PO-CH/NL/0261
PART I

Chex
Lawson

PART D

CONFIDENTIAL
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PO -CH /NL/0261

PART D

CHANCELLOR'S PAPERS ON COMPETITION POLICY

PO -CH /NL/0261
PART D

DD: 25 years

29/9/95

Begins: 4/7/88
Ends: 27/7/88

CONFIDENTIAL

Reference No E 0585

SECRETARY OF STATE FOR EMPLOYMENT

POTATO SUPPORT IN GREAT BRITAIN
Letter from the Minister for Agriculture,
4 July 1988

DECISION

You will want the Sub-Committee to decide whether it agrees the draft consultative document on potato support circulated by Mr MacGregor with his letter. The main question at issue is whether it refers sufficiently positively to the case for a free market in potatoes.

BACKGROUND

2. At present, the Potato Market Board (PMB) operates a quota system for potato growing and intervenes in the market when there is a surplus. The Government provides a guarantee by sharing the cost of intervention, up to a limit. It also sets an annual target area for planting, to prevent abuse of the power to control planting. These arrangements are to be reviewed by 1990.

3. Mr MacGregor has circulated a draft consultation paper on the future of these arrangements. He would issue it in September and give notice of it in a written answer before the Recess. The draft says that the Government will withdraw from support in 1991. (It cannot be earlier because that would require legislation next Session and there is no place in the programme). The question then becomes what would happen to the PMB. The document discusses three options:

i. Move to a completely free market.

ii. Abolish the PMB's control over planting, but leave their power of intervention.

iii. Give non-producer interests a say in the PMB's exercise of its powers.

ISSUES

4. There will be no disagreement with the proposal to issue a consultation paper, or that it should announce the Government's intention to withdraw its support.

5. The only question at issue will be about how far the Government should state its preference for the option of moving to a completely free market. In an earlier round of correspondence Mr Ridley, Lord Young and Mr Major all said they would like this preference stated. Mr MacGregor's letter of 4 July says that while he too is 'intuitively attracted' to the free market option he does not want to recommend it too openly. This is because farmers are likely to react strongly against withdrawal of Government support, and because announcing a firm preference now would undermine the credibility of the consultation. He says he has however presented the free market option so as to make its attractions clear.

6. If you wished, you could probably get agreement that Mr MacGregor's draft is satisfactory on this point. Mr MacGregor has the support of the other agricultural Ministers, Mr Walker and Mr Rifkind. Mr Major who earlier wanted the Government's preference made clear, also says that he accepts the draft.

7. Lord Young has however written to say (20 July) that he would still prefer the Government to state its preference for the free market option. If you wanted to consider alternatives to Mr MacGregor's formulation, it would be possible to make some changes without altogether departing from general approach. Paragraphs 17-20 of the draft consultative document are the ones to concentrate on. There are many possibilities. One approach might be to make it more explicit that the Government is inclined to the free market

option, but has not made up its mind. Paragraph 19 could for example start with a statement like 'The Government believes, subject to the outcome of this consultation, that there are strong arguments in favour of this approach'.

8. There is another possible question. Paragraph 20 of the draft consultative document says that the R and D work now being done by the PMB could be taken over by a Development Council funded by a levy on the industry. Lord Young has written (20 July) to say that it should be made clear that this was not a decision for the industry alone. And in E(ST) discussions, the Prime Minister has seen strong arguments against levies on producers. The simplest thing might be to delete this paragraph altogether.

HANDLING

9. You might ask the Minister of Agriculture to introduce the subject. The Secretary of State for Wales and the Secretary of State for Scotland (represented by the Minister of State) would be co-authors of the consultative document. The Secretary of State for Trade and Industry and the Secretary of State for the Environment have expressed views on the main point at issue. The Financial Secretary will probably also be interested.

G W MONGER

Cabinet Office
22 July 1988

iae.nj Wyn/104 **CONFIDENTIAL**

FROM: P WYNN OWEN
DATE: 4 July 1988

PS/CHANCELLOR

cc Financial Secretary
Sir P Middleton
Mr Monck
Mr Burgner
Mrs Case
Mr Burr o.r.
Mr Revolta

E(CP)

The Lord Chancellor wrote to the Chancellor of 29 June, suggesting delaying a paper for E(CP) until "the Autumn (presumably October)". Formal advice will be given by the Cabinet Office, but you said you would also welcome Treasury official views.

2. I have consulted Mr Revolta in HE. It is very disappointing that the Lord Chancellor's Department has proved unable to produce a report back to E(CP) by the Summer break on reforming the legal professions. The Marre Committee was set up by the legal profession, in part at least to play for time. So a willingness to await its findings arguably plays into the hands of the lawyers. The request for a postponement also suggests that the Lord Chancellor's Department may not be all that keen on thinking for itself and second-guessing the profession once Marre's findings are available. On the other hand, Lord MacKay seems to be taking a more positive approach to potential reform than his predecessors and the relevant E(CP) remit simply requested a report back by the Summer "if possible", so a legitimate escape clause existed.

3. The Cabinet Office (Mr Neilson), like us, thinks that there is no realistic prospect of obtaining a paper for a July meeting. There are, in any case, several issues currently lined up for the 26 July E(CP) and a second meeting would probably have had to be arranged to accommodate a major paper on the legal professions. The Cabinet Office will sound out Ministers' Diaries on the possibility of the first Autumn meeting being in September rather than October, at which they would aim to take this paper from the Lord Chancellor's Department.

4. I suggested to Mr Neilson that the draft reply should be somewhat disappointed in tone and that, it should definitely secure the paper for the first possible date after the Recess.

Philip Wynn Owen

P WYNN OWEN

Reference No: E 0582

CHANCELLOR OF THE EXCHEQUER

Ch/ Content to write (both to Ld. Mackay + Mr MacGregor) as proposed? See also Mr Wynn Owen's minute, behind.

E(CP)

The Lord Chancellor's letter of 29 June says that the report of the Marre Committee on the legal profession has slipped. Publication is now expected to be on 13 July. He asks that the E(CP) discussion, which you had planned for the July meeting, should be taken at a meeting in the autumn.

2. The slippage is a pity, but it does not seem practical to resist the Lord Chancellor's suggestion. There are however two points to watch:

- The E(CP) discussion should if possible be fitted in before the Party Conference and Star Chamber. We have found a suitable time on 5 October.

- The Lord Chancellor's Department should not reach agreements with the profession before the E(CP) meeting takes place. There may not be much danger of this but the references in the Lord Chancellor's letter to discussion with the professions - for example on item (iii) - raise the question. It might be wise to insert a sentence on the point in your reply.

3. I attach a draft reply to the Lord Chancellor accordingly.

4. The agenda for the meeting now arranged for 25 July looks substantial even without the item on the legal profession. It should consist of:

- Paper by DTI on direct auction of bands of radio frequency spectrum (remit from May meeting).

- Paper by DTI giving more up to date information on EC car price differentials (remit from May meeting).

- Paper by DTI on whether the Government should take further action to terminate VRAs from which its support has been withdrawn (remit from May meeting).

- Agricultural Marketing Boards.

5. The last item is the most important. There are three strands:

a. British Wool Marketing Board. There is a long-standing remit on the Minister of Agriculture to produce a paper on the future of the BWMB before present arrangements end in 1990. At the May meeting you asked for this to be ready in July. MAFF are now saying this might be difficult.

b. Potato support. Mr MacGregor proposes to issue a consultative document on the future of potato support arrangements in the autumn. The question at issue has been whether this should present the options neutrally, or should say that the Government would prefer to move to a free market. Mr MacGregor's latest draft, sent to the Chief Secretary on 4 July, is still mainly neutral. It may not be acceptable to other Ministers and in that case a discussion will be necessary. You said at the last meeting that this could take place at the July meeting.

c. Milk Marketing Board. Mr MacGregor wrote to you about this on 1 July. E(CP) might find it useful to have a look at this at the same time that it discusses the

arrangements for wool and potatoes. It is not clear for example whether Mr MacGregor's letter deals adequately with the underlying question of whether the Board's Dairy Crest subsidiary should continue. The outcome might be that you asked for a paper about this for a later meeting.

6. It may be useful for you to write briefly to Mr MacGregor to prevent any backsliding on the wool paper. You could also suggest a discussion on potatoes and milk, on the basis of the letters already circulated, so that the Committee can look at the support arrangements as a whole. This would short circuit the Ministerial correspondence now in progress. I attach a draft accordingly.

G W MONGER

Cabinet Office
5 July 1988

PSC type final

CONFIDENTIAL

Draft letter for Chancellor of the Exchequer
to send to the Lord Chancellor

E(CP)

Thank you for your letter of 29 June. It is a pity that the publication of the Marre report has slipped but in the circumstances I agree with you that the E(CP) discussion of the legal profession should be postponed until the autumn. ~~We~~ The Cabinet Office have accordingly arranged for a meeting on 5 October. I ~~presume~~ trust that no decisions will be made before then on any of the matters at issue.

It would also be helpful if at the same meeting we could take the paper which Malcolm Rifkind offered on the scope for extending competition in the Scottish legal profession.

I am sending a copy of this letter to the other members of E(CP) and Malcolm Rifkind, and to Sir Robin Butler.

CONFIDENTIAL

CONFIDENTIAL

Rt Hon John Macgregor OBE MP

Draft letter for the Chancellor of the Exchequer to send to the Minister of Agriculture

E(CP)

Thank you for your letter of 1 July about milk marketing arrangements. I have also seen your letter of 4 July to John Major about potato support.

We are of course due to discuss a paper on the future of the British Wool Marketing Board at the E(CP) meeting now arranged for 25 July. I suggest that we might look at the issues on milk and potatoes at the same time, on the basis of the letters you have already circulated. It would help the Committee to consider all the marketing arrangements together.

I am sending copies of this letter to the other members of E(CP), and Peter Walker, Tom King and Malcolm Rifkind, and to Sir Robin Butler.

CONFIDENTIAL

CONFIDENTIAL

Treasury Chambers, Parliament Street, SW1P 3AG
01-270 3000

6 July 1988

The Rt Hon Lord Mackay of Clashfern
House of Lords
London SW1

cc: Financial Secretary
Sir P Middleton
Mr Monck
Mr Burgner
Mr Wynn Owen
Mrs Case
Mr Burr
Mr Revolta

E(CP)

Thank you for your letter of 29 June. It is a pity that the publication of the Marre report has slipped but in the circumstances I agree with you that the E(CP) discussion of the legal profession should be postponed until the autumn. The Cabinet Office have accordingly arranged for a meeting on 5 October. I trust that no decisions will be made before then on any of the matters at issue.

It would also be helpful if at the same meeting we could take the paper which Malcolm Rifkind offered on the scope for extending competition in the Scottish legal profession.

I am sending a copy of this letter to the other members of E(CP) and Malcolm Rifkind, and to Sir Robin Butler.

NIGEL LAWSON

cc thro (+ letter below) to Mr Burgner, Cab. O/ice

Treasury Chambers, Parliament Street, SW1P 3AG
01-270 3000

6 July 1988

The Rt Hon John MacGregor OBE MP
Minister of Agriculture, Fisheries and Food
Ministry of Agriculture, Fisheries and Food
Whitehall Place
London SW1

cc: Financial Secretary
Sir P Middleton
Mr Monck
Mr Burgner
Mr Wynn Owen
Mrs Case
Mr Burr
Mr Revolta

Dear John

E(CP)

Thank you for your letter of 1 July about milk marketing arrangements. I have also seen your letter of 4 July to John Major about potato support.

We are of course due to discuss a paper on the future of the British Wool Marketing Board at the E(CP) meeting now arranged for 25 July. I suggest that we might look at the issues on milk and potatoes at the same time, on the basis of the letters you have already circulated. It would help the Committee to consider all the marketing arrangements together.

