OFFER BY 21ST CENTURY FOX, INC. FOR THE REMAINING SHARES IN SKY PLC

PRELIMINARY BRIEFING TO THE DEPARTMENT FOR CULTURE, MEDIA AND SPORT

1. INTRODUCTION AND EXECUTIVE SUMMARY

1.1 This briefing paper relates to the offer by 21st Century Fox, Inc. (**21CF**) to acquire the entire issued and to be issued share capital of Sky plc (**Sky**) that 21CF does not already own (the **Transaction**), which was announced pursuant to Rule 2.7 of the City Code on Takeovers and Mergers (the **Code**) on 15 December 2016.[1]

1.2 As DCMS is aware, when News Corporation sought to acquire the remaining shares in Sky (as it then was) in 2010 (the **News Corporation/Sky Bid**), the bid was the subject of intervention by the Secretary of State on public interest grounds relating to media plurality. Given this history, 21CF acknowledges that the Secretary of State may want to consider whether to intervene in the Transaction on those public interest grounds now. The purpose of this briefing paper is therefore to provide DCMS with background information on the Transaction and its context, and explain the change in circumstances that should inform that decision.

1.3 For the reasons expanded upon in this paper, 21CF considers that the Transaction does not raise public interest issues that require an intervention by the Secretary of State. In summary:

(a) the Transaction gives rise to none of the circumstances identified in relevant statutory guidance as circumstances in which the Secretary of State would consider intervention; and

(b) no exceptional circumstances exist that would otherwise justify intervention; and circumstances have changed since the time of the News Corporation/Sky Bid, in particular those resulting from:

(i) the split of News Corporation into two publicly traded companies in June 2013; and

(ii) the transformational impact of the internet on the way in which audiences access news.

1.4 In 2010, the Secretary of State intervened on the footing that the merger then contemplated, in which News Corporation's newspapers and Sky News would be coming under common control, was "akin" to one where a large number of news channels come under single control. The Secretary of State was satisfied that these "exceptional circumstances" warranted his intervention in that case.[2]

1.5 The circumstances of the present Transaction are very different. Since the News Corporation/Sky Bid, the assets of News Corporation were split into two publicly traded companies in June 2013, (new) News Corp and 21CF. 21CF is a diversified global media company with operations in three main industry segments: cable network programming, television and filmed entertainment. 21CF does not own newspapers or radio stations broadcasting in the UK, or news channels targeted at a UK audience. 21CF indirectly holds approximately 39.14% of the issued share capital of Sky.

[1] The announcement is available online at: https://www.21cf.com/sites/default/files/uploaded/investors/rule_2.7_announcement_dated_15_december_2016.pdf

[2] Letter dated 15 November 2010 from Andrew Rees, Deputy Director, Consumer and Competition Policy at the Department for Business, Innovation and Skills to John Pheasant, Partner, Hogan Lovells International LLP (representing News Corporation), headed "NewsCorp/BSkyB Case – Public Interest Intervention".

Accordingly, in determining whether an intervention is warranted in the current circumstances, due account must be taken of the following:

(a) the Transaction does not result in a material reduction in the plurality of controllers of TV news broadcasters, since 21CF's only news outlet available to UK audiences is the Fox News channel, a re-transmission of a US news channel with no UK-specific news programming and marginal audience share;

(b) 21CF no longer holds UK newspaper assets, which are now owned by News Corp, a separate publicly-traded company with majority-independent shareholders and a majority-independent Board of Directors; and

(c) accordingly, the Transaction does not give rise to a cross-media overlap between 21CF and Sky.

1.6 The Transaction will not result in any change to the degree of ownership held by the Murdoch Family Trust (**MFT**) in 21CF or News Corp, which will remain unchanged, at approximately 39% (this is illustrated diagrammatically by Figure 1 in the main body of this paper).

1.7 Even taking into account this degree of common ownership between 21CF and News Corp, the Transaction cannot result in insufficient plurality of news provision in the UK:

(a) the degree of common ownership of newspapers and Sky News resulting from the Transaction would be **less** than existed prior to the News Corporation/Sky Bid:

(i) the News Corporation/Sky Bid would have created a situation in which Sky would have come under the 100% ownership of a company, News Corporation, that also held 100% ownership of several UK newspapers (*The Times, The Sunday Times*, *The Sun* and the *News of the World*);

(ii) in contrast, if the Transaction is carried into effect, the degree of common ownership between Sky and the News Corp newspapers would be limited to a common shareholding of approximately 39%, with two public company boards between them with independent board majorities (and with no independent directors in common);

(iii) on the broadcasting side, this is no greater than the shareholding of News Corporation in Sky that the Competition Commission concluded in the Sky/ITV case had not resulted in influence over the Sky News agenda (see paragraph 4.20 below); and, on the newspaper side, is lower than the control News Corporation had over its 100%-owned titles;

(b) the degree of common ownership is also less than existed in 2003, when the Government considered plurality sufficient to introduce extensive deregulatory measures through the Communications Act 2003 (**CA 2003**), and in 2007, when an in-depth investigation by the Competition Commission into the Sky/ITV case judged plurality was and would remain sufficient;

(c) the Transaction will not increase the scope for co-ordination of the editorial output of the News Corp newspapers and Sky News:

(i) in the News Corporation/Sky Bid, Ofcom was concerned about the impact of operational integration between Sky News and News Corporation's newspapers. This *will not and cannot* occur as a result of the Transaction, since Sky News and the newspapers will remain owned by separate public companies with majority-independent shareholders and majority-independent Boards;

(ii) similarly, the concerns raised in relation to the News Corporation/Sky Bid regarding the loss of independent shareholders and directors as a safeguard for the independence of Sky News are not applicable here, since Sky News and the News Corp newspapers will remain owned by two separate companies with majority-independent shareholders and majority-independent Boards;

(d) the Court of Appeal has confirmed that the extent of control actually exercised over news outlets is relevant to any plurality assessment (see paragraph 4.12 below). In this case the Transaction will not result in common control being exercised over the editorial output of News Corp newspapers and Sky News as:

(i) the only change in ownership resulting from the Transaction is the increase in 21CF's shareholding in Sky. This is inconsequential to an assessment of plurality; and

(ii) Sky News, as a broadcast news provider, is subject to specific regulation that is a significant constraint on a proprietor exercising control over its editorial decisions.

