

## INDEPENDENT AUDITOR'S REPORT TO THE MEMBERS OF CHANNEL FOUR TELEVISION CORPORATION (THE 'CORPORATION') ONLY

### Opinions and conclusions arising from our audit

#### 1 Our opinion on the financial statements is unmodified

We have audited the financial statements of the Corporation for the year ended 31 December 2014 set out on pages 130 to 162. In our opinion:

- the financial statements give a true and fair view of the state of the Group's and of the Corporation's affairs as at 31 December 2014 and of the Group's surplus for the year then ended;
- the Group financial statements have been properly prepared in accordance with International Financial Reporting Standards as adopted by the European Union (IFRSs as adopted by the EU);
- the Corporation's individual financial statements have been properly prepared in accordance with UK Accounting Standards, including FRS101 Reduced Disclosure Framework; and
- the financial statements have been prepared in accordance with the requirements of the Companies Act 2006 as if that Act applied to the Corporation.

#### 2 Our assessment of risks of material misstatement

We summarise below the risks of material misstatement that had the greatest effect on our audit, our key audit procedures to address those risks and our findings from those procedures in order that the Corporation's Members as a body may better understand the process by which we arrived at our audit opinion. Our findings are the result of procedures undertaken in the context of and solely for the purpose of our statutory audit opinion on the financial statements as a whole and consequently are incidental to that opinion, and we do not express discrete opinions on separate elements of the financial statements.

#### Programme and film rights (£242 million)

Refer to page 123 (Audit Committee Report), page 137 (accounting policy) and page 149 (financial disclosures).

**The risk** – There is significant judgement involved in estimating the value to the Group of programme and film rights, and there is a risk of a write-down being required when indicators of a reduction in the value of individual assets are identified, for example when:

- The quality of the programme means it may no longer be broadcast in the originally intended transmission slot such that there is a reduction in the related expected future viewing performance; or
- Forecast future theatrical and DVD revenues no longer support the carrying value of developed film rights.

The majority of the costs of programme and film rights are written off on first transmission. There is, however, an increased level of judgement involved in assessing the profile of expected future advertising, sponsorship or other related revenue in relation to certain types of programming including feature films, sports rights and acquired series which may be written off over more than one transmission.

**Our response** – Our audit procedures included:

- We focused on those programme and film rights that are the oldest or have the highest carrying amounts, and those near rights expiry. We evaluated the Group's assessment of the expected future transmissions and forecast revenues through enquiry of the programme scheduling team who operate independently from finance; inspection of the programme schedule for the three month period following the year end date; and compared a sample of programmes scheduled at the year end to third party TV listings for that period:

- With regard to film rights in production, critically assessing forecast film rights income through independent enquiry of the Film 4 commissioning team to understand performance expectations; reference to third party theatrical release data and sales of distribution rights to date; and historical experience of theatrical, distribution and DVD revenues generated from film releases; and
- Challenging the assumptions underlying the calculation of transmission cost write off profiles with reference to historical viewing data, in particular programmes and films that were not fully expensed on first transmission.

**Our findings** – We found:

- the estimates made in relation to expected future scheduling and forecast revenues in assessing the carrying value of programme and film delivery rights to be balanced.
- the estimates in respect of future film rights income on films in production to be mildly optimistic.
- the assumptions regarding the viewing profile used to calculate the transmission cost write off profiles to be mildly cautious.

#### Revenue recognition (£938 million)

Refer to page 123 (Audit Committee Report), page 135 (accounting policy) and page 139 (financial disclosures).

**The risk** – In terms of audit risk, the Group's revenue can be divided into two categories:

- Advertising revenues (£780 million): Whilst the majority of advertising revenue contracts are straightforward, there are a small number of individually significant one-off contracts in respect of barter arrangements, where Channel 4 exchange advertising revenue for programmes, and contracts where Channel 4 acts as a sales agent for other broadcasters' advertising. These contracts can contain unique contract terms including complex commission calculations, and judgement is required to determine the appropriate revenue recognition treatment.
- Sponsorship and other revenues (£158 million): This includes many agreements with differing individual terms in respect of the following revenues: sponsorship, subscription income from other platforms, box office and DVD sales. The volume and variety of different contracts gives rise to a risk of incorrect revenue recognition between accounting periods, in particular in relation to the allocation of revenues where contracts span the year end.

**Our response** – Our audit procedures included:

- Testing the design and implementation of controls operating over the standard advertising revenue arrangements, and testing of the operating effectiveness;
- Agreeing the treatment of barter and sales agent contracts, in terms of
  - i. Applying the relevant accounting standards to the contract terms and comparing with the actual treatment adopted;
  - ii. obtaining evidence of performance of contractual obligations including the delivery of airtime;
  - iii. considering the valuation basis applied for the programmes received in barter deals with reference to production costs which are seen to reflect value;
- Testing the revenue recognition approach on a sample of higher value items of sponsorship and other revenue with reference to our own analysis of the application of relevant accounting standards to non-standard contract terms and transmission schedules in respect of sponsorship campaigns, to assess whether revenue has been recognised in the appropriate accounting period; and
- Considering the adequacy of the Group's accounting policy disclosures in their description of the method applied to recognising revenue for these arrangements.