I am sending copies of this letter to the other members of E(CP), and Peter Walker, Tom King and Malcolm Rifkind, and to Sir Robin Butler.

Yours
Nigel

NIGEL LAWSON

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IAN GRIST MP

WELSH OFFICE
GWYDYR HOUSE
WHITEHALL LONDON SW1A 2ER
Tel. 01-270 3000 (Switchboard)
01-270 (Direct Line)
From The Parliamentary Under-Secretary

CH/EXCHEQUER
REC. -8 JUL 1988
ACTION FST
COPIES TO

8 July 1988

CT/4414/88

Dear Nigel,

MILK MARKETING ARRANGEMENTS

In Peter Walker's absence from the office I am writing in response to John MacGregor's letter of 1 July to you reporting on the operation of the milk marketing arrangements in the UK in the light of the Touche Ross report on Dairy Crest.

I fully agree with John that the new arrangements are having the desired effect. The recent rationalisation programme has provided firm evidence, particularly in Wales, that Dairy Crest Limited is now operating with clear commercial objectives. The system of regular monitoring of reports on Dairy Crest's financial management and market situation is also well established.

Accordingly, I endorse John's conclusion that the approach which E(CP) approved in 1986 remains valid and that the position should be reviewed again in 1990.

Copies of this letter to other members of E(CP), to Tom King, Malcolm Rifkind and Sir Robin Butler.

Yours ever,

Ian

The Rt Hon Nigel Lawson MP
Chancellor of the Exchequer

dti
the department for Enterprise

The Hon. Francis Maude MP
Parliamentary Under Secretary of State for
Corporate Affairs

Department of
Trade and Industry

1-19 Victoria Street
London SW1H 0ET

Switchboard
01-215 7877

Telex 8811074/5 DTHQ G
Fax 01-222 2629

Jonathan

19/7

13/7

CH/EXCHEQUER
REC. 13 JUL 1988
ACTION MR WYNN OWEN
COPIES TO FST
SIR P. MIDDLETON
MR MONCK
MR BURGNER
MRS CASE
MR BURR
MR REVOLTA

The Lord Chancellor
The Rt Hon The Lord Mackay of
Clashfern
House of Lords
LONDON
SW1A OPW

Direct line 215 4417
Our ref
Your ref
Date 11 July 1988

Dear James,

RECOGNISED INSTITUTION RULES

I have seen your letter of 29 June to Nigel Lawson, copied to members of E(CP).

I do hope that the paper to which you refer in paragraph (v) will be before us as soon as possible. I have received a number of representations about competition in conveyancing and it seems to me that serious distortions exist. Solicitors are allowed to offer estate agency services provided that they do not call themselves estate agents. The result is that solicitors may advertise to sell properties for a fee which is inclusive of all legal work. Other institutions offering estate agency services cannot, as I understand it, offer the same sort of package since arrangements with solicitors to enable this are not permitted under solicitors practice rules. It would help all concerned, except perhaps those solicitors who are benefiting from the current situation, if there could be clarification as soon as possible on the question of the recognition of institutions and practitioners as suitable to provide conveyancing services.

I also note that the June Council of the Law Society went less far than had been expected in the proposed practice rules about introduction arrangements. It is reported that it was argued against the original proposal that it would seriously undermine the Law Society's position in the debate on recognition rules and that the proposal was contrary to the Law Society's strategy that solicitors should move to complete independence in property services by combining property selling and financial services advice with conveyancing. I do think that we need to be quite clear where prudential considerations end

JA2DUL

and self interest starts and to make our views known.

I am copying this letter to other members of E(CP).

Yours ever

Francis.

FRANCIS MAUDE

JA2DUL

From: Mrs V Imber
Date: 14 July, 1988

1 MR BONNEY
2 CHANCELLOR

copies attached for:
Chief Secretary
Financial Secretary

cc: Sir Peter Middleton
Mr Anson
Mr Monck
Mr Burgner
Mr Burr
Mr Tyrie
Mr Call

MILK MARKETING ARRANGEMENTS

On 1 July, the Minister of Agriculture wrote to you in your capacity as Chairman on E(CP) following up a remit from E(CP) in July 1986 for a review of the arrangements then agreed for the Milk Marketing Board. You have replied, in that capacity, suggesting that the next meeting of E(CP) on 25 July look at the issues of competition in the milk sector along with those for wool and potatoes.

2 It is arguable that Mr MacGregor's letter does not provide an adequate basis for a discussion on competition in the milk market. It is confined to the operation of the agreement between the Milk Marketing Board and Dairy Crest, a wholly owned commercial subsidiary, whereas there is a long standing Cabinet remit (dating back to February 1984) for a fundamental review of milk marketing. Attempts to carry out such a review have been thwarted twice in the recent past. In 1984 difficulties with the Commission over our pricing policy resulted in a decision to postpone any fundamental review until after a more restricted consultants' examination of the commercial activities of the Milk Marketing Board. But when this was discussed in E(CP), some two years later, it was again concluded that the time was not ripe for fundamental change (following a letter from No. 10 to that effect). Mr MacGregor's recent letter simply ducks the issue. It is written on the assumption that E(CP) had concluded that, if they worked, the new arrangements with Dairy Crest were all that would be required in the foreseeable future.

3 However, the 1986 decision was one of pragmatism rather than

principle. Any fundamental change in milk marketing would require primary legislation to break the monopoly of the Milk Marketing Board as the initial purchaser of milk. The Agriculture Ministers argued that the industry could not bear major upheaval in its marketing arrangements so soon after the introduction of quotas and the superlevy (a tax on surplus production) in 1984. The Prime Minister agreed that their proposal to turn the MMB's commercial activities into a separate, but wholly owned, plc. was the furthest we could reasonably go at the time.

4 The original paper, E(CP)86(2) canvassed two other options:

(i) ending the MMB's statutory monopoly as a buyer of milk;

X

(ii) hiving off Dairy Crest from MMB ownership, perhaps as a separate producer co-operative.

It would now be open to other ministers to re-open the issue of a fundamental review. There are no direct public expenditure implications and the main Treasury interest lies in ensuring appropriately competitive marketing arrangements.

5 In principle we would recommend that you press for reconsideration of option (i). Ending the monopoly would require primary legislation and is no less likely to prove politically controversial than it was two years ago. However, since July 1986, although milk quotas have been effectively cut by 9.5% and new weaker intervention support arrangements introduced, farmers have adjusted themselves to the newer arrangements. Moreover, the European Court cases on the MMBs pricing policies which were still outstanding in 1986 have now been resolved (in favour of the Commission.)

6 The option of hiving off Dairy Crest could be a more viable option, and has been made easier by the separate creation of the plc. following the 1986 decisions. But unlike then, there is no presure from the Dairy Trade Federation, who are now contemplating admitting the company to one of their constituent bodies, the Creamery Proprietors' Association. Moreover, the Dairy Crest is wholly owned by the MMB who would need to be persuaded that its sale was in the interests of the milk producer, unless primary

legislation were introduced allowing the Government to direct MMB to hive it off.

7 If you were minded to pursue either of these options it would be necessary to commission a more substantive analysis of the issue than the present MAFF paper. You could expect some support from Lord Young on grounds of competition policy principles but other interested Departments would probably favour continuation of the status quo. The Prime Minister's views would of course be critical (and the not so recent debates on the continuation of the doorstep delivery service may still cast their shadow). We are trying to get a steer from the No. 10 policy unit on her current position.

Mr Grist's letter, behind, shows that he favours the status quo.

8 We should be grateful to know whether you would wish to open up the debate on milk marketing policy along the lines discussed above or whether you are content for E(CP) to concentrate on the narrower issues in Mr MacGregor's paper. When we have your reaction to this submission we will brief the Financial Secretary accordingly.

Valerie Imber

VALERIE IMBER

NH8/73Jo

CONFIDENTIAL

FROM: J M G TAYLOR
DATE: 15 July 1988

MRS IMBER

cc PS/Chief Secretary
PS/Financial Secretary
Sir P Middleton
Mr Anson
Mr Monck
Mr Burgner
Mr Bonney
Mr Burr
Mr Tyrie
Mr Call

MILK MARKETING ARRANGEMENTS

The Chancellor has seen your minute of 14 July.

2. He does think the time has come to reconsider ending the MMBs statutory monopoly as a buyer of milk.

J M G TAYLOR

iae.st/Fl/117 **CONFIDENTIAL**

FROM: S J FLANAGAN
DATE: 21 July 1988

1. MR WYNN OWEN
2. FINANCIAL SECRETARY

cc Chancellor
Chief Secretary
Paymaster General
Economic Secretary
Sir P Middleton
Mr Monck
Mr Burgner
Mr Mountfield
Mr Odling Smee
Mr Bonney
Mr Burr
Mr P Davies
Mr Revolta
Mr Waller
Mr de Berker
Mrs Imber
Mr Molan
Mrs Pugh
Ms Roberts
Mr Stevens
Mr Wanless
Mr Call
Mr Tyrie

E(CP): MONDAY 25 JULY

You are attending E(CP) at 3.30pm on Monday 25 July. I understand that the Chancellor will not be present, and **Mr Fowler** will be in the chair.

2. I attach briefing as follows:

(i) **Milk Marketing Arrangements:** brief by IAE1 at **Annex A.**

(ii) **Potato Market Support in Great Britain**: brief by IAE1 at **Annex B.**

(iii) **E(CP)(88)9: Future of the British Wool Marketing Board and the Wool Guarantee**: brief by IAE1 at **Annex C**

(iv) **E(CP)(88)8: Auctions of Radio Spectrum Licences:** brief by IAE2 at **Annex D.**

(v) **E(CP)(88)11: Motor Vehicles - Price Differentials in the EC**: brief by IAE2 at **Annex E**

(vi) **E(CP)(88)12 Voluntary Restraint Arrangements on Imports**: brief by AEF1 to follow tomorrow.

(vii) **E(CP)(88)10: Action Programme and Future Work of the Sub-Committee**: brief by IAE3 at **Annex F.**

3. The Action Programme notes that **Mr Ridley** is due to report to E(CP) this month on local authority national collective agreements. I understand that his officials have provided him with a draft letter, and he may write to the Chancellor in advance of Monday's meeting.* The gist is likely to be that there has been limited progress towards greater local flexibility, but that it is likely to take off after the introduction of the community charge and extended competitive tendering measures; but it looks as if competitive tendering is already exercising on moderating influence on current pay negotiations. Pay agreements have yet to be reached this year. Pay division advise that there is little to discuss, and no need to press for immediate follow-up.

S J FLANAGAN

* I now understand that Mr Ridley has written today, but his letter has yet to arrive.

ANNEX A

Milk Marketing Arrangements

letters from:

Minister for Agriculture, Fisheries and Food (1 July)
Chancellor of the Exchequer (6 July)

Proposals

E(CP) asked to endorse conclusion that approach adopted in 1986 remains valid. (ie turning Dairy Crest into a plc wholly owned by the Milk Marketing Board (MMB)

Line to take

Positive

- review should not be confined to relationship between MMB and Dairy Crest;
- long standing Cabinet remit for **fundamental review** of milk marketing; twice postponed 1984 and again in 1986; time now ripe; should set new deadline of October 1988;
- clearly need to consider **ending the MMB's statutory monopoly** as a buyer of milk; completely out of line with **free market** approach; MMB supports **producer against the consumer;**
- European Court cases on MMB's pricing policies now settled, no risk of further disallowance on that account;
- full review could gain credit with the Commission; need to look to **1992** and **opening up the UK market to competition.**

Defensive

- farmers have now adjusted themselves to the new CAP support arrangements; aware of the wind of change, becoming more adaptable; less likely to resist legislation;
- far from MMB promoting consumption of liquid milk, recent arbitration case shows they are increasing the price to the consumer.