1.8 Accordingly, the impact of the Transaction on "the plurality of persons with control of media enterprises" is very different to that under the contemplated News Corporation/Sky merger in 2010. Moreover the relevant factual context has undergone profound change. 21CF believes the Transaction does not risk reducing plurality for any audience in the UK, still less risk resulting in insufficient plurality within or across media in the UK. 21CF's views on this point are bolstered by the enormous increase in plurality in the UK media since the deregulatory measures of the CA 2003, since the last comprehensive review (by the Competition Commission in the Sky/ITV case) and since the News Corporation/Sky Bid, for reasons including:

(a) the rise of social media such as Facebook and Twitter, which have revolutionised how opinion is formed and the landscape of news provision – traditional media outlets cannot act as gatekeepers that dominate the news agenda and shape public opinion in a world in which consumers are in direct contact with key opinion-formers and can readily share news and opinions with large groups at once;

(b) the entry and expansion of distinctive new players facilitated by the low barriers to entry for news provision on the internet and, more generally, the shift of consumption from print to online;

(c) aggregators (such as Google News and Apple News) and social media (such as Facebook and Twitter) are reshaping consumption of online news, leading consumers to a range of sources and thereby supporting multi-sourcing. Smartphones contribute to this trend by making news available at any time, with users also reading more titles on average than in print; and

(d) the presence of the BBC as by far the largest news provider within radio, TV and online and across platforms, which is expected to continue for the foreseeable future.

1.9 21CF therefore believes that there would be a firm basis for the Secretary of State to conclude that her intervention in the Transaction is unnecessary. However, 21CF also recognises that the Secretary of State may wish to obtain Ofcom's advice on these matters. 21CF would be keen to engage with DCMS and, subject to DCMS' views, Ofcom at the earliest opportunity to discuss what further evidence may be desirable and the timing that is currently envisaged for any decision. 21CF would also like to keep DCMS apprised of the progress towards notification to the European Commission and discuss the impact that this would have on the DCMS decision-making process.

1.10 As an initial step, 21CF would be happy for DCMS to share this paper with Ofcom and the CMA, should it wish to do so. However, given the highly sensitive nature of the matters discussed in this paper, 21CF asks that DCMS, and, if shared with them, Ofcom and the CMA, observe all appropriate safeguards to protect confidential information. The information provided should not be disclosed beyond the relevant case teams at DCMS, Ofcom and the CMA without 21CF's prior written consent.

2. THE PARTIES AND THE TRANSACTION

21CF

2.1 21CF is a diversified global media company with operations in three main industry segments: cable network programming, television and filmed entertainment. 21CF is a Delaware corporation whose shares are listed and traded on the NASDAQ Global Select Market.

2.2 21CF owns a global portfolio of cable and broadcasting networks and properties including FOX, Fox Networks Group, National Geographic and STAR, the film studio Twentieth Century Fox Film, and television production studio Twentieth Century Fox Television. In addition to its interest in Sky (see further below), 21CF holds equity interests in the online video service Hulu in the US, the Endemol Shine/CORE Media TV production joint venture, the Indian satellite TV platform operator Tata Sky and a 5% stake in the digital media company VICE.

2.3 21CF formerly owned the Sky Italia and Sky Deutschland direct broadcast satellite TV businesses, principally active in Italy and Germany and Austria respectively. In November 2014, 21CF sold its interests in these businesses to Sky.

2.4 In the UK, 21CF's principal activities involve the licensing and distribution of audio-visual works for theatrical exhibition, television and home entertainment viewing, and the wholesale supply of TV channels. 21CF does not own newspapers or radio stations broadcasting in the UK; nor does it own news channels targeted at a UK audience.[3]

Separation of News Corporation into 21CF and News Corp

2.5 On 28 June 2013, News Corporation completed the separation of its business into two independent publicly-traded companies, by distributing to its shareholders shares in a newly-formed entity known as (new) News Corporation (referred to in this paper as **News Corp**, as distinct from the former News Corporation). As described in the materials sent to shareholders in connection with the separation, the board of News Corporation determined that it was in the best interests of its shareholders for its businesses to be separated into to independent companies, one focused on media and entertainment, the other on newspapers and publishing, which could then "focus on and pursue distinct strategic priorities and industry-specific opportunities".[4]

2.6 News Corporation changed its name to 21CF and retained interests in cable network programming, television, satellite broadcasting and filmed entertainment.

2.7 News Corp holds News Corporation's former businesses including newspapers, information services and integrated marketing services, digital real estate services, book publishing, digital education and sports programming and pay-TV distribution in Australia. News Corp's operations in the UK are principally conducted through News UK and HarperCollins.[5] News UK publishes the following newspaper titles in print and digital formats: *The Times, The Times Literary Supplement* (a weekly periodical literary review), *The Sunday Times*, *The Sun*, *The Sun on Sunday* and *Sun Online* (the combined online offering of *The Sun* and *The Sun on Sunday*). News Corp also recently acquired Wireless Group, which in the UK operates the talkSport, talkRadio and Virgin Radio UK national radio stations, as well as a portfolio of predominantly music-based local radio stations.

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[3] The US-focused Fox News channel is available in the UK on the Sky platform, with a very limited UK viewership.
[4] Definitive Proxy Statement for the special meeting of stockholders held on 11 June 2013, Annex C, *Reasons for the distribution*.
[5] News Corp also owns Dow Jones and the *Wall Street Journal*, which have offices located in London.

The Murdoch Family Trust

2.8 Following the separation described above, the MFT (in conjunction with other small interests associated with K. Rupert Murdoch) holds approximately 38.9% of 21CF's Class B Common Stock and approximately 39.4% of News Corp's Class B Common Stock.

