opportunities to the market to supply to the BBC. The trend in the market for good competition issues would tend to say the publisher broadcaster model is very efficient, until you get to the point where you want to wholly own and control intellectual property rights. That is when you get tempted to set up in-house production. From where I sit, we would be fundamentally opposed to that on Channel 4. When that has been mooted by previous Governments we have made it very clear that would be damaging to the interests of the diversity of the SMEs that we represent.

**Baroness Healy of Primrose Hill**: Mr Browne, would you be concerned for your viewers and listeners that the quality and the types of programmes being made would be affected?

***Colin Browne:*** We would certainly be concerned that the diversity of programmes would be affected. It is an important part of Channel 4's remit, as we have heard, to provide different, distinctive and diverse programming. We would have concerns. We come at this from what is in the interests of viewers, and it seems to us that to play around with this model has significant risks and it is very difficult in any firm kind of way to identify what the benefits would be. We certainly would have those concerns, yes.

***John McVay:*** I understand that under a new administration you want to look at everything and the status quo is often seen as difficult. I have reminded the Secretary of State that the status quo in British broadcasting has been arrived at through Parliament, through interventions, debates and discussions, and understanding what the purposes are of a regulated broadcasting system. In America, TV is a commodity. We do not take that view. I have often used the phrase that what we have, including with Channel 4, is a Rubik's cube of intervention, regulation and market dynamics, which is generating one of the world's most successful TV economies. We are the second largest exporter. We are in every single major market around the planet. We have soft power in China and Latin America. Everywhere you go you will see British programming. The global TV industry is the biggest entertainment market at $400 billion and the world wants great quality product. By accident, design or intervention we have magicked up a system that produces that. We would be mad to mess around with it too much, because that would suit other people who would like to eat our lunch. These debates are right and proper for a government of any political persuasion to look at the system, but it is a system that has evolved through successive Parliaments. It was Margaret Thatcher who created Channel 4 and who introduced the regulations for the independent production sector. It was a Labour Government who introduced the Communications Act, which gave us our intellectual property. All those things have combined to produce a system which is geared towards creativity, competition and quality. That is one of our USPs internationally, and Channel 4 is an important part of that.

***Colin Browne:*** Expanding very slightly on that, the concern we have from the point of view of our viewers is if Channel 4 were part of a larger international group, a conglomerate of some kind, once again there would be internal pressures to make programmes that were designed for an international audience. Obviously, it is good for British programmes to sell abroad, and in principle we support that, but our prime concern is programmes that are made for a British audience, preferably by British programme makers and creative talent, and we feel that is another area that would be under significant erosion if Channel 4 fell under international ownership in particular.

**Lord Hart of Chilton**: I think Mr Browne has answered my question.

**The Chairman**: We can move swiftly on. Baroness Bonham-Carter.

**Q37 Baroness Bonham-Carter of Yarnbury**: John, the terms of trade have been key to the growth of the independent production sector in the UK. How do you feel a potential privatisation of Channel 4 would affect that? For everyone here maybe you could explain what they are too.

***John McVay:*** The terms of trade were introduced in the 2003 Communications Act after scrutiny by Committees in both Houses of Parliament, which concluded that there needed to be intervention to address buyer power in the market. The four PSBs accounted for 90% of all programming spend, and were able to leverage all intellectual property rights from their suppliers as a consequence. Today PSBs still account for 87%, so not much has changed. What has changed for the independent producers is the fact we own our intellectual property under legislation and regulation, and that has allowed us to go from an £800 million sector in 2002 to a nearly £3 billion sector today.

The benefits to the sector have been multiple. My members are now proper entrepreneurs and businesses which have been able to invest in programming by investing their own profits or offsetting their profits against future earnings. That money has gone on the screen with British programming and led to true price competition and broadcasters not paying the full price of the programmes they make, which has incentivised us as businesses to go and find new ways to get OPM—a technical term we use for “other people’s money”—to bring it back in to the UK from Germany, France, Latin America and America, and invest it in our content. That has been a really good thing because that has allowed us to maintain high-quality content even in the teeth of the recession. When many other countries were diminishing the quality of their programming or cutting the hours of programming, the UK did not do that, and that was a combination of our Rubik’s cube and the supply side being able to find those funds.

It is all underpinned by a very simple piece of regulation in the Communications Act. Clause 285 requires that the four PSBs must have a code of practice that regulates the dealings between them and their suppliers, the independent producers. If you are bought by a foreign broadcaster or foreign media company with broadcasting interests in the UK, you are no longer an independent producer and therefore you do not get the benefits of intervention.

