

DEPARTMENT FOR CULTURE, MEDIA AND SPORT
NOTICE OF CONSULTATION ON THE PROPOSED ACQUISITION BY NEWS
CORPORATION OF UP TO 60.9% OF BRITISH SKY BROADCASTING
GROUP PLC
UNDERTAKINGS GIVEN BY NEWS CORPORATION PURSUANT TO
PARAGRAPH 3 OF SCHEDULE 2 OF THE ENTERPRISE ACT 2002
(PROTECTION OF LEGITIMATE INTERESTS) ORDER 2003

Views are sought by midday on Friday 8 July 2011 as to whether the attached undertakings in lieu are sufficient to remedy, mitigate or prevent the public interest concerns in relation to media plurality raised by this merger. For reasons explained below, the Secretary of State is not consulting on any competition aspects of the proposed merger.

Executive Summary

The Secretary of State has considered the points raised during the consultation period and further reports from OFT and Ofcom. These reports make it clear that nothing raised during the consultation process has led the OFT and Ofcom to reconsider their earlier advice to the Secretary of State. A number of constructive changes have been suggested to strengthen the undertakings which the Secretary of State has accepted and he therefore proposes to consult further for a period ending at midday on Friday 8 July 2011.

In particular a number of changes were suggested that would strengthen the arrangements around the editorial independence of Sky News:

- Sky News' Articles of Association set out the definition of independent directors, mirroring the definition in the undertakings.
- Meetings of the board of Sky News about editorial or journalistic matters will only be quorate if an Independent Director with senior editorial and/or

journalistic expertise is present. Similar arrangements apply to the corporate governance and editorial committee. The change will ensure that Sky News organises its business so as to ensure that there is always appropriate senior editorial and/or journalistic expertise at relevant meetings.

Representations were also made about interim protection for Sky News. As a consequence, the undertakings require the appointment of a Monitoring Trustee whose main role is to ensure that News complies with the undertakings in the run up to Sky News being spun off.

There were also suggestions around operational and financial sustainability. As such the Secretary of State has made the following changes:

- The undertakings have been changed to ensure that Sky continues to cross-promote Sky News on its channels. This means Sky News will continue to enjoy the same promotional support as the current business.
- The Monitoring Trustee will advise the Secretary of State in his review of the key operational agreements requiring his approval to ensure that they are fair and reasonable.

As a number of the safeguards are contained in the Articles of Association, including the requirement that Sky News' services will abide by the principle of editorial independence and integrity in news reporting, the undertakings have been amended so that the Articles have to be approved by the Secretary of State. An additional undertaking has been included to ensure that News shall not attempt to cause Sky News to act in breach of its Articles of Association. A copy of the Articles of Association is published along with the consultation document and the revised undertakings.

The Secretary of State considers that the changes made to the undertakings strengthen them in a number of areas highlighted in the consultation responses. As such he proposes to accept these changes and have a further consultation period ending at midday on Friday 8 July 2011. Further more detailed explanation of these and other changes are outlined later in this document.

Background

On 3 November last year, News Corporation (News) indicated that it intended to increase its shareholding in British Sky Broadcasting Group Plc (Sky) from 39.1% to 100%. In light of the turnover of the merging companies and the interaction of United Kingdom and European law, any competition concerns arising in relation to the transaction fell to be considered by the European Commission. On 21 December last year, the European Commission concluded that the increased shareholding would not significantly impede effective competition.

However, under UK law, an issue arose as to whether this transaction gave rise to concerns about plurality of persons controlling media enterprises. The Secretary of State for Business, Innovation and Skills issued a European intervention notice raising this public interest. He asked Ofcom to investigate and report to him by 31 December. That report was produced by Ofcom and provided to the Secretary of State for Culture, Olympics, Media and Sport, Jeremy Hunt (the Secretary of State). In addition, the OFT provided a report on jurisdiction on 30 December [<http://www.culture.gov.uk/publications/7737.aspx>].

On 25 January, the Secretary of State informed Parliament of his initial decision on the proposed News/BSkyB merger. Having considered the Ofcom report and the concerns raised, he concluded that the relevant statutory test was met and intended to refer the merger to the Competition Commission. However, before doing so he also made it clear that he would consider undertakings in lieu of that reference which had been offered by News and which, in his opinion, had the potential to remedy, mitigate or prevent the potential threats to media plurality identified in the Ofcom report.