2.9 Certain members of the Murdoch family serve as officers and/or directors of News Corp and 21CF. K. Rupert Murdoch serves as News Corp's Executive Chairman and Executive Chairman of 21CF; Lachlan K. Murdoch serves as News Corp's Co-Chairman and Executive Chairman of 21CF, and James R. Murdoch is a member of News Corp's Board and serves as CEO of 21CF. However, the boards of both 21CF and News Corp comprise a majority of independent directors (none of whom serve on both boards).

Corporate governance at 21CF

2.10 The Board of 21CF comprises 13 directors, of which a majority of eight are independent directors under applicable US corporate governance rules. The independent directors are Sir Roderick I. Eddington (lead director), Delphine Arnault, James W. Breyer, Viet Dinh, Jacques Nasser, Robert S. Silberman, Tidjane Thiam and Jeffrey W. Ubben. The committees of the Board include two committees with responsibility for corporate governance matters, both of which are composed exclusively of independent directors: the Audit Committee (chaired by Sir Roderick Eddington) and the Nominating and Corporate Governance Committee (chaired by Viet Dinh).

2.11 In addition to the Audit Committee, the Nominating and Corporate Governance Committee and the majority of independent directors on 21CF's Board, 21CF has adopted strong governance measures and controls to ensure it meets the highest standards of corporate conduct. In April 2012, the company established an enhanced global compliance programme, including a global compliance steering committee under the leadership of the general counsel and chief compliance officer. Amongst other things, these arrangements provide for the rapid escalation of material issues from individual businesses through the compliance steering committee to the independent directors of the Audit Committee and the full Board.

Sky

2.12 Sky is a multi-territory entertainment and communications company active through a number of subsidiaries in the provision of satellite broadcasting, on-demand online streaming, broadband and telephone services. Sky is a public company whose shares are listed on the London Stock Exchange.

2.13 Sky retails subscription television services to residential and commercial premises in the UK, Ireland, Germany, Austria and Italy.[6] Sky also produces a range of TV channels that it makes available to retail subscribers on its own and third party TV platforms and supplies on a wholesale basis to other retailers. Sky's other businesses include the sale of advertising on its own and partner channels and its international distribution operation and the sale of communications services in the UK and Ireland.

2.14 Sky's portfolio of TV channels includes Sky News, a 24-hour international news channel available in the UK to Sky's pay-TV subscribers, and other retail pay TV services and on free-to-air TV. Outside of the UK, Sky also offers Sky News International, a channel which has the same news content as Sky News but without UK adverts, in Europe, Africa, Asia and the US. In addition to these news channels, Sky provides rolling news content in the form of bulletins and articles on its website, as well as on a range of mobile devices. Sky News is provided under licences held by Sky's subsidiary Sky UK Limited.

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6 As noted above, in November 2014 Sky acquired 21CF's interests in Sky Italia and Sky Deutschland.

2.15 Sky also owns and operates Sky News Radio, the radio arm of Sky News, which supplies news to the Independent Radio News (**IRN**) network of radio stations in the UK. The IRN network provides more than 280 stations (including well-known brands such as Absolute Radio, Capital, Classic, Heart, Magic, LBC, Smooth and talkSport) with a continuous service of national and international news, comprising live hourly news bulletins, scripts, audio clips and a suite of pre-recorded news content. Stations incorporate this content into the bulletins they prepare, or at certain times simply rebroadcast the bulletin created by Sky News Radio. Sky News Radio also supplies digital content such as news stories in text and video to the websites of the IRN network radio stations.[7]

2.16 Between January 2005 and February 2012, Sky News provided news data and content to Channel 5. This arrangement ended in February 2012, when the Channel 5 contract switched to ITN.

21CF's shareholding in Sky

2.17 21CF was a founding shareholder of Sky and has remained its major shareholder since it was listed in 1994. 21CF currently holds approximately 39.14% of the issued share capital of Sky and controls 37.19% of the voting rights in Sky.[8]

2.18 Since Sky's public listing in 1994, a number of the directors on the Board of Sky have been affiliated with 21CF at the same time as holding their office. At present, of the 11 directors of Sky, the following three hold office at 21CF.

(i) **Mr James R. Murdoch** (Chairman of Sky since April 2016, previously CEO (2003-2007) and Chairman (2007-2012) is the CEO of 21CF (appointed in June 2015). Mr Murdoch previously served as Co-Chief Operating Officer and Chairman and CEO for Europe and Asia of 21CF and CEO (2003-2007) and Chairman (2007-2012) of Sky.

(ii) **Mr Chase Carey** (non-executive director of Sky since January 2013) is the Vice Chairman of 21CF. Mr Carey previously served as President, Chief Operating Officer and Deputy Chairman (2009-2015) and Executive Vice Chairman of 21CF (July 2015 to July 2016).

(iii) **Mr John Nallen** (non-executive director of Sky since November 2015) is Senior Executive Vice President and Chief Financial Officer of 21CF (appointed in November 2015). Mr Nallen previously served as Senior Executive Vice President and Deputy Chief Financial Officer of 21CF (2001-2013).

2.19 The UK authorities have previously found that 21CF has a degree of commercial influence over Sky that may be deemed to give "control" for the purposes of the EA 2002.[9]

The Transaction

2.20 The Transaction contemplates the acquisition by 21CF of up to 100% of Sky's shares. Following the implementation of the Transaction, 21CF would exercise sole control over Sky.

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7 However, as Ofcom has noted other commercial radio operators source, produce and broadcast their own news content including the two largest commercial radio operators in the UK, Global and Bauer Radio: see Ofcom's News Consumption in the UK 2015 Executive Summary at footnote 17 and Ofcom's Advice to the Secretary of State on a Measurement Framework for Media Plurality at 3.40 – 3.42.

8 Pursuant to a voting agreement dated 21 September 2005 between 21CF, Sky and affiliated entities, the voting rights that 21CF can exercise at general meetings of Sky are capped at 37.19%.

9 Most recently, in its report to the Secretary of State on the News Corporation/Sky Bid, the Office of Fair Trading stated that "At present, News Corporation already owns 39.14 per cent of Sky and may therefore already exercise some degree of control over Sky for the purposes of the Act. That is, the ability to control or materially influence the policy of Sky, but without having a controlling interest in Sky." (paragraph 15 and footnote 7 of the report).