We are post quite a concerted campaign by Channel 4 to try to seek the amendment or removal of the terms of trade. The Secretary of State asked Ofcom to do a specific report for him in September last year. On the back of their PSB report in July, where Ofcom found there was no problem, they produced another report, delivered to the Secretary of State on 20 December, which concluded the same thing: that the system is working pretty well and there is no rationale for major intervention. Mr Whittingdale set a number of other questions that it answered, and which were more tweaks that may be considered and not recommendations. To this day we await the outcome of the Secretary of State’s deliberations on the Ofcom report, but we are deeply concerned that since September this has had a chilling effect on the market, where many of my member companies are unable to raise the investment they are seeking to grow or develop.

**Baroness Bonham-Carter of Yarnbury**: Sorry, what has had a chilling effect, the spectre of privatisation or the lack of response?

***John McVay:*** The fact that we do not know whether the regulation underpinning our businesses is going to be retained or not. I have spoken to a number of venture capital and equity companies and they will not be investing in the sector any time soon because we are all driven by IP and if we lost the IP which underpins our businesses, they will not invest.

**Q38 Lord Goodlad**: In that connection, do you think that Ofcom would be able to regulate a privatised Channel 4?

***Colin Browne:*** It would probably need additional resources to do it. I have a fair amount of respect for Ofcom as a regulator. It regulates ITV's public service requirements and recommends the appointment of the board of Channel 4 at the moment, so, with sufficient resources, I am sure that could be done, yes.

***John McVay:*** I think there is a problem in the current regulation of Channel 4 around my earlier point about children's programming, which Ofcom has raised in its own reports about Channel 4's remit, but, because it does not have the powers from Parliament to require Channel 4 to do more about that, it can wring its hands and say, "We are not very happy. Can you do some more, please?" If you were under the current regime, any smart commercial operator would continue to behave in the same way, or would go further, and I do not think Ofcom would have the powers to do anything about that.

**Lord Goodlad**: Do you think there would need to be any changes to the present regulatory system if Channel 4 were privatised? If so, would it impact on the wider public service broadcasting ecosystem?

***John McVay:*** I think you would have to, if you wanted to be very precise and make sure any future owner was delivering precisely what you wanted. Under the current looser regime that was introduced in the Communications Act, there are a number of things Ofcom cannot require to be done. Children's programming is one of them. I go back to my earlier point, that if you were doing it for Channel 4, you would have to do it for everyone, to be fair in the commercial market. Channel 4 is a commercial operator and you would have an asymmetrical degree of regulation for people who are competing in the commercial market.

***Colin Browne:*** Ofcom's core competence is as an economic regulator. When one gets into some of these other areas, particularly to do with qualitative judgment and programme-making, it is not an area where Ofcom claims to have expertise or even wants to have expertise. It is not impossible, but things would have to be changed to make it happen.

**Q39 Baroness Jay of Paddington**: In the context of the other questions, Mr Browne talked about some of his general concerns about potential owners. May I ask you to be a bit more specific and broaden those concerns? Who do you think is the most likely to be able to purchase Channel 4 if it comes up for privatisation? If it goes to a foreign owner or foreign investors, should there be any restrictions or any possibility of restrictions on who that should be?

***Colin Browne:*** This is not really my area of expertise.

**Baroness Jay of Paddington**: You mentioned your concerns about foreign investment.

***Colin Browne:*** My concern more generally with foreign ownership is that there would be pressures on Channel 4, or what became of it, to produce programming that was geared towards an international market and international audience. Therefore, one would lose one of the big strengths of Channel 4 at the moment, which is making programmes for the British market, and for parts of the British market that are not covered by some of the other mainstream broadcasters. There would be serious pressure on Channel 4 under any alternative ownership, but particularly under international ownership, to remove itself somewhat from that form of programming. Speculating on one owner against another is quite difficult. To an extent, you can control a lot by regulation, but you then come back to my fundamental point that so much depends on the underlying stretch of an organisation, what ends up on screen depends on the motivation and the incentives on the people actually producing the programmes, and that in turn comes right back to the way in which that company is funded.

**Baroness Jay of Paddington**: Do you think that would be a potential difficulty, for example, if ITV or Sky were to be the possible owners?

***Colin Browne:*** Clearly there are issues. ITV is a target. ITV might acquire Channel 4 and then be acquired itself. Once one goes down this route, it is quite difficult to know what the end point would be.