Background

1 The Minister for Agriculture wrote to the Chancellor, as Chairman of E(CP), following a remit to review the arrangements for milk marketing agreed in 1986. His review is confined to the operation of the agreement between the Milk Marketing Board and a wholly owned commercial subsidiary, Dairy Crest. It is arguable that the E(CP) remit requires a more fundamental review of the milk marketing. Lord Young and Mr Ridley will certainly support this interpretation, as will Mr Fowler, who will chair the meeting.

2 Attempts to carry out the a longstanding Cabinet remit (dating back to February 1984) for fundamental review have been thwarted twice in the recent past. In 1984, difficulties with the Commission over pricing policy lead to its postponement until after a more restricted consultants' (Touche Ross) examination of the commercial activities of the MMB. When this was discussed in E(CP) some two years later it was again concluded that the time was not ripe for fundamental change (following a letter from No. 10 to that effect.)

3 Any fundamental change in milk marketing would require primary legislation. The 1986 decision was essentially pragmatic. Agriculture ministers argued that the industry could not bear major upheaval so shortly after the introduction of quotas and the superlevy (tax on surplus production). The Prime Minister agreed that the proposal to turn the MMB's commercial activities into a separate but wholly owned plc. was the furthest we could reasonably go at the time. We understand that she was particularly swayed by the idea that major change could risk the continuation of doorstep deliveries.

4 The original paper (E (CP)86(2)) canvassed the option of ending the MMB's statutory monopoly as a buyer of milk from the farm. This is wholly consistent with competition policy and we recommend that you press for a full reconsideration of this option.

5 Agriculture ministers will argue that although they support the idea in principle, it is impracticable, employing the usual excuses for the retention of monopolies:

- economies of scale, eg the value of a network in minimising the costs of collection from many small scattered producers;

- efficient management of peaks and troughs in production;

To these they add:

- maintaining incomes of small farmers in remote areas particularly the hills (a similar argument is used for the preservation of the British Wool Marketing Board),

- maintaining a supply for "doorstep" deliveries, which not only slows down falling consumption of liquid milk but gives a "social service" through the milkman's regular visits

They attempt to clinch the argument by saying that legislation would be contentious in view of the popularity of the MMB with the dairy farmer, and the rural community in general.

7 These arguments can be challenged:

- the existing mass of regulation and price control may benefit the farmer but it works to the detriment of the consumer. (Following an arbitration in favour of the MMB's right to fix the price of liquid milk, the dairy companies will have to increase the price to the consumer).

- blanket subsidies for "social" reasons distort the balance of supply and demand, engendering economic inefficiency;

- It is entirely in keeping with the Government's objectives for agriculture that farmers should become increasingly subject to commercial risk. They have now adjusted themselves to milk quotas and the tighter intervention arrangements introduced by the December 1986 Agriculture Council.

8 You are unlikely to secure agreement to the abolition of the MMB and its statutory monopoly at the meeting, but it should be possible to get a commitment from Mr MacGregor to produce a thorough review by the end of October in time for the November meeting of E(CP).

ANNEX B

E(CP)(88)

POTATO MARKET SUPPORT IN GREAT BRITAIN AFTER 30 JUNE 1990
A CONSULTATION PAPER

Letter from Minister of Agriculture, Fisheries and Food (4 July 1988)

Proposals

- Abolish guarantee arrangements for potatoes.

- Issue consultation document on future of potato market support in Great Britain.

Line to take

- Support abolition of potato guarantee.

- Government should not fix target planting area. **Needs of the market** should dictate level of production.

- No longer a need for financial intervention from Government. PMB has its **own reserves** and Government money **reduces** Board's **incentive** to solve problems of over supply.

- Strongly favour **abolition** of PMB but accept that consultative document should offer choices. Abolition would

  - bring producers **into line** with main competitors;

  - allow them to **exploit market opportunities** without quota restriction;

  - compete on **equal terms** with cheap imports.

- Do not reject out of hand possible creation of Development Council if majority of producers are prepared to finance it.

Background

This paper proposes to end the present guarantee arrangements for potatoes which are due to be reviewed before 30 June 1990. Such a decision would clearly have implications for the Potato Marketing Board (PMB) so it also discusses various options for its future. Mr MacGregor suggests that the paper is circulated for comment to the potato industry and other interested parties.

2. Potatoes are not covered by the Common Agricultural Policy but national support arrangements exist in Great Britain and are administered by the PMB under the Potato Marketing Scheme 1955 (as amended). The scheme was last revised on 1 July 1985 following a review which expressed concern about the Government's contingent liability for potato support but concluded that the market was not yet ready to switch into being completely free and open. Since these changes which placed more responsibility on producers to meet the cost of removing surpluses from the market, there has been no call on public funds for market support purposes. The Board's reserves currently stand at £6 million and MAFF expect them to be about [£14 million] by 1990. Where we were previously hesitant, there now seems to be no reason why the Government should not end its contingent liability and encourage the industry to accept financial responsibility for its own affairs.

3. Mr MacGregor's consultation paper recognises that once the present guarantee arrangements cease, the PMB should not be left in a position in which it could control potato prices and distort the market to favour producers. In the absence of the constraints imposed by the present Financial Agreement, conditions would exist whereby the Board could restrict production to increase growers returns. Such exercise of monopoly powers would penalise processors and consumers through higher prices as well as taxpayers (because the price of potatoes has a significant bearing on the Retail Price Index).

4. The paper proposes three options for the future:

(a) Abolishing the PMB.

(b) Retaining the PMB but restricting its freedom to manage the market.

(c) Replacing the PMB with some other statutory organisation.

Of these three we strongly favour abolishing the Board. This is consistent with advocating maximum freedom for market forces and the Chancellor's objectives for agricultural reform set out in his minute to the Prime Minister of 30 November 1987. The Secretary of State for Trade and Industry is extremely enthusiastic about this option and has suggested that any paper should openly support it. Whilst Mr MacGregor has admitted that he is "intuitively attracted" to the free market solution he is not persuaded that it is correct to present only one option in a consultative document. The Chief Secretary agreed in his letter of 15 July, indicating that he was happy that the balance of the argument is quite clear. It seems sensible to acknowledge that other options are also possible if a majority of producers are prepared to take full financial responsibility for the PMB's continued activities.

5. Removing the Board would bring British potato producers into line with their main competitors and would allow them to concentrate on exploiting market opportunities without the constraints of quota control. The domestic industry is increasingly in competition with cheap imported potatoes and abolishing the Scheme will allow our farmers to compete on equal terms.

6. A free market has always been strongly supported by the potato processors. Furthermore, a vocal lobby group has consistently expressed dissatisfaction with present arrangements and claim that, though they could sell many more potatoes, they are reluctant to do so for fear of incurring excess quota levy (£534.50 per hectare).

7. Lord Young has expressed doubts about the suggestion that the PMB might be replaced by a Development Council (paragraph 20) because it would impose a statutory levy on the industry. We would prefer any future arrangements to be wholly outside Government but the agricultural industry tends to have a

preference for Development Councils. These can only be established with the support of a majority of the industry and such support must be tested every five years. Given such constraints we need not automatically oppose the formulation of such a Council. It would certainly be preferable for any future R and D expenditure to be financed by levies on producers who have voluntarily set up a Development Council than for continued public expenditure for this area, though we recognise that a statutory levy might be perceived as "anti-competitive".

8. Primary legislation is required to end the potato guarantee and abolish the PMB.

IAE1

ANNEX C

E(CP)(88)9

FUTURE OF THE BRITISH WOOL MARKETING BOARD AND THE WOOL GUARANTEE

Memorandum by the Minister of Agriculture, Fisheries and Food

Proposals

i Abolition of the wool guarantee
ii Writing off existing deficit (around £17 million) in guarantee stabilisation account
iii Retention of the Wood Board in its current form
iv Review position of the Board's subsidiaries.

Line to take

- support abolition of guarantee. Will remove **anachronistic** and **unnecessary** government intervention in market. Accept that this implies writing off any remaining deficit.

- Oppose any compromise. Would leave Exchequer involvement in area where producers can, if they wish, operate their own stabilisation system.

- Oppose retention of Wool Board's statutory monopoly. Producers should operate **freely** and in **competition.**

- Not in the business of subsidising inefficiently produced UK wool when imports of at least equivalent quality are readily available.

iael.mg.docs.3.20.7

Defensive

- large producers are as likely to object to a Wool Board without the Guarantee as they are to opt out of a voluntary co-operative. In each case they would, in effect, be subsidising smaller producers.

- accept success of Wool Board's marketing and promotion campaigns. But if they are popular with producers they will choose to retain a voluntary co-operative.

- wool is a by-product for livestock farmers. Do not accept there will be extreme levels of hardship encountered if a few inefficient producers cease production. Wool accounts generally for only 5 to 10 per cent of their total income.

Background

In July 1987, E(CP) concluded that there should be a full review of the British Wool Marketing Board (BWMB) and its activities in 1988, before the existing financial agreement with the Government came up for renewal in 1990. Mr MacGregor's paper meets this objective.

2. Wool is one of only two major agricultural products not covered by the Common Agricultural Policy (the other being potatoes). The BWMB was established in 1950 to operate the price support arrangements under the 1947 Agriculture Act. Its principle objective has been to maximise returns to farmers from the sale of British wool by minimising administration and marketing costs and maximising the market price.

3. Under present arrangements the BWMB has a statutory monopoly on purchases of UK produced wool and operates a price stabilisation scheme with Government support. The Board pays producers a price (currently 129p per kilo) guaranteed by the Government and then sells the wool at international auction in the UK. If the sale price is lower than the guaranteed price deficit is met from previously accumulated surpluses or, failing that, by advances from the Exchequer in the form of an interest-free loan. If the sale price is above the guaranteed price any surplus is used first to pay off any outstanding Exchequer advances and then to build up a stabilisation fund which is available to meet future deficits. In practice the Board has maintained a substantial debt to the Exchequer, though this has fallen in recent months to around £17 million.

4. You can support abolition of the wool guarantee. As Mr MacGregor notes, once the potato guarantee is removed in June 1990, wool would remain curiously as the only guarantee commodity.

5. In the past we have argued that a proportion of the deficit should be carried forward by the Board but given the proposed abolition of the Guarantee this seems unreasonable on this occasion. The question as to whether the writing off any deficit would count as a state aid is one which lawyers will need to address but this should not prevent us in principle from agreeing to abolition of the guarantee.

6. The Government's competition policy requires that we should also press for abolition of the BWMB. Mr MacGregor will argue that:

(i) the Board is popular with producers and that it provides valuable buying, marketing, promotional and sales services in which some individual producers at the margin would otherwise be unable to indulge;

(ii) it acts on behalf of the 100,000 sheep farmers for whom wool is a by-product generally worth only 5 to 10 per cent of their total income benefit from economies of scale;

(iii) many small producers are likely to be forced out of wool production if larger ones refuse to establish a cooperative.

Against this you can argue;

(i) the market should be allowed to sort itself out;

(ii) individual producers should be given the freedom to choose how and at what price they sell their wool.

(iii) there is no reason why the Government should continue to subsidise the production of inefficiently produced UK wool (even in the Less Favoured Areas) when imports of equivalent or better quality are readily available.

7. There is little evidence that large producers would object to the establishment of a voluntary cooperative to succeed the BWMB. And any potential objections might equally be raised about existing arrangements where they effectively subsidise smaller producers through paying average collection costs for their wool.

8. The Board's subsidiaries were considered in detail by E(CP) last July [paper E(CP)(87)4]. There seems little need to enter into detailed discussions on the inter-relationships between these bodies when we favour abolition. But it is useful to address these issues in any consultative document which does not firmly recommend a single solution.

9. Primary legislation is required if the Wool Guarantee is to be ended or the BWMB abolished.

IAE(1)

ANNEX D

CP(88)8: AUCTION OF RADIO SPECTRUM LICENCES

Memorandum by the Secretary of State for Trade and Industry

Proposals

This paper sets out proposals for the framework for the auction of radio spectrum in certain frequency bands which was agreed at the last meeting of E(CP). The Committee is asked to endorse the framework set out in the paper and agree that officials should work out detailed proposals to be included in a consultation document to be issued in the Autumn.