2.21 The Transaction is subject to the Code and, as noted, was announced publicly pursuant to Rule 2.7 of the Code on 15 December 2016 (following the announcement of a possible offer pursuant to Rule 2.4 of the Code on 9 December 2016). The Transaction has been recommended to Sky's shareholders by the independent directors of Sky. It is envisaged that the Transaction would be implemented by way of a court-approved scheme of arrangement.

2.22 The acquisition of the entire share capital of Sky brings clarity to 21CF's capital allocation strategy and constitutes an opportunity for 21CF to achieve financial consolidation with a company in which it has held a substantial stake from the outset. The Transaction will also allow 21CF to diversify its activities geographically, by acquiring a significant presence in markets where its activities in the TV sector are limited, and to diversify its sources of earnings towards more stable subscription-based revenues.

<u>Review under the EUMR</u>

2.23 The Transaction would be a concentration with a Union dimension requiring notification to the European Commission under the EU Merger Regulation (**EUMR**)[10] for review of its possible effects on competition, because:

(a) 21CF does not currently exert "decisive influence" over Sky for the purposes of the EUMR, but would acquire decisive influence over Sky through the Transaction; and

(b) the jurisdictional thresholds under the EUMR would be met, since in the most recent financial year:

(i) the combined worldwide turnover of 21CF and Sky exceeded EUR 5 billion;

(ii) each of 21CF and Sky generated turnover in the European Union exceeding EUR 250 million; and

(iii) 21CF and Sky did not generate more than two-thirds of their EU turnover in one and the same Member State.

2.24 21CF considers that the Commission is the most appropriate authority to review the Transaction's possible effects on competition, taking into account its experience in the context of the News Corporation/Sky Bid and the fact that, as explained above, Sky has since expanded its operations within the EU, including to Italy, Germany and Austria.

2.25 21CF submitted a request for the European Commission to allocate a case team (the first step in the EUMR process) on 16 December 2016 and envisages that the customary pre-notification discussions will commence in substance in early January 2017.

3. LEGAL FRAMEWORK

<u>Overview of the legal framework for public interest intervention</u>

3.1 The statutory framework for media plurality regulation is set out in the Communications Act 2003 (**CA 2003**) and the Enterprise Act 2002 (**EA 2002**). The CA 2003 sets out general regulatory provisions that require Ofcom to secure, in carrying out its principal duty, ends that include the maintenance of a sufficient plurality of providers of TV and radio services; lays down certain media ownership rules relating to TV, radio and newspapers; and requires Ofcom to conduct regular reviews of those rules.

10 Council Regulation (EC) No. 139/2004 on the control of concentrations between undertakings.

3.2 The EA 2002 sets out the regime for public interest intervention in media mergers. Read in conjunction with relevant secondary legislation[11] and Article 21 of the EUMR, it permits the Secretary of State to intervene in mergers subject to the exclusive competition jurisdiction of European Commission under the EUMR (as the Transaction would be) by serving an intervention notice that cites one or more of the public interest considerations specified under section 58 of the EA 2002. This triggers a review of the transaction's effects with regard to that or those public interest considerations, in which the Secretary of State has the power to decide whether there is a public interest concern that warrants further investigation by the Competition and Markets Authority (**CMA**) and, ultimately, to determine any remedies to address those concerns. The European Commission retains exclusive jurisdiction to assess the effects of the transaction on competition.

3.3 The public interest considerations specified under section 58 of the EA 2002 that relate to media mergers are the following:

(a) the need for accurate presentation of news and free expression of opinion in newspapers (section 58(2A));

(b) the need for, to the extent that it is reasonable and practicable, a sufficient plurality of views in newspapers in each market for newspapers in the United Kingdom or a part of the United Kingdom (section 59(2B));

(c) the need, in relation to every different audience in the United Kingdom or in a particular area or locality of the United Kingdom, for there to be a sufficient plurality of persons with control of the media enterprises serving that audience (section 58(2C)(a)):

(d) the need for the availability throughout the United Kingdom of a wide range of broadcasting which (taken as a whole) is both of high quality and calculated to appeal to a wide variety of tastes and interests (section 58(2C)(b)); and

(e) the need for persons carrying on or controlling media enterprises to have a genuine commitment to the attainment of the broadcasting standards objectives set out in section 319 of the CA 2003 (section 58(2C)(c)).

3.4 The concept of "plurality" used in section 58(2C)(a) of the EA 2002 has been considered in numerous regulatory reviews and inquiries in recent years. There is a broad consensus that the focus of any public interest test on the basis of this consideration should be on news and current affairs content, rather than other genres. This reflects that the underlying rationale for media plurality regulation is located in the importance of media plurality for a healthy and informed democratic society. This was confirmed by the Competition Commission in its public interest review of Sky's acquisition of a 17.9% shareholding in ITV plc (**Sky/ITV**).

> *The parties overlap in a broad range of content, but news and current affairs are the genres most closely connected with the formation of public opinion about issues of national significance through the communication of a range of information and views. National news is an important genre of programming for both ITV and Sky. Considering all content genres, including current affairs, documentaries and satire, viewers rank news first in terms of 'societal importance', with a majority of the public saying that news helps them feel part of the democratic process. We also believe that news provision is a reasonable indicator of, and better defined than, a wider range of other content relevant to the formation of public opinion about issues of national significance. We therefore focused on national news and*

[11] The Enterprise Act 2002 (Protection of Legitimate Interests) Order 2003.

refer to the range of information and views communicated to audiences through the news as the 'plurality of news'.[12]

3.5 Ofcom applied this approach in subsequent public interest reviews into the News Corporation/Sky Bid[13] and Global Radio's acquisition of Guardian Media Group's radio stations.[14]

3.6 In November 2015, at the request of the Secretary of State and following a process of consultation, Ofcom published a measurement framework for media plurality. The framework contemplates the use of quantitative measurements of the availability, consumption and impact of different news sources, but crucially in conjunction with a qualitative assessment of all "contextual factors" that, while not quantifiable, are relevant to an understanding of plurality (discussed further below).[15] Ofcom observes that "It is important to note that contextual factors are an integral, rather than a supplementary part of the framework".[16]

Intervention in the News Corporation/Sky Bid

3.7 As DCMS is aware, in 2010 News Corporation sought to acquire the shares in Sky that it did not already own. The bid was announced pursuant to Rule 2.4 of the Code on 15 June 2010 and notified to the European Commission under the EUMR on 3 November 2010. On 21 December 2010, the European Commission cleared the bid unconditionally, following a first-phase review.