***John McVay:*** Having watched a number of foreign or non-UK media companies acquire UK assets, my view is we have to be very careful about how we discuss this. I am very proud that we have foreign investors pouring money into our creative economy, sustaining high-quality jobs, at both creative and high-level commercial executive level, which has led to huge growth and competitive advantage for us. The creative industries are worth 8% of GDP. They are one of the fastest growing parts of the economy. Television is the world's biggest entertainment business. Looking to my European counterparts and competitors, which are starved of capital investment and scale, we should welcome money from anywhere on the planet, provided it meets the requirements that we set it. There are tests on fit and proper persons. There are rules people have to follow to be able to own media assets in the UK. Thankfully, we do not have the non-foreign ownership rules they have in Canada which have led to a complete diminution of the competitiveness of that system. It is a locked-in, now subperforming system, using hundreds of millions of Canadian dollars of taxpayers' money. We have an open market approach in the UK which is good and we should welcome investment.

**Baroness Jay of Paddington**: For example, do you think it is realistic, as I think David Elstein was arguing, that you could, as it were, strengthen the remit of Channel 4, at least theoretically, as part of a sale document? Would that be possible? You have described the conditions on foreign ownership and investment.

***John McVay:*** Clearly anything is possible. The question is whether it means anything in the long term and whether it has any traction. If a big company with deep pockets wants to lobby to change regulation or legislation, then they are perfectly able to do so. You may start off in a very firm, tough place, but you may not end up there, and then I would question why you did it in the first place. There may have been a lot of pain and grief on the way. Being clear about the system and what the purposes are is where the Secretary of State and the Government should be looking.

We have a very valuable asset, including Channel 4, but I do not think we should be sending out a message that we are not interested in foreign investment in our media or creative economy. Ironically, although David Abraham has complained about British money going back to America, the opposite is happening. Indeed, one of his most successful dramas, "Humans", was funded 50% by an American broadcaster, AMC, and it was the biggest hit in a generation for their drama. Instead of money going out of the UK to America, I see more money from America coming here, and it is precisely because of our creative economy, our competitiveness, our quality, and our openness to investment.

***Colin Browne:*** I would make the point that joint funding is very different from ownership.

**Baroness Jay of Paddington**: I was going to ask you to underline that point. Specifically on Channel 4, is there any role for the new content companies, such as Netflix or Amazon, regarding ownership?

***John McVay:*** I cannot see why they would be interested. They are in a pay model and in 130 countries. I think Channel 4 would be at the margins of their interests.

**Baroness Bonham-Carter of Yarnbury**: I have a supplementary as a result of Baroness Jay's questions. Quite a lot of our big indies are now owned by Americans, are they not?

***John McVay:*** They are not indies; they are just producers.

**Baroness Bonham-Carter of Yarnbury**: Right, but that has not had a detrimental effect.

***John McVay:*** We have produced a report, not yet published—it is with the Secretary of State—by a leading libertarian economist which showed that the characteristics of our market in the UK are a very concentrated demand side in the broadcasters but a highly unconcentrated supply side. Indeed, over a number of years we have mapped the number of start-up companies. Every year at Pact we get 100 new members and at the end of the two-year period there are 100 still standing, so it is quite a high attrition rate. In spite of consolidation in the UK supply market and foreign ownership and investment, we have seen no diminution at all in the number of companies that want to set up and compete to win commissions from our system. Indeed, in the recession we saw an increase in companies setting up and looking to become TV production companies.

**Baroness Kidron**: I am curious to know, in that ever-so-delicate ecosystem you are describing, whether Channel 4 in the form it is acts as a sort of gatekeeper to all that nuanced work that you are describing,

***John McVay:*** I think that is a very good point. When I was asked in an informal meeting with someone at the Treasury, "Why do you think Channel 4 is important?"—and of course being the Treasury they probably expected something about numbers and money—I said, "The reason why Channel 4 is really important to the system is that it allows people to get into the TV sector who should not really be in the television industry". It allows in mavericks, innovators and disrupters, and people who probably would not get a commission at ITV or somewhere else, and that is a very valuable purpose, particularly when the big debate across all our creative industries is about diversity. That is a very important issue for us, because if we are to achieve diversity, we should be reaching out a lot more and creating more opportunities for different voices, because those different voices are engaging with our audiences, and those audiences are driving the revenues for investment in the first place. There is a mutual purpose there. There is a lot of talk about the remit. For me, the primary purpose of Channel 4 is to be a door to let people in to a system which can otherwise seem quite hermetically sealed.

**Baroness Kidron**: David Elstein said that fewer smaller indies are now being commissioned by Channel 4. Have you seen evidence of that over the years?