Line To Take

- agree that auctions should be based on transferrable licences and that a consultation document should be prepared, but suggest:-

  i. that Ministerial discretion in accepting auction bids should be specifically limited to issues of competition and possibly security and interference and not open-ended as the paper proposes;

  ii. any new licences issued under the present arrangements for the auctionable bands should be limited to the period up until the date of the auction rather than unlimited as the paper proposes;

  iii. auctioned licences should be for a limited period rather than indefinite as the paper proposes;

  iv. restrictions on transferability of licences should be limited to issues of competition, security and interference as for auctions.

Background

2. E(CP) decided at their last meeting that auctions should be introduced for certain radio frequencies in order to introduce market forces into the allocation of radio spectrum, which is currently managed through an administrative licence system. A note explaining the present arrangements and outlining the work leading up to the E(CP) decision is annexed. In addition to the introduction of auctions, E(CP) decided that trial Frequency

Planning Organisations should also be set up. Proposals on this will be discussed at E(CP) at a later stage.

3. The paper focuses on the auctioning of licences to use equipment within a spectrum band, and disregards the idea of simply auctioning the right to use without reference to particular equipment. Auctions of licences for equipment, achieve less deregulation than auctions of right to use spectrum, because licences are linked to specific types of equipment and after the auction there is potentially less scope for changing the use of spectrum and thus for competition. But legislation for auctions of licences, and enforcement are simpler and such auctions are a welcome first step in deregulation of the selected mobile radio bands.

4. The paper proposes that Ministers should have discretion to accept bids other than the highest for reasons such as international obligations, security, competition policy and technical efficiency. This is so wide that there is a danger of the new arrangements resembling an administrative rather than an market system and you should therefore press for discretion to be limited and clearly specified. Restrictions on the transferability of licenses should also be limited.

5. There is a conflict between keeping frequencies clear in the run-up to auctions (end-1990 at the earliest) and postponing profitable interim use by refusing licences or granting them for short periods only. The paper proposes that ordinary licences should be continued to be issued which would be for an unlimited period, until auction legislation is before Parliament (possibly in early 1990). However, if such licences are indefinite, prospective bidders will when the consultation document is published simply apply for the vacant spectrum under the current procedures, thus defeating the purpose of the auction. There is no guarantee that other channels within the spectrum will become available in the intervening period. It would, therefore, be more sensible to offer short term licences for the period up until the auctions can be held.

6. The paper does not propose a maximum period for the auctioned licences, although the Government would retain the power to terminate licences. If there was an unrestricted secondary market in licences which enabled the use of spectrum to change, the only disadvantage of unlimited licence periods would be the potential revenue loss from creaming off monopoly profits (because bidders would be unlikely to allow much in their bids for uncertain profits

beyond 10 years or so). However, if, as seems likely, transfers of licences are restricted, then an unlimited licence period could have the serious disadvantage of restricting the scope for new users of radio spectrum.

IAE2
21 July 1988

35/G/3505/008/SR

ANNEX D
APPENDIX 1

BACKGROUND NOTE

At present responsibility for radio regulation is spread across a number of Government Departments. The civil use of radio spectrum requires a licence under the Wireless and Telegraphy Acts. With the exception of broadcasting authorities, which are licensed by the Home Office, licences are isssued by the Radio Regulatory Division of the Department of Trade and Industry. RD is the main source of professional expertise in radio frequency planning and has wide responsibilities for spectrum planning and international aspects of radio regulation; in addition it is also responsible for policing licensing and investigating complaints about interference. Crown use of radio spectrum is exempt from licensing and the MOD has a major involvement in spectrum management for the Armed Forces. The present basis of charging for the assignment of radio frequencies is through licence fees which are designed to fully recover RD's administrative costs of some £13m a year.

2. Spectrum management was reviewed by Dr J H H Merriman in 1983. His "Report of the Independent Review of the Radio Spectrum" did not reach any firm conclusion on the case for spectrum pricing, but recommended commissioning a feasibility study. In 1985 DTI commissioned CSP International to review the case for introducing market forces into spectrum management, to develop a proposal which market forces a greater role and to examine the economic impact of market orientated allocation.

3. CSPI concluded that the present administrative system of spectrum management had considerable weakness. Allocation (designation of a frequency band to one or more classes of user) had not responded to changes in users' demand, and assignment (designation of specific frequencies for use by specified persons, for specified types of use) has been inefficient.

4. CSPI's main recommendation was that competing Frequency Planning Organisations (FPOs) should be created to sell the right to use spectrum. Major users (eg would also be allowed to sell the use of their allotment of frequencies). Annex B of CP(88)7 describes the CSPI proposals in more detail.

5. An interdepartmental Working Group of proposals, chaired by the DTI and with Treasury representatives, was set up in September 1987 to look at ways of introducing market forces in the light of the CSPI report. The Working Group discussed various options, including FPOs, direct auctions and an "evolutionary approach" whereby Radio Communications Division contracted out frequency planning. It was a discussion group only and produced no final report.

6. Proposals for introducing market forces into spectrum management were set out in E(CP)(88)7. The main issues decided by the Committee were:

i. that Lord Young should prepare proposals for auctions in selected mobile radio bands (and he should put proposals to the Committee in July);

ii. that Frequency Planning Organisations (FPOs) should be set up in certain parts of the spectrum (a further report on this will be made to E(CP) in due course);

iii. that steps should be taken to open up the database of spectrum users held by Radio Communications Division to encourage greater private sector involvement in frequency planning.

ANNEX E

E (CP) (88) 11 MOTOR VEHICLES: PRICE DIFFERENTIALS IN THE EUROPEAN COMMUNITY

The paper is by the Secretary of State for Trade and Industry

Proposals

The paper summarises the latest information on car price differentials between the UK and our EC partners and invites the Committee to note : that the weighted average of discounted pre-tax prices of 9 EC countries is 6% below the average UK price; that there is no reason why substantial price differentials should persist in the longer term and that there is a trend towards narrower differentials suggesting that the EC Block Exemption regulation is not a material factor in the persistance of price differentials. The paper proposes a further report at the end of 1989.

Comment : the paper seems complacent and insubstantial. It assumes that there is no underlying competitive problem when it is clearly in the interests of producers to perpetuate differentials. The 6% differential identified is by no means insubstantial and in any case assumes that the UK consumer consistently achieves most of the maximum discount available. The paper ignores the opinion of consumer groups. The conclusion from the present paper is that the case is not clear and that more and detailed evidence needs to be presented by DTI if their arguments are to be substantiated : any further paper needs to present more detailed assessments of the market and to explore specific anti competitive practices.

Line to take

Welcome the paper and its conclusion that price differentials are moving in the right direction;

Express some **reservation** about whether uncompetitive practices will wither with the coming of 1992;

Agree to DTI's suggestion that a **further paper** be presented and **stress** that this should cover pricing differences in more detail, include consumer views and look specifically at anti competitive practices.

Background

At the E(CP) meeting on 3 May a paper on this subject was presented by the Secretary of State for Trade and Industry. This summarised the situation on price differentials between the UK and other Member States of the EC and concluded that price differentials were continuing to narrow amd that there had been a further reduction in the level of complaint from UK consumers about obstacles to the purchase of vehicles in other member states ("personal imports").

At that E(CP) meeting the Secretary of State for Trade and Industry was invited to submit a further report this month containing the most up to date price comparisons available, a description of the price differentials faced by individual buyers in the UK who were unable to benefit from the discounts available to fleet purchasers, an explanation of the extent to which price differentials could be justified by the genuinely higher cost of supplying the UK market, and advice on whether the EC Block Exemption regulation for motor vehicle distribution systems was a material factor in the persistance of price differentials.

The present paper suggests that there was little shift in overall price differentials between July 1987 (the basis of the last paper to E(CP)) and March 1988 and that these were now about 6% on discounted prices.
On the question whether price differentials can be justified by underlying cost differences the paper concludes that neither the claims of manufacturers nor the uniqueness of the demand for right hand drive suggest price differences can be justified.
On the EC Block Exemption regulation the paper concludes that the differentials taking into account consumer discounts have narrowed following the introduction of the regulation but reaches no clear conclusion on whether the regulation is responible for the continuation of price differentials.

The present paper takes matters forward only marginally. In order to conduct a full survey of price differentials DTI would have needed to have commissioned special research. However DTI should report back when further survey information on Community-wide price differntials is available in 1989.

E(CP)(88)10: ACTION PROGRAMME AND FUTURE WORK OF THE SUB-COMMITTEE
Note by the Parliamentary Under Secretary of State for Corporate Affairs, DTI (Mr Maude)

Proposals

1. The bulk of the paper is an updated version of the **Action Programme,** which lists work currently in progress on competition. A previous version was discussed at the E(CP) meeting on 28 January.

2. Mr Maude also proposes the following **agenda for the 5 October meeting** of the sub-committee:

- Restrictive practices in the legal profession (LCD)
- Solicitors in Scotland: fee sharing multi-disciplinary practices (Scottish Office)
- VRAs and Quantitative Restrictions on imports (DTI)
- Barriers to multi-disciplinary practices in the professions (DTI)

3. Finally, Mr Maude also suggests a tightening of the sub-committees procedure by calling for **interim reports** on items with long time-scales, to avoid losing momentum.

Line to take

- **endorse** Action Programme and broad lines of proposed agenda for 5 October
- suggest **Scottish Solicitors** paper should be broader in scope, covering parallel range of issue to LCD paper on English legal profession
- support proposal for **interim reports** on long-term items: Specific dates should be agreed at official level to ensure they are relevant to each item.

Background

4. E(CP) last saw the Competition Initiative Action Programme at its 28 January meeting. In the intervening 6 months, Mr Maude has held bilateral meetings with departmental Ministers, producing the revised version attached to this paper. Deadlines for reporting back to E(CP) have been tightened and made more specific. Mr Maude also proposes that where items have long time-scales, interim reports should be made to the sub-committee. These are welcome developments, as they should help to pick up the momentum of the Competition Initiative, and counter the tendency for E(CP) papers (and meetings) to slip.

5. Unfortunately, the specific dates suggested by Mr Maude for interim reports have not been agreed with the relevant departments. Certainly, we were not consulted on the October date given for reporting on EFT/POS (Electronic Funds Transfer at Point of Sale). There appears to be little rationale to the October date. The DTI originally added EFT/POS to the list and we had no objection to its inclusion providing joint DTI/TSY status was given, but EFT/POS is, of necessity, a rather unspecific item with no obvious timetable. DTI officials apparently envisaged that any difficulties with particular dates could be raised at this meeting. But with so many items on the list, this could become needlessly messy. We recommend that you suggest that Mr Maude should ask his officials to check the appropriateness of dates with officials in relevant departments. He might then report back to the next meeting with a revised timetable.

6. The agenda proposed for the next meeting looks broadly satisfactory. The item on restrictive practices in the legal profession has been held over to October to allow the recommendations of the Marre Committee to be taken into account. The paper on Quantitative Restrictions on imports was requested by the Chancellor in his letter of 1 July to Lord Young.

7. You might, however, like to suggest that the paper on "Solicitors in Scotland" should be expanded to cover the anti-competitive practice in the Scottish legal profession more generally. The English legal profession is to be scrutinised this

way in the LCD paper, and it would be a missed opportunity for the Scottish Office paper to concentrate only on limited aspects of the Scottish profession. Mr Fowler (in the chair) is likely to support suggestions to expand the Scottish Office paper in this way.

the department for Enterprise

The Rt. Hon. Lord Young of Graffham
Secretary of State for Trade and Industry

The Rt Hon Norman Lamont MP
Financial Secretary to the Treasury
HM Treasury
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Date 21 July 1988

Dear Norman

NEWSPAPER DISTRIBUTION

Thank you for your letter of 5 July asking me to consider whether my Department should prepare a paper on newspaper distribution for E(CP).