The Secretary of State asked for further advice from OFT and Ofcom on the extent to which the undertakings in lieu addressed the plurality concerns raised in the Ofcom report, and whether the undertakings were likely to be financially and practically viable. Further reports were received from both organisations on 11 February and 1 March. [<http://www.culture.gov.uk/publications/7880.aspx>]

On 3 March the Secretary of State made a statement to the House explaining that, on the basis of the advice he had received, he believed that the proposed undertakings addressed the plurality concerns that Ofcom had identified in its report of 31 December 2010 and were practically and financially viable for up to 10 years. He therefore announced that he intended to accept undertakings from News on its proposed merger with BSkyB in lieu of a reference to the Competition Commission. However, before he did so he launched a public consultation seeking views on the undertakings. [<http://www.culture.gov.uk/consultations/7887.aspx>]

The undertakings provide that Sky News be spun-off as an independent public limited company. Shares are to be distributed amongst the existing shareholders of Sky in line with their existing shareholdings. The effect of this would be that, after the proposed News/BSkyB merger was completed, the shareholdings in Sky News would remain as if the merger transaction had not happened. The new company would have a majority of independent non-executive directors and have long-term carriage and brand licensing agreements with the newly-merged News/BSkyB company so as to ensure its financial viability. The undertakings specify that News would not be able to increase its shareholding in the new company without the permission of the Secretary of State for a period of 10 years. After that period, any reacquisition would be subject to the general legislative merger control provisions, including a reference to the Competition Commission on plurality grounds depending on circumstances at that time.

Summary of the Undertakings

The undertakings which were consulted upon are as follows:

- The Board of the new company must have a majority of independent directors who have no other News, or News-associated, interest;
- The Board, including the independent non-executive directors, must have the appropriate balance of skills, experience, independence and knowledge, and at least one must have senior editorial and/or journalistic experience;

- The Chairman must be an independent director;
- Sky News' services must abide by the principle of editorial independence and integrity in news reporting;
- The Board must have a Corporate Governance and Editorial Committee to ensure compliance with the principles of editorial independence and integrity in news reporting;
- A 10 year carriage contract which sets out the future financing arrangements;
- A 7 year brand licensing (with potential to extend for a further 7 years).

Changes to the undertakings following consultation

This consultation on the proposed undertakings closed on 21 March. There were over 40,000 responses, including a very large number of near-identical responses as a result of internet campaigns. Summaries of the main responses¹ are today published on the DCMS website. The Secretary of State met representatives from Trinity Mirror, Guardian Media Group, Telegraph Media Group, Associated News and Media, and Slaughter and May on 24 March and met Avaaz on 15 April. Notes of meetings will be published at the end of the process.

These representations have been carefully considered by the Secretary of State and, where appropriate, Ofcom and OFT. The Secretary of State is grateful to Ofcom² and the OFT³ for the written advice they provided him with on 22 June and both these reports are today published on the DCMS website.

Both regulators make it clear that they consider that the points raised in the consultation exercise do not require them to change their previous advice to the Secretary of State. Both they and the Secretary of State do consider, however, that there have been some constructive suggestions for strengthening the undertakings and, as a result, the Secretary of State proposes to consult on amended undertakings. Set out below are the main changes and, where not-self-explanatory, the Secretary of State's reasons for making them. A number of minor drafting

¹ <http://www.culture.gov.uk/consultations/8257.aspx>

² <http://www.culture.gov.uk/publications/7880.aspx#1>

³ <http://www.culture.gov.uk/publications/7880.aspx#1>

changes to the undertakings are not included in this document though they are included in the version of the undertakings published today and a more detailed explanation of the reason for all the changes is included in the OFT's report.

Articles of Association

The Articles of Association of Sky News must be approved by the Secretary of State prior to the undertakings being accepted [3.1]. This reflects the importance of the Articles of Association to Sky News and, in particular, addresses concerns that the Articles might limit Sky News' ability to borrow. The Secretary of State is satisfied that the borrowing arrangements set out in the Articles of Association are reasonable.

The undertakings require that the Articles of Association set out the definition of independent directors [3.1(iv)]. This is consistent with the definition in the undertakings, and is found in Article 1(1).