3.8 On 4 November 2010, the Secretary of State issued an intervention notice specifying the public interest consideration in section 58(2C)(a) of the EA 2002 (the need for a sufficient plurality of persons with control of media enterprises). Following a report in which Ofcom recommended that the transaction be referred to the Competition Commission for an in-depth review, the parties offered undertakings in lieu of reference. After extensive interaction between the parties, DCMS, Ofcom and the OFT on the terms of those undertakings, and positive reports from Ofcom and the OFT on the effectiveness and viability of the revised undertakings, the Secretary of State on 30 June 2011 announced that he was minded to accept those undertakings and not refer the bid. However, before a final decision was reached, News Corporation withdrew the undertakings for reasons unrelated to the bid. On 11 July 2011, the Secretary of State therefore referred the bid to the Competition Commission for an in-depth review. The bid was abandoned two days later.

Application of the DTI Guidance to the Transaction

3.9 The Secretary of State has published statutory guidance pursuant to section 106A of the EA 2002 on the circumstances in which she would expect to intervene in a media merger on public interest grounds (the **DTI Guidance**).[17] The DTI Guidance sets out the Secretary of State's policy that, other than in "exceptional circumstances", she will consider intervention only in cases where the transaction would otherwise have been governed by media ownership rules that have been removed by the Communications Act 2003. The cases that come within this category relate to mergers involving:

(a) owners of national newspapers with a market share in excess of 20% and the Channel 5 licence holder;

12 Competition Commission report, Acquisition by Sky of 17.9 per cent of the shares in ITV plc, 14 December 2007, paragraph 5.32.
13 Ofcom, Report on public interest test on the proposed acquisition of Sky by News Corporation, 31 December 2010, paragraphs 3.2 and 3.3.
14 Ofcom, Report on public interest test on the acquisition of Guardian Media Group's radio stations (Real and Smooth) by Global Radio, 11 October 2012, paragraph 1.17.
15 Ofcom, Measurement framework for media plurality: Ofcom's advice to the Secretary of State for Culture, Media and Sport, 5 November 2015 (**Ofcom Measurement Framework**), paragraph 1.20.
16 Ofcom Measurement Framework, paragraph 3.16.
17 Department for Trade and Industry, Enterprise Act 2002: Public Interest Intervention in Media Mergers – Guidance on the operation of the public interest provisions relating to newspaper and other media mergers, May 2004.

(b) owners of national newspapers with a market share in excess of 20% and a national radio service;

(c) Channel 3 and national radio;

(d) Channel 5 and national radio;

(e) two or more national radio stations;

(f) Channel 3 or the national ITV licence holder and Channel 5; or

(g) a takeover of a Channel 3 licence holder.[18]

3.10 None of these scenarios would arise as a result of the Transaction.

3.11 The DTI Guidelines envisage that "exceptional circumstances" warranting intervention outside the scenarios listed above may exist in the following three cases:

(a) a transaction bringing a large number of news or educational channels under common control;

(b) a transaction involving all the music channels coming under the control of a single person; or

(c) a prospective new entrant to local radio ownership has not shown a genuine commitment to broadcasting standards in other media or countries.[19]

3.12 Again, none of these scenarios would arise as a result of the Transaction.

3.13 Nor is there any other reason to consider the Transaction an "exceptional" case that warrants intervention. As the DTI Guidance makes clear, an adverse public interest finding in terms of the broadcasting and cross-media consideration set out in section 58(2C)(a) of the EA 2002 is possible only where concerns are identified that meet a very stringent legal threshold. Specifically, an adverse public interest finding would require that the Transaction would lead to a "*significant* reduction in plurality in relation to any relevant audience" and thereby result in "*unacceptable* levels of media and cross-media *dominance*" that undermined even a "*minimum* level of plurality" (emphases added).[20]

3.14 As the remainder of this paper explains, there is no basis for such a conclusion here.

4. NO EXCEPTIONAL CIRCUMSTANCES JUSTIFY INTERVENTION

<u>The Transaction will not materially reduce the plurality of controllers of TV news</u>

4.1 The principal activity of Sky relevant to the media public interest test is the Sky News TV channel.

4.2 There is no material overlap between this activity and 21CF's business. The sole TV news outlet owned by 21CF that is accessible by viewers in the UK is the Fox News channel, which is available on the Sky platform. This is a retransmission of a US news channel with no UK-specific news

18 DTI Guidance, paragraph 8.2.
19 DTI Guidance, paragraph 8.8.
20 DTI Guidance, paragraphs 7.7 and 7.11.

programming, and has only a marginal viewership in the UK.[21] Its share of viewing in November 2016 was 0.02%.[22]

No cross-media overlap between 21CF and Sky

4.3 As a result of the separation of News Corporation's businesses in 2013, 21CF is not active in the UK newspaper or radio sectors. The UK newspaper assets formerly held by News Corporation are now owned by a separate, publicly-traded company, News Corp. As such, no overlap arises between 21CF and Sky on a cross-media basis.

The Transaction will not change the degree of common ownership between 21CF and News Corp

4.4 The Transaction does not involve any increase in the MFT's stake in 21CF or News Corp. Accordingly, there is no change to the degree of common ownership between the two companies and their media assets, which will remain limited to approximately 39%.

The degree of common ownership of newspapers and Sky News would be less than existed prior to the News Corporation/Sky Bid

4.5 As described above, the MFT holds a significant minority shareholding in both News Corp and 21CF. However, the end-result of the Transaction would nevertheless be to bring about a significantly different situation in terms of plurality to that which would have been created had the News Corporation/Sky Bid been carried into effect.