As you say, the MMC and OFT have both examined this subject and you may be aware that the OFT are continuing to keep under scrutiny recent developments in newspaper distribution. This work is undertaken by virtue of the statutory framework in which the OFT exists and which gives perspective to its functions. The legislative frame-work is concerned with questions of competition, monopoly and restrictive trade practices and requires the Director General of Fair Trading to consider whether any particular practices adversely affect the interests of consumers in the UK.

I am not persuaded that it would be an effective allocation. of resources for my Department to examine this issue. The OFT has the expertise and the remit and any examination would necessarily duplicate much of their work. If the OFT and MMC are unable to find that consumers are adversely affected,to launch a further Departmental enquiry may be seen to be interfering unnecessarily in commercial arrangements.

the department for Enterprise

I think that we can rely upon the Director General of Fair Trading to keep this matter under review (and recommend whether further action under the competition legislation is appropriate) and therefore I suggest that you make your concerns known to him directly. My Department routinely passes on complaints to the OFT and advises complainants to approach the OFT directly with evidence of alleged malpractice.

I am copying this letter to members of E(CP).

Yours
David

CONFIDENTIAL

Reference No E0586

SECRETARY OF STATE FOR EMPLOYMENT

FUTURE OF THE BRITISH WOOL MARKETING BOARD AND THE WOOL GUARANTEE

Paper by the Minister of Agriculture, E(CP)(88)9

DECISION

Mr MacGregor recommends the end of the wool guarantee. This will be readily accepted. But he also recommends leaving the operation of the Wool Marketing Board unchanged. This will be controversial. Possible ways forward would be to ask Mr MacGregor to put in further reports on turning the Board into a voluntary cooperative, or requiring it to dispose of its subsidiaries.

BACKGROUND

2. At present, the Government operates a wool guarantee. It provides a national guaranteed price for wool each year. It operates through a stabilisation fund which is supposed to be self-financing but has built up a deficit of £17m.

3. The British Wool Marketing Board (BWMB) is the statutory monopoly buyer of all wool produced in the UK. It sells the wool through auctions. The guarantee is operated by means of the price paid by the Board, but the Board could continue as a monopoly buyer even if the Government withdrew the guarantee. It also has subsidiary companies 'upstream' (collecting and handling the wool before the auctions) and 'downstream' (buying some of the wool at the auctions, and processing and marketing it).

4. These arrangements are to be reviewed by 1990. Last year E(CP) asked Mr MacGregor to 'consider whether the BMWB was necessary at all and the case for privatising it and its subsidiaries as a whole or in part'. This paper is the result.

CONFIDENTIAL

ISSUES

The wool guarantee

5. Mr MacGregor proposes to abolish the wool guarantee, as soon as the necessary primary legislation can be passed. Nobody will object to this, and the meeting will probably not need to spend much time on it. A number of detailed questions will arise, for example on the writing-off of the accumulated deficit. There seems no need to decide these now, and if they are raised you might simply ask the agricultural Ministers to discuss them with the Chief Secretary.

Future of the BMWB

6. Mr MacGregor also recommends leaving the operation of the BWMB unchanged. This may be much more controversial. It may be useful to divide the question into two:

- Should the BWMB continue at all?

- If it does continue, should it have to give up its subsidiaries?

Should the BMWB continue at all?

7. Mr MacGregor argues that the BMWB should continue as the monopoly purchaser of British wool because:

a. The producers want it. Abolition would 'almost certainly' need primary legislation and would be very controversial.

b. It does no harm to consumers. BMWB wool is sold at auctions, in competition with imported wool, at the world price.

c. Its size enables it to get full advantage of economies of scale in collecting wool from producers and preparing it for scale.

d. It charges the average collection costs for all producers. This favours those who offer small amounts or are in remote locations. The Government would not want to see such producers disadvantaged. The regional Ministers are likely to make this point strongly.

8. It seems undeniable however that retaining a statutory buying monopoly in this industry would be inconsistent with the Government's general policy, and other members of the Sub-Committee are likely to be sceptical about the case. The Financial Secretary will press for its abolition. Mr MacGregor's argument here also does not obviously fit well with his acceptance of the strong case for a free market on potatoes (item 4).

9. A possible compromise might be to turn the Board into a voluntary co-operative, so that producers also had the option of selling on the open market. Mr MacGregor does not like this because some producers might choose to break away, and it would not give the same help to the smaller, more remote producers. But it could be argued that on both these points what he sees as disadvantages are really the market at work.It could also be said that in practice the result would be a gradual transition from the buying monopoly to a free market, which could be positively advantageous as a way of managing the change without upheavalThe Financial Secretary might accept this proposal. One way forward at this meeting might be to ask Mr MacGregor to submit a further report to E(CP) by the end of October on ways of turning the Board into a voluntary cooperative.

10. A further compromise would be to accept Mr MacGregor's view on the BMWB's monopoly of purchase and in return press for more action on the divestment of their subsidiaries.

The Board's subsidiaries

11. The Board's subsidiaries handle about half the total national production before it is delivered to the Board and buy about a third of the wool at the Board's auctions. The Board has actually extended the range of its subsidiaries in the last few years. Even if the

Board's buying monopoly continued, these interests could be privatised.

12. Mr MacGregor opposes this because:

i. The Board would not agree voluntarily and primary legislation would be needed.

ii. The industry would strongly oppose the legislation.

iii. The work of the subsidiaries has been valuable, especially in promoting British wool as a distinctive product.

13. Nevertheless, privatisation would so obviously be consistent with the Government's general policy that you might want to press Mr MacGregor on the case for it, covering such questions as:

- Has he discussed the possibility of divestment with the Board? If not, can he do so? (In 1985 E(CP) asked his predecessor to press the Board, but it is not clear that this ever happened).

- Do the objections seen by the Board and the industry apply to all subsidiaries? Surely privatisation would be more acceptable for some than others?

- Would it be possible to introduce a partial private sector shareholding, at least to start with? This could conveniently be in Wool Growers Limited, the subsidiary through which all other interests are held.

If the course of discussion justified it, you could ask Mr MacGregor to return to the Committee later in the year with specific proposals on divestment of the Board's subsidiaries.

CONFIDENTIAL

HANDLING

14. You will want to ask the Minister of Agriculture to introduce his paper. The Secretary of State for Wales, the Minister of State, Scottish Office and (since the wool arrangements apply to the UK) the Parliamentary Under-Secretary, Northern Ireland Office all have a direct Departmental interest. The Secretary of State for Trade and Industry and the Financial Secretary, Treasury will be interested in the competitive aspects.

G W MONGER

Cabinet Office
22 July 1988

Molan/minute/13

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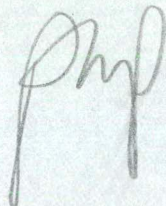


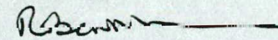
FROM: R MOLAN
DATE: 22 July 1988

FINANCIAL SECRETARY

cc Chancellor
Chief Secretary
Paymaster General
Economic Secretary
Sir G Littler
Mr Mountfield
Mr Burr
Mr Davis
Ms Symes
Mr Flanagan
Miss Preston
Mr Tyrie

E(CP)(88)(12): VOLUNTARY RESTRAINT ARRANGEMENTS ON IMPORTS

I attach a brief on the above paper which is due to be discussed at E(CP) on Monday 25 July.



R. MOLAN

E(CP)(88)(12): VOLUNTARY RESTRAINT ARRANGEMENTS ON IMPORTS - MEMORANDUM BY THE SECRETARY OF STATE FOR TRADE AND INDUSTRY

PROPOSALS

Lord Young's paper fulfils a remit to consider whether further action is needed to terminate VRAs for which government support has been withdrawn in the past. It reviews the action which was taken in each relevant sector following the termination of Government support and, by implication, concludes that no further Government action is called for.

LINE TO TAKE

2. i. Is there independent evidence that arrangements covering music centres and mono TV sets are not continuing?

   ii. If pottery VRA not terminated within reasonable time, what steps will DTI be taking to press for it to be ended?

   iii. Intention of British Cutlery and Silverware Association to maintain their VRAs in the face of Government disapproval highlights the limitations of Government powers in this area.

iv. Is it not the case that some VRAs may be in contravention of the Restrictive Trade Practices Act? Should this possibility not be looked at in cases where arrangements persist despite disapproval and the Office of Fair Trading be asked to investigate if appropriate?

v. There is clearly case for considering inclusion of VRAs in illustrative list of agreements which proposed new RTP legislation will outlaw.

vi. Accept one cannot prevent exporting countries imposing restraints where they consider this to be in their interest. But is there not more we can do to impress our views upon those countries. For instance, might not a DTI Minister write to his opposite number?

BACKGROUND

3. The review of VRAs initiated by E(CP) in 1985 has led to the withdrawal of Government support for the majority of such arrangements. In answering a written PQ last March, DTI for the first time publicly acknowledged that the Government asks the industries concerned to eliminate arrangements which have no justification. The reply listed those arrangements which the Government had taken such a view on. However, we had obtained information that a number of these arrangements remained in existence following the withdrawal of government support and an article in "The Economist" in April also suggested that this was the case. At the last meeting of E(CP) in May Lord Young confirmed that

there had been evidence that some UK manufacturers had tried to perpetuate VRAs after the withdrawal of Government support. But he claimed that it would become more difficult for manufacturers to do this following the written answer and the publicity which this had received. Nevertheless, he was asked to report back to the Sub-Committee on the question of whether the Government should take further action to terminate such arrangements.

4. The paper records that support was withdrawn for arrangements relating to music centres and mono TV sets at the end of 1985. Lord Young says that he has no doubt that these arrangements were not continued. But rather oddly he adds that "even in 1985 they were of little relevance". This seems to suggest that if DTI's understanding is incorrect, the maintenance of the arrangement is nothing to worry about anyway. That begs the question why the UK industry sought the protection it afforded in the first place: it must have been of some value to them. It would be worth asking Lord Young if DTI have independent evidence which confirms their understanding of the situation.

5. Support was withdrawn at the end of 1987 from the arrangement covering pottery imports from Japan. DTI have checked the current position with the British Ceramic Manufacturers Federation and Lord Young understands that they are taking steps to terminate the arrangement. DTI will be confirming the BCMF position in due course. It is unsatisfactory that 7 months after the withdrawal of Government support the arrangement still exists. You could ask Lord Young what steps DTI will be taking if the BCMF do not end the arrangement very soon.

6. Arrrangements covering cutlery imports from Korea and Japan also lost support at the end of 1987. Lord Young indicates that the British Cutlery and Silverware Association are nevertheless seeking to maintain this arrangement, although is not clear with what sucess. He says that DTI will be making sure that the Association fully understands the Government's view of these arrangements.

7. A third set of arrangements which lost support at the end of 1987 was those covering colour televisions imported from Japan and the Asian NICs. Having consulted the trade association involved, Lord Young says DTI have no reason to believe that these VRAs are continuing. He suggests that the import figures for the first 4 months of 1988 confirm this. We have examined these figures and these show a very significant increase in imports from Japan since the end of 1987 but it is difficult to discern any change in imports from the other countries involved (Singapore, Korea and Taiwan). It would be more reassuring if some independent evidence confirmed that the arrangements for these countries have indeed come to an end.