The original undertakings require News to establish Sky News with Articles of Association which provide that Sky News will abide by the principle of editorial independence and integrity in news reporting. News now offers an additional undertaking not to attempt to cause Sky News to act in breach of its Articles of Association [3.3].

Independent Director with senior editorial and/or journalistic expertise

Article 128 provides that meetings of the board of Sky News about editorial or journalistic matters shall only be quorate if an Independent Director with senior editorial and/or journalistic expertise is present. Similar arrangements apply to the corporate governance and editorial committee (at articles 138 and 139). This is a response to representations that these arrangements could be undermined if this Director was often unavailable for meetings for whatever reason. This will ensure that Sky News organises its business so as to ensure that there is always appropriate senior editorial and/or journalistic expertise at relevant meetings

[3.1(iii)(C); 3.1(ix)(E)].

Solicitation

News shall not solicit staff transferred to Sky News for a period beginning on the Closing Date and ending [words added] 24 months after the date of spin-off. This extends the non-solicitation provision to cover the period between Closing Date and spin-off [4.2].

Carriage and Brand Licensing Agreement

For the avoidance of any confusion, the reference to a 7 year Brand Licensing Agreement which is automatically renewed for a further 7 years has been changed to a reference to a 14 year Brand Licensing Agreement [4.6].

Promotion of Sky News

News shall ensure that Sky continues to cross-promote Sky News on Sky's linear channels to a level and in a manner comparable with such cross-promotion for the period of 12 months prior to the date on which the undertakings are accepted. This is important to ensure that Sky News continues to enjoy the same promotional support as the current business [4.9].

Operational Agreements

News shall ensure that Sky will, prior to or at spin-off, enter into the agreements with Sky News under which Sky will provide facilities and support services to Sky News on arms'-length terms which are fair and reasonable [words added]. This change provides the context for the Monitoring Trustee (see below) to assess News' fulfilment of its obligations in relation to the terms of the operational agreements [5.1].

Charges to Sky News under the main operational agreements are set for the first

year at a fixed price equivalent to the cost of Sky providing the relevant services plus a 5% margin. Thereafter charges will be increased by the Consumer Price Index (CPI). The undertakings have been changed to cap this increase. This caps the CPI-related charges payable by Sky News to News and so provides an enhanced degree of financial security for Sky News [5.3(iii)].

The payments will also be adjusted for actual usage where appropriate and savings or cost increases of services which Sky obtains from a third party. The undertakings have been changed to give Sky News audit rights in relation to these adjustments if Sky fails to provide any relevant information [5.3].

News must ensure that operational agreements will contain a dispute resolution mechanism. The undertakings have been amended to provide that, in the case of the agreements requiring the approval of the Secretary of State, they cannot be terminated until any dispute between Sky News and Sky has gone through the dispute resolution process. News will bear all reasonable costs (including Sky News' reasonable costs) of any dispute resolution process originating from a proposed termination by Sky [5.4].

Appointment of Monitoring Trustee

It was suggested that the undertakings should include the requirement for a Monitoring Trustee to ensure that News complies with the undertakings in the period leading up to the spin-off of Sky News. As a consequence there are now five new sections dealing with the appointment, functions and obligations of a Monitoring Trustee [6-10].

The undertakings have been amended so that, in effecting the spin-off, "News shall not take any action that would prevent the new company being placed in an overall position of editorial, governance, commercial and financial independence in which it will contribute to plurality as Sky News did prior to the Transaction" [2.1]. This provides a context for Monitoring Trustee to assess News' fulfilment of its obligations in respect of the spin-off of Sky News.

In addition to ensuring that News is complying with its obligations under the undertakings, the Monitoring Trustee will provide advice to the Secretary of State in relation to the latter's review of the key operational agreements requiring his prior approval. These include agreements on satellite capacity, playout, and uplink.

Within 20 Working Days of the undertakings being agreed, News has to nominate a Monitoring Trustee to be approved by the Secretary of State. Although News has to pay for the Monitoring Trustee, whoever is selected must be independent and have no material conflict of interest. Paragraph 7.1 of the undertakings expressly provides that the Monitoring Trustee acts on behalf of the Secretary of State. The Monitoring Trustee will remain in place until all of the operational agreements detailed become effective.