(a) The News Corporation/Sky Bid would have created a situation in which Sky would have come under the 100% ownership of a company, News Corporation, that also held 100% ownership of several UK newspapers (*The Times, The Sunday Times, The Sun* and the *News of the World*).

(b) In contrast, if the Transaction is carried into effect, the degree of common ownership between Sky and the News Corp newspapers would be limited to a common shareholding of approximately 39% in both companies held by the MFT.[23]

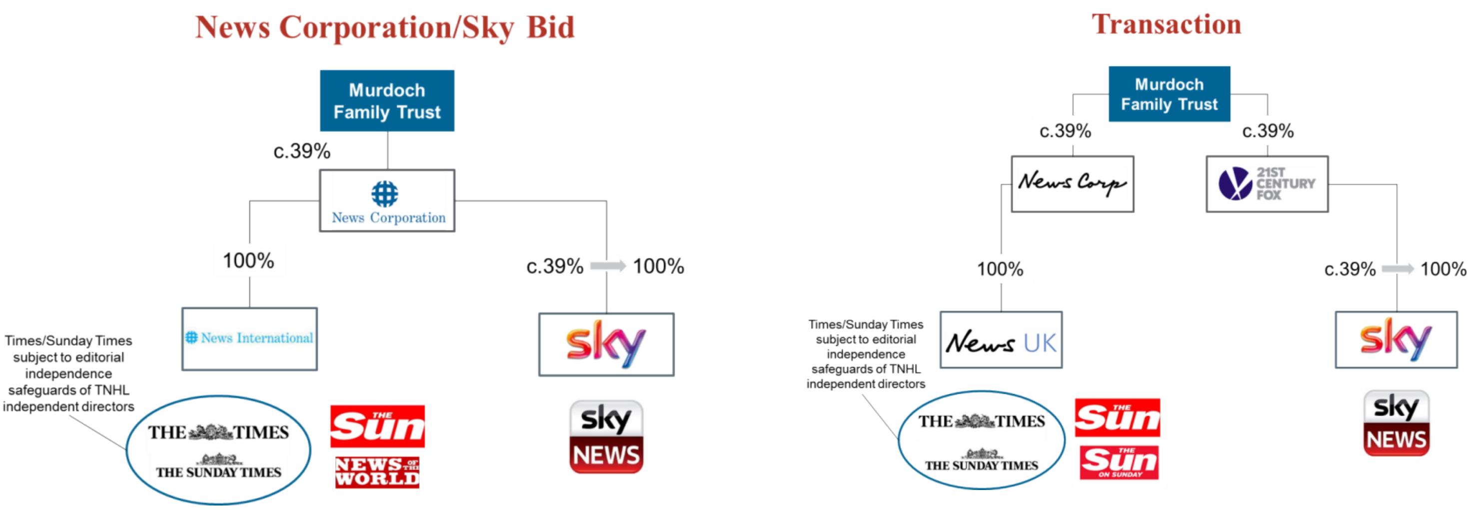
4.6 In fact, the degree of common ownership between Sky and the News Corp newspapers resulting from the Transaction would be less than the level that existed *prior to* the News Corporation/Sky Bid. News Corporation then held an interest of approximately 39% in Sky (similar to the interest of the MFT in Sky that would result from the Transaction) and full ownership of the relevant newspapers (considerably *greater* than the approximate 39% interest held by the MFT in News Corp). These points are illustrated in the diagram below.

21 According to Ofcom research, significantly less than 1% of UK adults who use TV for news use Fox News. Source: Ofcom, News Consumption in the UK 2015, data table 34.

22 BARB

23 While News Corp now owns the radio stations operated by Wireless Group, this is not a material point of differentiation to the situation in 2010. The Wireless Group stations participate in the IRN network and therefore receive news content from Sky News Radio.

Figure 1: Comparison of News Corporation/Sky Bid and the Transaction



<u>The degree of common ownership would also be less than existed at the time of previous reviews that judged plurality to be sufficient in the UK</u>

4.7 It follows that the degree of common ownership post-Transaction would also be less than existed at the time of previous in-depth governmental and regulatory reviews that concluded plurality was sufficient in the UK:

(a) in 2003, when the Government introduced extensive deregulatory measures regarding media ownership through the CA 2003, which must necessarily have been premised on the conclusion that plurality in the UK media was sufficient; and

(b) in 2007, when the Competition Commission conducted its most recent in-depth review of plurality in the UK, following intervention by the Secretary of State in Sky's acquisition of a 17.9% stake in ITV. The Competition Commission concluded that plurality would remain sufficient in the UK following that transaction, and the Court of Appeal upheld this conclusion.

<u>The Transaction will not increase the scope for co-ordination of the editorial output of News Corp newspapers and Sky News</u>

4.8 As explained above, the degree of common ownership between the News Corp newspapers and Sky News would be **less** than would have resulted from the News Corporation/Sky Bid, and also **less** than existed prior to that bid; limited to a c.39% common shareholding in both companies. It is relevant in this respect that the concerns identified by Ofcom's report into the News Corporation/Sky Bid were necessarily premised on the basis that the implications for plurality of bringing media enterprises under full common ownership differ significantly from those of a situation in which outlets are deemed to be under common control on the basis of material influence; a situation which existed prior to that bid.[24]

4.9 In particular, in its 2010 report on the News Corporation Sky/Bid, Ofcom had concerns that once the News Corporation newspapers and Sky news were under 100% common ownership, internal plurality could not be guaranteed and could not be relied on to ensure plurality overall. However, these conclusions were specifically tied to "circumstances of 100% ownership and control",[25] which will not exist in the case of the Transaction.

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24 See paragraphs 1.16 and 1.17 of Ofcom's report.
25 Ofcom report on the News Corporation/Sky Bid, paragraph 5.125.

4.10 There are clear reasons why any such concerns do not arise in relation to the Transaction, which will not increase the scope for of co-ordination of the editorial output of News Corp newspapers and Sky News.