8. The paper says nothing about possible further steps which could be taken over arrangements which persist in the face of government disapproval. Lord Young says that the attention of exporting countries has been drawn to the answer to the recent PQ and it is true that British Embassies in the countries concerned have been briefed to confirm that the government no longer supports certain specified arrangements. But there may be a case for a high profile approach with DTI Ministers writing to their opposite numbers in

these countries to reinforce the message. Possible legal avenues for action should also be considered. DTI officials have indicated to us that some VRAs may be in breach of the Restrictive Trade Practices Act 1976 (RTPA). Possible grounds for legal action under this statute should be considered in those cases where arrangements persist and the Office of Fair Trading should be brought in if appropriate. There is also a need to look to the future and a need for a legal mechanism to outlaw these arrangements. It is believed by DTI that the new legislation which has been proposed in a recent Green Paper to replace the RTPA would catch VRAs. This legislation would be aimed at agreements which give rise to anti-competitive effects: the existing legislation only catches agreements which exist in a particular form. The Green Paper suggests that the new legislation would establish a general prohibition but would provide an illustrative list of particular forms of agreement which the legislation is targetted upon. DTI should consider whether VRAs should be included on this list. (It should be added that it is conceivable that when the Internal Market is completed in 1992 the European Commission will outlaw national, as opposed to EC wide restrictions, such as VRAs. But until it is clear what their policy will be it would still appropriate be for the UK to consider what can be done domestically to outlaw these arrangements.)

9. Closing the paper, Lord Young says that it is difficult to prevent exporting countries from limiting their exports unilaterally if they consider such action to be in their own interest. He quotes the current example of Korea which is allegedly limiting the quantities of consumer electronic products being exported to the Community because of its concern about current anti-dumping

investigations by the European Commission. This example of restraint is not obviously relevant to the situation which applies to VRAs. The self interest which may more typically encourage unilateral export restraint is that arising from the opportunity to be given a market slice with high profits attached. But it will not always be the case that this would be preferable to a larger market share with a smaller rate of profit. The avoidance of political disputes which export restraints may bring may be welcome to the exporter but if the government in the importing country expresses its opposition to such measures such self denial is unlikely to serve any political purpose.

Reference No: E0587

SECRETARY OF STATE FOR EMPLOYMENT

MILK MARKETING ARRANGEMENTS

(Letter from Mr MacGregor to the Chancellor of 1 July;
Letter from PUSS, Welsh Office to the Chancellor of 8 July)

DECISIONS

Mr MacGregor reports that Dairy Crest, the marketing subsidiary of the Milk Marketing Board (MMB) is now operating independently of its parent. The Sub-Committee may be able substantiallyto accept that and if that is all could agree Mr MacGregor's proposal that it should review the relationship again in two year's time.

2. The more important question is whether the Sub-Committee should ask for a furether report on more radical changes, such as abolition of the MMB's monopoly of purchase or the possible sale of its Dairy Crest subsidiary.

BACKGROUND

3. The MMB is the statutory monopoly buyer of virtually all fresh milk produced in England and Wales. It purchases all milk offered to it, within EC quota limits, and any surplus to immediate consumption requirements goes to butter or cheese production and can end up in intervention stocks. The Board is financed by the 38,000 milk producers and the Government is not involved financially. It also administers the Common Agricultural Policy price regime (a task which would otherwise fall to MAFF), co-ordinates milk marketing companies and has certain milk hygiene and quality responsibilities (the industry is burdened by heavy regulation).

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4. The MMB also has a subsidiary, Dairy Crest, which buys and markets about 20% of the milk sold by the Board.

5. In 1985 the Government appointed consultants (Touche Ross) to carry out a detailed study of the commercial operations of Dairy Crest, following complaints by the Dairy Trade Federation (DTF) that Dairy Crest was not competing with the independent dairy companies belonging to the DTF on an equal footing, as required under EC law. Touche Ross concluded that Dairy Crest's rate of return might not have been acceptable to a commercial company and that certain changes could be made to ensure that they operated at arm's length from the MMB. E(CP) therefore considered three options in July 1986 (E(CP)(86)1st meeting). These were:

1 ending the MMB's purchasing monopoly;

2 requiring the MMB to dispose of its Dairy Crest subsidiary;

3 changing the relationship between Dairy Crest and the MMB to meet the immediate criticisms of the Touche Ross report.

6. E(CP) accepted Mr Jopling's recommendation of the least radical option 3. MAFF also offered comprehensive monitoring of Dairy Crest's performance and of MMB's compliance with EC law. Before the meeting, the Prime Minister had said that it would not be timely to pursue the other two options. It was also agreed that Dairy Crest's relationship with the MMB should be reviewed after two years, and a further report submitted to E(CP).

ISSUES

Recent Review of Dairy Crest

7. Mr MacGregor's letter gives limited information about his reasons for concluding that the present relationship between the MMB and Dairy Crest is satisfactory. Annex II to his letter summarises the progress made in implementing the Memorandum of Agreement of July 1986 between the Government, and MMB and the DTF (attached at Annex

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I). Ministers may ask for more information about Mr MacGregor's review before reaching a decision. In particular, there are some points in Annex II which seem worth probing:

a. Has a target rate of return yet been set for Dairy Crest (item 6 of Annex II)? The wording here suggests that there have been some difficulties.

b. What issues from the report on Dairy Crest's activities for April-September 1987 are still under discussion with the MMB (item 20 of Annex II)? Has the report for the year to March 1988 been received? If so, are any important issues raised? If not, is monitoring keeping sufficiently up to date?

c. Mr MacGregor's letter (on the first paragraph of the second page) says that DTF's complaints about Dairy Crest have been 'largely' silenced. What DTF complaints are outstanding? Do they have any substance?

d. Has sufficient progress been made in separating Scottish Pride (Dairy Crest's Scottish equivalent) from the 3 Scottish Milk Marketing Boards Mr MacGregor's letter (page 2) implies that this is only being discussed.

8. Depending on the discussion, you may be able to sum up that E(CP) accept that Dairy Crest's relationship with the MMB is reasonably satisfactory, and should be reviewed again by E(CP) in two years time, as Mr MacGregor proposes. But the more important question is whether to reconsider the more radical options.

9. The most radical would be abolition of the MMB monopoly. The Financial Secretary may propose that it should now be seriously considered. The main reasons for abolishing the monopoly are -

a. it is wholly inconsistent with the Government's policy of promoting competition to retain a statutory monopoly in milk marketing;

b. the monopoly is likely to introduce cross-subsidies between producers and is unlikely to be in the best interests of consumers;

10. Against this, it may be argued that -

a. there is widespread support by producers for the present arrangements, so any legislation to abolish the MMB would be controversial;

b. abolition could destroy a national system of prompt distribution of a perishable product, and longstanding arrangements for providing price stability despite peaks and troughs in demand and production;

c. abolition might lead to higher intervention stocks;

d. abolition might put at risk the wide availability of doorstep milk delivery;

e. abolition might lead to lower prices for small isolated producers, putting at risk employment in marginal agricultural areas.

11. The case for proposing a study is that it would allow the weight of arguments for and against abolition of the MMB's monopoly to be carefully investigated. Depending on the discussion, therefore, you may wish to propose that Mr MacGregor should be asked to come back to E(CP) in 3 months times with a detailed report on the abolition of the MMC's monopoly. It would be helpful to suggest that MAFF involves Treasury and DTI officials in the preparation of the report, and that the report should identify any significantly different considerations in respect of the Scottish and Northern Irish milk marketing arrangements.

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Privatisation of Dairy Crest

12. A less radical option would be to require the MMB to dispose of Dairy Crest. This also will be opposed by Mr MacGregor. You could however ask him to report back on the possibility. It would be much better for such a report to be additional to the report on ending the monopoly, not a substitute for it.

HANDLING

13. You may wish to invite the Minister of Agriculture, Fisheries and Food to describe why he is now confident that the revised commercial arrangements between Dairy Crest and the MMB are now working satisfactorily. The regional Agriculture Ministers have a direct interest. The Secretary of State for Trade and Industry and the Financial Secretary, Treasury may wish to comment on the implications for competition policy. Other Ministers may wish to contribute to the discussion.

G W MONGER

Cabinet Office
22 July 1988

CONFIDENTIAL

Reference No: E 0589

SECRETARY OF STATE FOR EMPLOYMENT

MOTOR VEHICLES: PRICE DIFFERNTIALS IN THE EUROPEAN COMMUNITY

[E(CP)(88)11]

DECISIONS

E(CP) need to decide whether the UK should take further action within the European Community (EC) over the differentials which exist between motor vehicle prices here and in most other member states.

2. The Secretary of State for Trade and Industry argues that the differentials are falling, and that we should take no action unless the favourable trend is reversed. However the paper shows that vehicle prices in a number of states are still substantially below UK prices, even after average discounts: in Denmark 23% lower, in Belgium 14% lower and in the Netherlands 12% lower. This is an area where successful action would bring direct and obvious benefits to consumers. E(CP) may therefore want to consider whether any action can be taken.

BACKGROUND

3. For many years car prices in the UK have been well above those in some other member states, notably Belgium, Holland and Denmark. In a competitive market such differentials could not be expected to persist in the absence of substantial cost differences. However the arrangements for marketing cars do not live up to the ideal of perfectly free competition: selective car distribution systems are exempt from the EC prohibition on restrictive agreements.

4. Following pressure on this point, the EC Commission introduced a new Block Exemption Regulation on 1 July 1985. This maintained the exemption, but provided new safeguards which allowed individual car buyers to import from other member states. But it did not require manufacturers to supply right hand drive cars to continental dealers for stock, or to supply such cars for resale to unauthorised UK

importers/dealers. Consequently parallel imports have not developed on a commercial basis.

5. E(CP) last considered this subject in April (E(CP)(88) 2nd Meeting), when Lord Young put forward similar arguments against any change, on the basis of comparative price figures for July 1987. The Sub-Committee asked him to submit a further report based on the most up-to-date figures; to consider factors which might justify the price differentials, such as higher discounts in the UK or genuine cost differences; and to consider whether the Block Exemption Regulation was a material factor.

MAIN ISSUES

Price differentials

6. The only recent price figures are in paragraph 2 of the Note by Officials. They come from a small scale survey dated March 1988, and suggest that, for the four countries covered, there was little change compared to the fuller survey of July 1987. However since March there has been a further appreciation of sterling against the main European currencies. You may like to ask Lord Young what impact this is likely to have had on differentials.

7. The paper bases its arguments on the fact that, taking account of discounts, the average differential between UK prices and those on the continent is now only 6 per cent. However this figure masks the much higher differentials between the UK and nearby countries like Denmark (23%), Belgium (14%) and the Netherlands (12%) - paragraph 5 of the note by officials. These differentials have persisted over a period of years, although their exact level has varied. Furthermore the paper admits that there are no genuine cost factors which justify the price differences. E(CP) may want to consider whether any action can be taken to bring this situation to an end.

Action by EC Commission

8. The EC Commission is preparing proposals to toughen the application of competition rules to the vehicle industry. Press reports refer to action on vehicle type approval, on subsidies to car manufacturers, and on restrictive import agreements with non-EEC countries like Japan. You may want to ask Lord Young whether the

Block Exemption Regulation is under consideration as part of this review. (See the attached article in the FT for 22 July).

9. The most radical possibility would be removal of the exemption of selective car distribution systems from the EC prohibition on restrictive agreements. You may wish to ask Lord Young about this. He may argue that it would not be practical to negotiate such a major change, which would affect the interesta of the motor industry in all member States. The Commission's reported intention to propose changes in other rules affecting this industry might however give us a good opening.

10. If you did not want to go that far, you could ask Lord Young to press the Commission for amendments to the Regulation. Possibilities include:

i. requiring manufacturers to supply right hand drive cars to continental dealers for stock (paragraph 14 of the Note by Officials). The manufacturers have argued that this would prejudice dealers' primary role of providing a comprehensive service in the territory allocated to them. The Note by Officials also argues that dealers would not wish to stock cars for a possibly transient parallel trade. You may feel that dealers should be free to judge for themselves, and that on past evidence a parallel trade might be far from transient;

iii. requiring manufacturers to supply cars for resale to unauthorised importers (paragraph 15). The paper argues that the 6% differential with average community prices might not be sufficient to provide such dealers with a profit. But it is surely the differentials with individual countries which are important: commercial importers would choose to buy in Denmark, at prices 23% below UK levels, not at the community average price. You may therefore feel that this route to commercial competition should be open.