***John McVay:*** Yes, and we have been talking to Channel 4 about how to address that, to make sure that it not necessarily always commissions but it creates relationships with new and different businesses. Anyone can set up as a producer. The barriers to entry are virtually zero. The barriers to failure are equally low: you do not get any work. It is part of Channel 4's purposes, and indeed the BBC's. In fact, the BBC has done a lot better on this over the past few years because it introduced that as a very clear policy. We would encourage Channel 4 to do more of that, particularly out of London, particularly with companies that are bringing more diverse ideas to them, and indeed it has plans to do that. It needs to improve. I would like to answer this question a year from now when we will see where we have got to.

**Baroness Kidron**: John, can I add one little piece to that? There has been a lot of criticism from the broader creative industries, particularly around tech and so on, that we, as a nation, are very good at starting up and disrupting—all those words you have just used—but we sell out too soon and we do not create big, and all the bigs come and buy us.

***John McVay:*** I had a debate on this in Edinburgh with people several years ago. There are a number of reasons why business people sell: age and an exit strategy, 20 or 30 years of working hand to mouth with low margins and opportunity. The problem is not the motivation of the people who are selling; the problem is who is coming to buy. I am on the record as saying that our financial sector is not there for the long term. If you are a tech company in San Francisco you might have repeat investors who will hold your hand for 15 years so you do not sell too soon. We do not have that in the UK and that is a real shame. I have no problem with American or any other media companies buying British businesses, but, too often, they are the only ones that are going to buy them because we cannot get investment from our own financial sector, one of the largest on the planet, because we are seen as too risky. To me the problem is not the motivation for selling but who ends up buying.

**Q40 The Chairman**: I am going to ask each of you whether you want to make any closing remarks, but let me put that into the context of David Elstein's earlier remarks. What he is tempting us to think of as a good idea is entering a process for privatisation which might not necessarily lead to privatisation itself, but opens up the opportunity to be rather tougher in relation to the remit that we give to Channel 4, which he regards now as pretty feeble and emasculated. John, you said we would have to be tough on ITV if we are going to be tough on Channel 4, but they are asymmetrical already and they are not exactly the same regarding regulation. Tell us why, if you think it is so, we should not be tempted by David Elstein's scenario of getting into this, toughening it up and seeing what kind of money people would put on the table for that well-regulated, tougher regime for a new Channel 4?

***John McVay:*** Unfortunately, I did not hear all David's comments as I only came in at the end, so I would not want to second-guess someone of his incredible intellectual abilities and his deep thought on this over many years. I would be concerned at having a false process. It would be very destabilising to everyone—to Channel 4, suppliers and regulators—and you would always be tempted, surely, if you reached the point where you thought it stacked up, to sell it anyway. If the options are, we would sell it/we would not sell it—a sort of binary process—provided that one was still legitimate, that is fair enough, but I think the temptations

would go the other way and you would create a lot of instability and insecurity in the system. I do not know what advertisers would think about that and whether they would be worried about it. You would have to ask them. Because Channel 4's remit is separate from ITV's, there may be an opportunity to consider how that could be toughened up just for Channel 4.
My earlier point was if a non-publicly owned commercial broadcaster were to own Channel 4 and you gave it a remit that was tougher than ITV's, it might feel a bit aggrieved because it is not publicly owned, and ask why it was being held to a worse commercial settlement than ITV, Channel 5, or others would be. If it is merely about Channel 4 ownership, I think there is scope to make sure its remit is properly focused, and the one area we are concerned about is children's programming.
***Colin Browne:*** Much as I like David, I think that particular idea is bonkers, if that is parliamentary language, for some of the reasons John has just given. Why would you go down the route of all that uncertainty? What would it mean for the staff there and for viewers? Also, if you went down that route and in the end you did not privatise it, there would be a sense of failure, and the uncertainty would be huge. Channel 4 has just been given a 10-year franchise. Surely the key thing is to give it the consistency it needs to deliver to its viewers. By all means look at the remit, it can be tightened at any other time, but to think of going down a privatisation route or, even worse, a threatened privatisation route, just to change the remit seems very, very strange.
***John McVay:*** If you were to do that and I was one of the executives, I would look to do a management buyout or compete for it myself, so it would become even more destabilising.
**The Chairman**: Are there final comments from either of you?
***Colin Browne:*** The only final comment I would make is, it would have been great had the Secretary of State been a little more specific as to why he was raising this issue at this time. It might have generated an even better debate, if I can put it that way. We have questioned him. He came to talk to us and he was very generous with his time, but when asked exactly why he was looking at the future of Channel 4 at this time, the answers were pretty vague: there may be a threat or there may be commercial pressures that it cannot withstand. It would have been great had he been a little more specific in his ideas.
**The Chairman**: We are seeing him next week, so we will put those very points to him. Thank you very much indeed for joining us. It has been very helpful.