(a) Ofcom's conclusion that internal plurality in respect of the News Corporation/Sky Bid would have been undermined by a process of operational integration between Sky News and News Corporation's news titles resulting from 100% ownership by News Corporation[26] is simply not relevant to the Transaction. Since News Corporation's former news titles are now owned by News Corp rather than 21CF, operational integration between those titles and Sky News cannot result from the Transaction.[27]

(b) Ofcom's conclusions relating to internal plurality were also influenced by representations arguing that internal plurality could not be guaranteed because the transaction would result in the loss of independent shareholders and independent directors as a safeguard for the independence of Sky News.[28] However, in the present Transaction, Sky News and the News Corp **will** remain under the ownership of separate companies and both will continue to have independent shareholders and boards comprising a majority of independent directors, so this concern does not arise.

4.11 The undertakings offered by News Corporation and provisionally agreed by the Secretary of State in the News Corporation/Sky Bid were aimed at maintaining the pre-existing degree of separation of Sky News from News Corporation's newspaper business. In the present Transaction, this issue no longer arises. Such separation is *already* achieved by the split via two publicly-traded companies. In fact, the degree of separation is greater, since the degree of common ownership with the newspapers is weaker, limited to the 39% interest of the MFT.

The Transaction will not result in common control being exercised over the editorial output of News Corp newspapers and Sky News

4.12 It is clearly established that in reviewing the effects of a transaction on media plurality, the Secretary of State and Ofcom must consider the extent of control actually exercised over media outlets that are under common ownership. The Court of Appeal held in its judgment on Sky/ITV that:

> *when it comes to assessing the plurality of the aggregate number of relevant controllers and to considering the sufficiency of that plurality, the Commission may, and should, take into account the actual extent of the control exercised and exercisable over a relevant enterprise by another, whether it is a case of deemed control resulting from material influence under section 26 or rather one of actual common ownership or control.*[29]

4.13 The need to consider the extent of common control actually exercised, and therefore the diversity of views, between media outlets under common ownership (so-called "internal plurality") is also acknowledged in Ofcom's measurement framework.[30]

4.14 There are strong reasons why, whatever the results of the News Corporation/Sky Bid might have been, the present Transaction would not result in common control actually being exercised over the News Corp newspapers on the one hand and Sky News on the other.

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26 Ofcom report on the News Corporation/Sky Bid, paragraphs5.61-5.65.

27 Such integration would also be inconsistent with the rationale for the separation of 21CF and News Corp, which, as noted, was based on the judgment that it would be in the best interests of shareholders for the two companies' businesses to be carried on separately. In this context, the companies' independent shareholders and directors could be expected to challenge such measures, even if they were practicable (which is not the case).

28 Paragraph 5.59 of Ofcom's report.

29 *Sky v Competition Commission* [2010] EWCA Civ 2, at paragraph 121.

30 Ofcom, Measurement Framework, paragraphs 1.20 and 3.17.

(a) Whereas the News Corporation/Sky Bid would have brought these outlets under the full ownership of a single company, News Corporation, the Transaction will leave them under the ownership of separate publicly-traded companies, News Corp and 21CF. Ofcom's measurement framework confirms the importance of this point, recognising the applicable "governance models (such as […] publicly limited companies with shareholders)" as a relevant contextual factor.[31]

(b) The only change in ownership resulting from the Transaction is the increase in 21CF's shareholding in Sky. However, as explained below, Sky, as a broadcast news provider, is subject to specific regulation and other factors that make it highly unlikely this would actually equate to increased control over the editorial decisions of Sky News, and in any event the change would not result in a reduction of TV, radio or cross-media plurality.

4.15 Further, editorial independence from proprietorial influence of The Times and The Sunday Times is also guaranteed by protections embedded within the governance structure of Times Newspaper Holdings Limited (**TNHL**), the holding company for those newspapers, including that the six independent directors of TNHL must approve the appointment or dismissal of each of the editors of The Times and The Sunday Times. The Transaction will have no impact on these existing protections.

Sky News will remain editorially independent within Sky

4.16 Sky News is subject to the impartiality requirements of the Broadcasting Code; contravention of which could result in the loss of its licence. This requires that television news be presented with due impartiality, and specifically prohibits expressions of the views or opinions of the person providing the service on matters of political or industrial controversy and matters relating to current public policy.[32]

4.17 This provides a significant constraint on the ability of a proprietor (regardless of its level of shareholding) to exert control over the output of Sky News.

4.18 The same obligations apply in respect of radio news under the Broadcasting Code and provide a similar check on the possibility of influencing the content supplied on a wholesale basis by Sky News Radio.

4.19 The importance of this contextual factor was acknowledged by the Competition Commission in Sky/ITV[33] and confirmed in Ofcom's measurement framework for media plurality, which notes the importance of "regulation and oversight, in some cases based on statutory obligations – e.g. Ofcom's Broadcasting Code".[34]

4.20 That ownership does not equate to control in respect of Sky News is borne out by the fact that 21CF, despite its long-standing interest in Sky, does not exert editorial influence over Sky News. This was acknowledged by the Competition Commission in its report on Sky/ITV. Indeed, the Competition Commission found that *Sky*, despite its *100*% ownership of Sky News, did not exert influence over Sky News' agenda.

[31] Ofcom Measurement Framework, paragraph 3.17.
[32] Paragraphs 5.1 and 5.4 of the Broadcasting Code, reflecting the standards objectives in sections 319(2)(c) and 320 of the CA 2003.
[33] "In television news, existing regulatory mechanisms – including quality controls (eg in the Broadcasting Code), requirements for impartiality and quotas for television news and current affairs programming – reduce the scope for influence over editorial decisions by owners of television channels which broadcast news." (paragraph 5.54)
[34] Ofcom Measurement Framework, paragraph 3.17.

Sky […] emphasized the role of their editorial staff in determining the day-to-day content of their programming. Sky told us that all editorial decisions regarding the content of Sky's various news services were taken by the Sky News editorial staff […] ***We received no evidence from third parties to suggest that senior executives at Sky or its parent companies exerted influence on the Sky News agenda****.* [35] (Emphasis added.)