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11. Finally, there is the possibility of pressing the Commission to take action within the existing regulation. In his previous paper, Lord Young said that the EC Commission's policy was to investigate possible withdrawal of the block exemption where price differentials persisted above 12%. This condition is met in the case of Denmark (where the differential is nearly twice the limit) and Belgium. You may want to ask Lord Young why the Commission is not carrying out an investigation.

12. It may be that the best outcome would be that Lord Young agreed to explore these possibilities with the Commission. He could then report back on progress, perhaps in the autumn. A fallback would be to ask him for a further report to the Sub-Committee on the case for such negotiations and the best way of making them succeed.

13. Lord Young himself proposes only that he should report back at the end of 1989 on the outcome of the next price Survey. Even if the Sub-Committee does not pursue the case for some action now, at least he could be asked to report back earlier than that, say in mid-1989.

HANDLING

14. The Secretary of State for Trade and Industry will want to introduce his paper. The Financial Secretary, Treasury will want to comment. The only other Minister with a Departmental interest is the Secretary of State for Transport, who is responsible for the question of type approval and its implications for importers.

G W MONGER

Cabinet Office
22 July 1988

EC plans tougher rules on car industry barriers

By William Dawkins in Brussels

TOUGHER rules for the European Community's car industry are in the final stages of being drafted by the European Commission.

The changes would clamp down on national state aid to the industry, lead to the scrapping of bilateral car import restraint agreements between individual EC countries and Japan, and abolish the remaining technical barriers to free Community trade in cars.

A full meeting of the Brussels executive this week paved the way for completion of a white paper on the car industry by endorsing plans from Mr Peter Sutherland, the Competition Policy Commissioner, to restrain government subsidies to car makers.

Commission officials say their main concern is to avoid governments using regional aid to outbid each other for Japanese investment.

The details will be part of a final package of proposals, expected to be adopted as official policy by the Commission in the autumn.

Japanese producers manufacturing in the EC would also have to abide by the tougher state aid procedures. The paper makes no response to demands, especially from France, for tough controls on the growing wave of Japanese car assembly in the EC.

A draft version of the document proposes that the number of Japanese cars sold in the Community should be frozen at present levels – just over 1m cars annually, or 9.5 per cent of the market – until 1992, to protect EC car makers while they adjust to the ending of internal market barriers.

In return, there would be an immediate end to the varying restrictions on Japanese car imports imposed by the UK, France, Italy, Spain and Portugal.

The main internal market barriers scheduled in the paper for removal are the differing national type approvals required for windscreens, tyres and towing weights. EC type approval is possible for all other car components and performance requirements.

On state aid, the Commission is considering plans to force governments to obtain advance clearance from Brussels for all assistance where total investment is worth more than a fixed minimum. This would be in contrast to the present practice of giving blanket clearance to general national aid schemes for less developed regions.

Brussels is understood to have considered setting a minimum level of local content for Japanese car assembly in the EC, an idea favoured by Mr Karl-Heinz Narjes, Industry Commissioner.

That idea has been scrapped at least at this draft stage, in the belief that it could contravene the General Agreement on Tariffs and Trade.

Industry officials say local content rules can only be applied in the context of a legitimate trade grievance, such as an anti-dumping action.

New broom, Page 2; Editorial comment, Page 22

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Reference No ED588

SECRETARY OF STATE FOR EMPLOYMENT

ACTION PROGRAMME AND FUTURE WORK OF THE SUB-COMMITTEE
E(CP)(88)10

DECISIONS

Discussion of this item can be brief. You could simply propose broad endorsement of Mr Maude's proposals. Other Ministers may have detailed comments on the Action Programme at Annex A but they could be asked to take them up bilaterally with Mr Maude. You could ask the Transport Secretary to put in a paper for the meeting after next on liberalisation of air services.

BACKGROUND

2. The Action Programme has been a regular feature of E(CP). It was last discussed at E(CP) in January, and has been updated for this meeting.

ISSUES

Action Programme

3. This contains some interesting items, some of them newly added. You will not, however, wish to get drawn into substantive discussion. Mr Maude has asked his officials to reconsider all the deadlines. We understand that, in the limited time available, DTI did not manage to consult other departments about the new dates, with the result that some of them may appear somewhat arbitrary or inappropriate. If such points are made about particular items, you may wish to suggest that they are settled with Mr Maude outside the meeting. If necessary, Mr Maude could then circulate as an E(CP) paper whatever changes he has agreed.

Agenda for next meeting

4. A suggested agenda for E(CP)'s next meeting on 5 October is described in paragraph 5 of Mr Maude's paper. It may not need separate discussion. If it does you could suggest endorsement, subject to two points:

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- The Financial Secretary is expected to suggest that the paper from the Scottish Office on restrictions in the legal profession should be as wide-ranging as the Lord Chancellor's paper. Indeed, Mr Lang offered such a paper at the previous discussion of the legal profession in January. You may therefore wish to suggest, or endorse Mr Lamont's suggestion, that the Scottish paper should not only consider fee sharing and multi-disciplinary practices involving solicitors as proposed in Mr Maude's paper , but all the issues due to be covered by the Lord Chancellor (in accordance with the remit he received in January).

- The DTI paper on VRAs and other quantitative restrictions on UK imports is also a substantial item. It was proposed by the Chancellor in his letter to Lord Young of 1 June. There may, therefore, not be time for Mr Maude's paper on barriers to multi- disciplinary practices in the professions or for anything else on 5 October. However, you will wish to welcome Mr Maude's offer of this paper and say that E(CP) will certainly want to consider it shortly.

European Air Services

5. E(CP) discussed the liberalisation of European air services in July 1986. The Chancellor summed up by stressing the importance of further progress on reducing scheduled air faces in Europe, both through bilateral negotiations and through discussion in the Community. He invited the Transport Secretary to report back on progress 'at an appropriate time'. Now that 2 years has passed it seems appropriate to review this issue again. You may therefore suggest that Mr Channon prepares a report on liberalising air services in Europe by the end of October, for consideration at the meeting after next.

Frequency of meetings

6. Mr Maude may suggest that E(CP) should meet more frequently in the future than it has recently. In fact it looks as though there will be 5 meetings of E(CP) this year, compared to 2 in each of 1986 and 1987, so the Sub-Committee is already getting through much more work than before. You could point this out, and give a general encouragement to the idea of keeping up a high level of work for the Committee, but point out that anything more precise, such as a target number of meetings, should be a matter for the Chancellor.

HANDLING

7. You may wish to invite the Parliamentary Under-Secretary of State for Corporate Affairs to introduce his paper. The Financial Secretary, Treasury and other Ministers may wish to comment.

G W MONGER

Cabinet Office
22 July 1988

CONFIDENTIAL

Reference No E 0591

SECRETARY OF STATE FOR EMPLOYMENT

VOLUNTARY RESTRAINT ARRANGEMENTS ON IMPORTS

(E(CP)(88)12

DECISIONS

This discussion can be brief. E(CP) are concerned that Voluntary Restraint Arrangements (VRAs) may continue when Government support is withdrawn. You might simply ask Lord Young to give an oral report on his efforts to ensure that they do not, especially on the pottery and cutlery VRAs where his paper leaves some doubt about what is happening.

BACKGROUND

2. VRAs have been considered regularly by E(CP) over the last 3 years. They are usually bilateral agreements between a UK trade association and manufacturers in a particular foreign country, with the implicit blessing of both Governments involved. The Chancellor concluded E(CP)'s discussion of VRAs in May by saying that the objective should be to phase out those remaining. He also said that withdrawal of support for further VRAs should be specifically announced in a Parliamentary written answer. Government support has been withdrawan for 30 VRAs, and only remains for 8. This meeting only needs to consider the relatively narrow issue of how to ensure that VRAs for which Government support is withdrawn are effectively terminated.

ISSUES

The Problem

3. There has recently been talk that some trade associations were trying to continue VRAs even after Government support was withdrawn: see for example the attached cutting from the Economist. DTI had been reluctant to publicise their withdrawal of support, ostensibly because it would lead to awkward questions about the VRAs still in existence. The letters which DTI originally sent out to trade associations telling them of the Government's decision to withdraw

support could have added to the confusion, because they did not state explicitly the Government's view that the relevant VRAs should end, but only that its support was ceasing.

Subsequent Action

4. When DTI's attention was drawn to what was happening, they gave in a Parliamentary written answer a list of all the VRAs for which Government support had been withdrawn. They also drew this answer to the attention of the London embassies of the foreign countries involved (paragraph 3). However, it is not clear what action has been taken with UK trade associations. Lord Young's paper says (paragraph 4) that the British Cutlery and Silverware Association are trying to maintain their VRAs with Korea and Japan, although their success is 'not clear'. It also says that it will 'confirm' that the British Ceramic Manufacturers are ending theirs with Japan. None of this is very definite, and you may wish to ask Lord Young to report on the latest position on the pottery and cutlery VRAs. Members of E(CP) may wish to suggest any further action, in the light of Lord Young's report.

5. The conclusion could probably be that the Sub-Committee notes the steps taken by Lord Young to ensure the termination of VRAs from which the Government has withdrawn support, and invites him to keep up the pressure as necessary.

HANDLING

6. You may wish to invite the Secretary of State for Trade and Industry to introduce his paper. The Financial Secretary, Treasury and other Ministers may wish to comment.

G W MONGER

Cabinet Office
22 July 1988

British trade

Economist 22/4/88

Grey areas

JAPANESE carmakers are in London to discuss "prudent" marketing policies in Britain for 1988-89. On May 10th South Korean shoemakers will visit the British Footwear Manufacturers' Federation to discuss how many pairs of shoes they should export to Britain. Both visits are about voluntary restraint arrangements (VRAs): deals in which foreign firms agree to keep down their exports to Britain. A month ago, a junior trade minister told Parliament that "government pressure has resulted in the termination of no fewer than a dozen" VRAs. Yet the government tolerates VRAs on six groups of products. It disapproves of VRAs covering another five—but nobody takes much notice.

VRAs have all the economic disadvantages of import tariffs, and three more besides. First, a VRA lets the foreign supplier collect the value that is being denied the consumer—for while a tariff diverts that value to government, a VRA lets the supplier put his prices up to keep his sales down. Second, VRAs divert trade away from the low-cost foreign suppliers which sign them to higher-cost ones which do not. Third, VRAs are not open for all to see.

This is why protectionist industries like them. Consumers, being ignorant of VRAs, do not object. Politicians can disclaim responsibility, arguing that they are a business-to-business affair. And VRAs are in the grey areas outside the General Agreement on Tariffs and Trade (GATT).

Why does Britain's government, so preachy about free markets, tolerate VRAs? In some cases, it does not have the evidence to quantify the damage they do. (Several British trade associations say that their VRAs have not in fact restricted imports at all: odd, then, that they should want them.) More often, as with the deal which has limited imports of Japanese cars to 11% of the British market since 1977, the political cost is too high. Although a study from the Trade Policy Research Centre argued in 1985 that this car deal has cost British consumers up to £500m a year, its abolition might raise the market share of imported Japanese cars to above 20%, cutting British carmaking capacity by 100,000 a year. That would make Rover less attractive to British Aerospace.

On March 30th, the Department of Trade and Industry named the products which it no longer wants covered by a VRA. On the list: monochrome and colour TVs, music centres, stainless steel cutlery and pottery.

The British Ceramic Manufacturers' Federation, which has operated for 15 years a tight VRA with Japanese pottery firms, has kept quiet in the hope that the Japanese will disregard the government statement. The Cutlery and Silverware Association, whose deals (first signed in 1966) now limit exports of spoons and forks from Japan to 2.5m dozen and from Korea to 4.05m dozen, says that the government's change of mind has had no effect on its arrangement. Equally unworried is the British Radio and Electronic Equipment Manufacturers' Association, which for at least 12 years has talked regularly with Japan, South Korea, Singapore, Taiwan, Hongkong and once even with Thailand.