## INDEPENDENT AUDITOR'S REPORT TO THE MEMBERS OF CHANNEL FOUR TELEVISION CORPORATION (THE 'CORPORATION') ONLY CONTINUED

### Our findings – we found:

- the judgments regarding measurement of airtime delivery to reflect the fulfilment of performance obligations on barter and sales agent contracts to be balanced.
- for barter and sales agency contracts the judgments applied in determining the fair value of goods and services received, used for the recognition of revenue, to be balanced.
- the judgments applied in arriving at the revenue recognition treatments to be balanced.
- the Group's accounting policy disclosures to be proportionate.

### 3 Our application of materiality and an overview of the scope of our audit

The materiality for the Group financial statements as a whole was set at £7.0 million, determined with reference to a benchmark of group revenue of £938 million (of which it represents 0.7%). We consider revenue to be an appropriate benchmark as the Corporation's aim is to achieve a long-term break even position.

We report to the Audit Committee any corrected or uncorrected identified misstatements exceeding of £0.3 million, in addition to other identified misstatements that warranted reporting on qualitative grounds.

The Group's operations are all accounted for at the Group's office in London. The Group audit team performed the audit of the Group as if it was a single aggregated set of financial information. The audit was performed using the materiality level set out above and covered 100% of total Group revenue, Group profit before tax, and total Group assets.

### 4 Our opinion on other matters prescribed under the terms of our engagement is unmodified

In addition to our audit of the financial statements, the Members have engaged us to audit the information in the Members' Remuneration Report that is described as having been audited, which the Members have decided to prepare as if the Corporation were required to comply with the requirements of Schedule 8 to The Large and Medium-sized Companies and Groups (Accounts and Reports) Regulations 2008 (SI 2008 No. 410) made under the Companies Act 2006.

#### In our opinion:

- the part of the Members' Remuneration Report which we were engaged to audit has been properly prepared in accordance with Schedule 8 to The Large and Medium-sized Companies and Groups (Accounts and Reports) Regulations 2008 made under the Companies Act 2006, as if those requirements were to apply to the Corporation; and
- the information given in the Members' Report for the financial year for which the financial statements are prepared is consistent with the financial statements.

### 5 We have nothing to report in respect of the matters on which we are required to report by exception

Under ISAs (UK and Ireland) we are required to report to you if, based on the knowledge we acquired during our audit, we have identified other information in the annual report that contains a material inconsistency with either that knowledge or the financial statements, a material misstatement of fact, or that is otherwise misleading. In particular, we are required to report to you if:

- we have identified material inconsistencies between the knowledge we acquired during our audit and the Members' statement that they consider that the annual report and financial statements taken as a whole is fair, balanced and understandable and provides the information necessary for stakeholders to assess the Group's performance, business model and strategy; or
- the Audit Committee Report does not appropriately address matters communicated by us to the audit committee.

Under the terms of our engagement we are required to report to you if, in our opinion:

- proper accounting records have not been kept by the Corporation, or returns adequate for our audit have not been received from branches not visited by us; or
- the Corporation's individual financial statements and the part of the Members' Remuneration Report which we were engaged to audit are not in agreement with the accounting records and returns; or
- certain disclosures of Members' remuneration are not made; or
- we have not received all the information and explanations we require for our audit.

In addition to our audit of the financial statements, the Members have engaged us to review their Corporate Governance Statement as if the Corporation were required to comply with the Listing Rules and the Disclosure Rules and Transparency Rules of the Financial Conduct Authority in relation to those matters. Under the terms of our engagement we are required to review:

- the Members' statement, set out on page 111, in relation to going concern; and
- the part of the Corporate Governance Statement on pages 115–117 relating to the company's compliance with the ten provisions of the 2012 UK Corporate Governance Code specified for our review.

We have nothing to report in respect of the above responsibilities.

### Respective responsibilities of Members and auditor

As explained more fully in the Members' Responsibilities Statement set out on page 112, the Members are responsible for the preparation of financial statements which are intended by them to give a true and fair view. Our responsibility is to audit, and express an opinion on, the financial statements in accordance with applicable law and International Standards on Auditing (UK and Ireland). Those standards require us to comply with the UK Ethical Standards for Auditors. Scope of an audit of financial statements performed in accordance with ISAs (UK and Ireland)

A description of the scope of an audit of financial statements is provided on our website at [www.kpmg.com/uk/auditscopeother2014](http://www.kpmg.com/uk/auditscopeother2014). This report is made subject to important explanations regarding our responsibilities, as published on that website, which are incorporated into this report as if set out in full and should be read to provide an understanding of the purpose of this report, the work we have undertaken and the basis of our opinions.

### The purpose of our audit work and to whom we owe our responsibilities

This report is made solely to the Corporation's Members, as a body, in accordance with the Broadcasting Act 1990 and the terms of our engagement, and, in respect of the separate opinion in relation to the Members' Remuneration Report, reporting on corporate governance, and, in order that the Corporation's Members as a body may better understand the process by which we arrived at our audit opinion, the inclusion of findings in respect of the identified risks of material misstatement, on terms that have been agreed. Our audit work has been undertaken so that we might state to the Members those matters that we have agreed to state to them in our report, and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Corporation and the Members, as a body, for our audit work, for this report, or for the opinions we have formed.

**Karen Wightman**  
for and on behalf of KPMG LLP, Statutory Auditor  
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25 March 2015