Interim Protection

In addition to the provisions for a Monitoring Trustee, there are a number of other changes which are designed to ensure that News cannot undermine Sky News in the run up to spin-off. For example, prior to the spin-off of the Sky News business, News must ensure that the Sky News business (as at the Closing Date) [words added] is maintained as a going concern [13.1(i)] and that the Sky News business, including its facilities and goodwill [words added], is maintained and run normally [13.1(iii)]. Similarly, News must not attempt to influence the editorial decisions of the Sky News business prior to the completion of spin-off [13.1(iv)] and must provide information to the Secretary of State to enable him to monitor News' compliance by with these undertakings [13.2].

Definitions

The definition of "Material Transaction" has been extended to cover the lease agreement and the main operational agreements (that is, those requiring prior approval by the Secretary of State).

As amended, the Secretary of State now considers that the concerns relating to plurality identified by Ofcom are now prevented, remedied or mitigated by the undertakings.

Carriage and Brand Licensing Agreements

The terms of the undertakings also ensure that the detailed provisions of the Carriage and Brand Licensing Agreements have to be approved by the Secretary of State before the merger can go ahead. The Secretary of State has therefore carefully considered the advice of Ofcom and OFT on these key Agreements. They have concluded that the drafts of the Carriage Agreement and the Brand Licence Agreement are consistent with the proposed undertakings. In addition, OFT conclude that the terms of the Carriage Agreement and Brand Licensing Agreement mean that Sky News will be practically and financially viable for the lifetime of the carriage agreement.

In terms of the length of the Carriage Agreement, OFT has reiterated its advice that the undertakings are likely to be practically and financially viable in the short and medium term. Its earlier reports have expressed concern about whether the undertakings would be viable over the long term, but recognised that the appropriate time-frame in this market was for the Secretary of State to decide, with Ofcom's advice.

Ofcom has reiterated its view that it considers a 10 year carriage agreement in the context of industry dynamics in this sector to be a long-term measure. The Secretary of State agrees with this view and therefore considers that the provision of a 10 year carriage agreement and a 14 year brand licensing agreement are of sufficient length to remedy, mitigate or prevent the concerns in relation to media plurality.

The Secretary of State is satisfied, following the advice from Ofcom and OFT, that the Carriage Agreement and Brand Licensing Agreements will ensure the financial and commercial independence of the new Sky News company over what is a very

long period in terms of this sector. He considers the Agreements along with the governance provisions will ensure editorial and operational independence of Sky News.

Other issues raised in the consultation

During the consultation period, a number of other issues were raised that were not material to the issue of media plurality and did not affect the Secretary of State's decision to consult on revised undertakings.

A number of respondents raised competition concerns. In addition to the fact that this could not be considered as part of the media plurality public interest test, these issues have already been fully considered by the European Commission which concluded on 21 December last year that the increased shareholding would not significantly impede effective competition.

Some respondents also argued that News could not be relied upon to abide by the requirements set out in the undertakings, citing previous guarantees and assurances given by News in the past, and the current phone hacking allegations against The News of the World. The Secretary of State takes the view that News have offered serious undertakings and discussed them in good faith. In all the circumstances and given that the implementation of those undertakings will be overseen by the Monitoring Trustee and thereafter monitored and if necessary enforced by the OFT, he takes the view that there are sufficient safeguards to ensure compliance with the undertakings. Furthermore, the various agreements entered into pursuant to the undertakings will each be enforceable contracts. Therefore whilst the phone hacking allegations are very serious they were not material to his consideration.

Conclusion

Having taken into account all relevant considerations, the Secretary of State proposes to accept the amended undertakings in lieu of a reference to the Competition Commission. As required by the Enterprise Act, he will undertake a

further consultation period starting today and ending at midday on Friday 8 July 2011. During this time all interested parties will be able to express their views on the undertakings in lieu. Once he has considered representations, he will reach a decision on whether he still considers that the undertakings (as amended) should still be accepted in lieu of a reference to the Competition Commission. If, after the consultation, he remains of the view that the undertakings address the concerns about media plurality, he will accept them and not refer this merger to the Competition Commission.

Representations should be sent to
bskyb-newscorp.consultation2@culture.gsi.gov.uk by **midday on Friday 8 July 2011**

Postal representations should be sent to:

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