4.21 The Transaction will have no impact on this conclusion.

<u>Plurality has increased since 2010</u>

4.22 If the Secretary of State were to intervene in the Transaction on the basis of the public interest consideration in section 58(2C)(a) of the EA 2002, the question to be decided would not simply be whether the Transaction would reduce plurality, but whether, as a result, there would no longer be "sufficient plurality".

4.23 It is therefore relevant that the plurality of the UK media is high, and, moreover, has grown since 2010 as technological change continued to transform news consumption.

(a) The lower barriers to entry for online media have enabled a range of news providers to enter the market and grow. For instance, Huffington Post and Buzzfeed have launched UK editions since 2010, and they now have online reach of 22% and 19% respectively (ahead of Sky News and Johnston Press).[36]

(b) The internet is also reshaping shares of consumption. For instance, while the *Sun* remains (just) the largest newspaper by print circulation, on the internet it is behind the *Guardian*, the *Mail*, the *Mirror* and the *Telegraph*, which are (in descending order) the leading titles by online reach.[37]

(c) Aggregators (such as Google News and Apple News) and social media (such as Facebook and Twitter) are reshaping consumption of online news, leading consumers to a range of sources and thereby supporting multi-sourcing.[38] Ofcom's research found that already in 2015, Facebook was the third most used source of news in the UK (on a 'share of references' basis), behind only the BBC and ITV. Facebook was as large as Sky News, the *Times* and the *Sun* combined across all platforms.[39] (More than ten minutes of every hour spent online is now spent with Facebook).[40]

(d) Consumption is shifting to online from print. Since 2010, daily print circulations are down 39%. (The *Sun* has seen a 46% decline). This is a shift to a platform with greater multi-sourcing, and overall the number of sources used across all platforms has increased from 2.9 to 3.5.[41]

(e) Smartphones are important contributor to this trend. They make news available at any time. Moreover, since news on phones is often consumed via social media or aggregators, a wider range of sources are used. For example, those reading newspapers in print use, on average, 1.77 titles. Those reading newspapers on smartphones read 3.93 titles.[42]

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35 Paragraph 5.57.
36 Comscore, *Digital-native Millennials embrace 'traditional' media outlets*, 29 September 2016.
37 Communications Chambers analysis of NRS, *NRS NPADD September 2016*, 29 November 2016.
38 Consumption by individual consumers across a diverse range of sources.
39 Ofcom, *News consumption in the UK: research report,* 15 December 2015.
40 UKOM, *UK Digital Market Overview – September 2016*, October 2016.
41 Ofcom, *News consumption in the UK: research report;* Ofcom, Report on public interest test on the proposed acquisition of British Sky Broadcasting Group plc by News Corporation, December 2010.
42 Communications Chambers analysis of NRS, *NRS NPADD September 2016*, 29 November 2016.

(f) Social media has revolutionised how opinion is formed and the landscape of news provision. It has undermined the ability of traditional news outlets to shape public opinion. Social media places consumers in direct contact with key opinion-formers such as politicians, business leaders, commentators and celebrities and enables them to readily share news and opinions with large groups at once. In this world media companies no longer act as gatekeepers, nor control the news agenda. For example, the Number 10 account has 4.8m followers on Twitter, larger than the readership of any print newspaper, and the Mayor of London has 2.5m followers. In 2012 Donald Trump said explicitly that a large Twitter following is "like having your own newspaper",[43] and since the 2016 election he has commented "[t]he fact that I have such power in terms of numbers with Facebook, Twitter, Instagram, etc., I think it helped me win all of these races where they're spending much more money than I spent".[44]

4.24 The increase in plurality brought about by these developments is even more remarkable when set against the situation in 2003 and 2007, when, as noted, plurality was judged to be sufficient by the Government and by the Competition Commission. The media and technologies described above, which have since transformed the media landscape, were scarcely present in the UK in 2003 (when, for example, broadband penetration was around 5%, the 3G rollout had only just begun, smartphones were unheard of and Facebook did not exist) and were significantly less developed in 2007 (when, for example, Twitter had only launched the previous year and was yet to attract a substantial user base).

4.25 At the same time, the BBC remains by far the leading news supplier, with the largest presence in each of TV, radio and online. Indeed, its importance is growing as news consumption shifts away from print, the one sector it does not lead. Its 'share of references' is almost five times that of its nearest rival, ITV.[45] By contrast, Sky News' share has remained roughly flat since 2010 (in terms of news viewing share, 6.5% in 2015 vs. 6.3% in 2010[46]; in terms of share of references at retail level, 6% in 2015 vs. 5% in 2010[47]). The BBC is highly likely to remain strong, with the Royal Charter expected to be renewed for another term extending through to 2027.[48]

5. CONCLUSION

5.1 For the reasons explained above, 21CF believes that there would be a firm basis for the Secretary of State to conclude that her intervention in the Transaction is unnecessary. However, 21CF also recognises that the Secretary of State may wish to obtain Ofcom's advice on these matters.

5.2 21CF would be keen to engage with DCMS and, subject to DCMS' views, Ofcom at the earliest opportunity to discuss what further evidence may be desirable and the timing that is currently envisaged for any decision. 21CF would also like to keep DCMS apprised of the progress towards notification to the European Commission and discuss the impact that this would have on the DCMS decision-making process.

5.3 21CF and its representatives would be pleased to provide further information in relation to any of the points raised above and to meet with staff from DCMS and, if the Secretary of State wishes to involve them at this stage, Ofcom and the CMA.

Allen & Overy LLP
20 December 2016

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43 *@RealDonaldTrump*, 17 October 2012.
44 CNN, *Where Donald Trump got his real power*, 16 November 2016.
45 Ofcom, *News consumption in the UK: research report*.
46 Figure 46 of Ofcom's 2015 *PSB Report*, based on BARB data.
47 Ofcom, *Report on the public interest test in News Corporation/BSkyB*; *News Consumption in the UK 2015*, figure 83.
48 As envisaged in the May 2016 White Paper, *A BBC for the future: a broadcaster of distinction*.