In short, exporting firms in Asia are themselves happy with covert deals that assure them a market slice with high profits and little political trouble. To change things, Britain must be more assertive. One hope: the Uruguay round of world trade talks is already discussing how to prevent "grey-area" protectionist arrangements, although there is little chance that VRAs will be outlawed.

If the EEC's plans for a single market are ripe by the end of 1992, national VRAs will have to be replaced by Community-wide arrangements. That is no guarantee of rationality; it might even make things worse. The EEC already has communal non-tariff barriers in steel and in textiles. If the example of cars is anything to go by, most other European countries are more protectionist than Britain. The share of the British market cornered by imported Japanese cars is, at 11%, almost two percentage points higher than the average for the EEC. Portugal allows each Japanese firm to export only 15 cars to it a year.

CONFIDENTIAL

Reference No E0590

SECRETARY OF STATE FOR EMPLOYMENT

AUCTION OF RADIO SPECTRUM LICENCES
E(CP)(88)8

DECISIONS

Colleagues will welcome in principle Lord Young's plans for auctions for allocating licences in certain mobile radio bands, and for issuing a consultative document in the autumn. However, both Mr Hurd and the Financial Secretary will wish to modify his specific proposals. The following issues are likely to be raised -

i. should auctioned licences last for a limited period or indefinitely?

ii. should any further licences issued under existing arrangements in the auctionable bands only last until auctions begin?

iii. should Ministerial discretion in accepting auction bids be open-ended in legislation, or should it be limited as in the proposed arrangements for awarding the next round of ITV franchises?

iv. should legislation on auctioning be prepared flexibly to allow licensing of spectrum by auction outside the mobile bands in due course?

BACKGROUND

2. In his paper to E(CP) in May Lord Young proposed the auctioning of certain mobile bands as one means of introducing more competition into the allocation of spectrum. E(CP) agreed, and asked him to submit a further paper in July with detailed proposals. This paper is the result..

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ISSUES

3. The remainder of this brief covers four issues which Mr Hurd and the Financial Secretary are expected to raise in discussion. They will be concerned principally to minimise administration and Ministerial involvement in the auctions, and to maximise receipts to the Exchequer.

Period of licences

4. Lord Young proposes that although auctioned licences would be subject to revocation after a period of notice, they would not have a maximum period (paragraph 8). His reason for avoiding a fixed termination date is that, if the date approached and renewal was not granted, the licensee would be left with equipment which he was unable to use. The risk of this occurring could deter full economic use of the spectrum

5. On the other hand, Mr Hurd and the Financial Secretary may suggest that -

a. lack of renewal could stifle new technical developments and new users and permit increasingly inefficient use of the spectrum;

b. unlimited licence periods could result in loss of revenue for the Exchequer, because bidders would be unlikely to allow much in their bids for uncertain profits beyond 10 years or so.

Depending on the discussion, you may conclude that the consultative document should propose licences would be auctioned for periods of 10-15 years.

Licensing procedures until auctioning begins

6. Lord Young points out that decisions have to be taken about the continued operation of licensing until auctioning begins in 2 years time (paragraph 12). He recommends that licensing in the mobile bands, should continue as before, in response to demand, until the auction legislation comes before Parliament. He then feels that

there would be a good case for refusing to grant any more licences until auctioning began. The difficulty with this approach, which he recognises, is that once the consultative document is issued, there will be a strong incentive for users to seek licences over the next year, at well below market prices, in the bands which were due to be auctioned. This might leave little spectrum left for auctioning by the time the legislation was through. The Financial Secretary will suggest that this should be avoided by permitting only short term use of auctionable bands for the next 2 years. Lord Young says this would produce "planning blight" on these frequencies, and lead to inefficient development of spectrum use in the important run-up to 1992. You will wish to assess the strength of the arguments in discussion. One possible compromise might be to licence spectrum over the next 2 years for relatively short periods of, say, 5 years.

Ministerial discretion

7. This may be the most controversial issue. Lord Young says it is essential to retain Ministerial discretion to award a licence to other than the highest bidder in exceptional circumstances where it appears to be in the public interest to do so (paragraph 11). He would not want any legislative provision which constrained how he could exercise this discretion. Lord Young has in mind taking into account international obligations, security matters, competition policy or technical use of the spectrum.

8. The Financial Secretary may suggest that this list is so wide ranging that the end result of the auctioning system could be little different from the present administrative arrangements. A more open approach with discretion limited and clearly specified would be more in line with the Government's competition policy. Mr Hurd may suggest that the auction arrangements should follow the proposals for awarding the next round of ITV franchises. This would involve a 2 stage process - DTI would first satisfy itself that bidders met a minimum quality or acceptability threshold, and then in the second stage licences would be awarded simply to the highest bidders who survived the first stage. You may conclude that an approach to

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spectrum auctioning which paralleled the broadcasting proposals would be the best way forward.

Flexibility in legislation on auctions

9. Mr Hurd may suggest it would be appropriate for legislative provision to be taken for auctioning of spectrum across a wider range of frequencies than the mobile bands. Lord Young is unlikely to object to this in principle. You may however suggest that there should be further consultation between Ministers on precisely how wide such powers might extend, (would they include broadcasting frequencies, for example) and not try to settle this in the meeting.

Next Steps

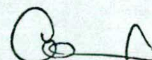
10. There are two ways of dealing with obstinate disagreements, in the interest of rapid progress:

a. They could be discussed further between the Ministers concerned, for example when the draft consultation document is prepared.

b. Alternative options could be put in the consultative document, and the government could make up its mind in the light of the response.

HANDLING

11. You may wish to invite the Secretary of State for Trade and Industry to introduce his paper. The Home Secretary, who has been invited for this item, will wish to respond. The Financial Secretary, Treasury will also wish to comment. Other Ministers may wish to contribute to the discussion.



G W MONGER

Cabinet Office
22 July 1988

CONFIDENTIAL

Reference No: E 0592

SECRETARY OF STATE FOR EMPLOYMENT

E(CP) 25 July

I attach detailed briefing for E(CP) on Monday.

2. We have put auctions of radio spectrum licences first so that the Home Secretary, who is attending only for that item, can get away quickly. We have put the three agricultural subjects next because the regional Ministers are attending only for those.

3. The agenda seems very formidable, but it is not as bad as it looks. Most of the items are progress reports, and will not require much discussion.

4. Item 1, on auctions of radio spectrum licences, ought not to take long. There are no differences of principle, although the Home Secretary and Financial Secretary will have detailed points on Lord Young's proposals. If necessary, disagreed points could be remitted to discussion between the Ministers directly concerned.

5. Item 2, on the Wool Marketing Board, is the most substantial item. There could be a disagreement. Mr MacGregor proposes to give up the Government guarantee, but wants to keep the Wool Marketing Board's monopoly buying and other activities unchanged. He will have the support of the regional Ministers. Mr Ridley, Lord Young and Mr Lamont are all likely to argue for abolition of the Board. The monopoly buying power seems clearly inconsistent with the Government's general policy. We have however suggested that if there is a disagreement that cannot be readily resolved, possible ways forward are to ask for a further report by Mr MacGregor on the possibility of replacing the Board by a voluntary cooperative or, less radically, requiring it to privatise its subsidiaries.

6. The underlying questions on item 3, milk marketing arrangements, are equally important and contentious. Again the agriculture

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Ministers will want to leave the Milk Marketing Board unchanged, and Ministers concerned with competition will want, at the extreme, to abolish it. But this item should be easier to deal with. There is no question of a final decision on Monday on the more radical possibilities, and if the case for a radical change is pressed you could simply ask Mr MacGregor for a further report on the possibility of abolishing the Board or, less radically, requiring it to dispose of its Dairy Crest subsidiary.

7. The point on potato support, item 4, is very limited. It is whether the consultative document which Mr MacGregor has circulated should state the Government's preference for moving to a free market, or should be neutral. There are gradations between these two positions.

8. Price differentials in the EC for cars, item 5, is an interesting subject. The DTI argues against action now, but most other members will want to take action to reduce the differential against the UK car buyer if a way can be found of doing so. It is not clear how far Lord Young would, if pressed, resist this. This is an area where successful action would bring direct and obvious benefits to the consumer. The brief suggests asking Lord Young to propose changes in the current rules to the Commission or press them to take action. As a fallback, he could put in a further report on these possibilities.

9. Item 6, VRAs on imports, requires very little discussion. The Sub-Committee could note the action taken by Lord Young to ensure the termination of VRAs from which the Government has withdrawn support, and ask him to keep up the pressure.

10. Item 7, the action programme, also requires very little discussion. The Sub-Committee could broadly endorse it.

G W MONGER

Cabinet Office
22 July 1988

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CH/EXCHEQUER
REC. 27 JUL 1988
ACTION FST
COPIES TO

The Rt Hon Nigel Lawson MP
Chancellor of the Exchequer
HM Treasury
Parliament Street
LONDON
SW1P 3AG

July 26

Dear Nigel.

In your absence I chaired the meeting of E(CP) on 25 July.

On item 1, auctions of radio spectrum licenses, the Sub-Committee accepted David Young's general approach, and agreed that the next step was the issue of a consultative document. They did however raise a number of points on his detailed proposals. He will consider these further in drafting the consultative document, and circulate a draft to the Sub-Committee before it is published.

On item 2, further [?] of the British Wool Marketing Board and the Wool Guarantee, the Sub-Committee endorsed John Gregor's proposal to abolish the guarantee. We came to no conclusion on the future of the Board, and John agreed to prepare further papers for the next meeting of the Sub-Committee on the possibility of replacing it by a voluntary co-operative, and of requiring it to divest itself of its subsidiaries. He will be anxious for a decision to be made quickly.

On item 3, milk marketing arrangements, it was agreed that this question would be pursued after wool and potatoes had been dealt with. John MacGregor will produce a paper for the Sub-Committee on the future of the milk marketing arrangements as a whole in the early part of next year.

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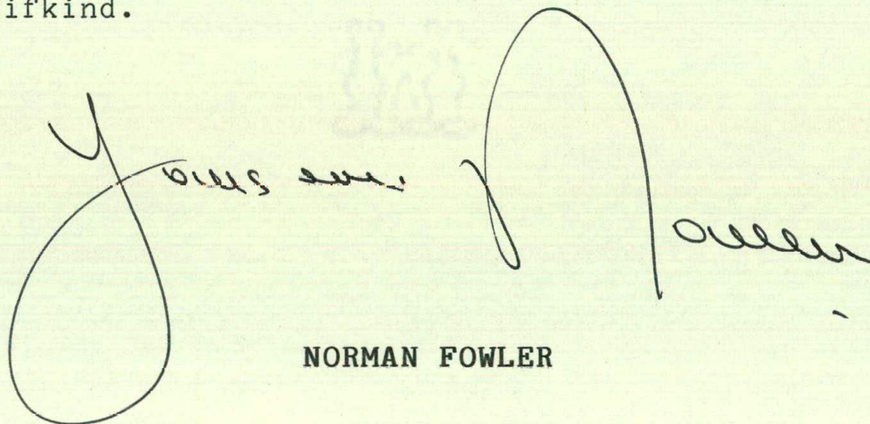
The Sub-Committee accepted John MacGregor's draft consultative document on potatoe support, item 4, and he will, as proposed, answer a Question before Parliament rises to give notice of its publication.

On EC car price differentials, item 5, the Sub-Committee agreed that a further paper should be circulated, as early as practical during next year, to give better and more up to date information about price trends.

On voluntary restraint arrangements on imports, item 6, the Sub-Committee noted the steps David Young is taking to ensure the termination of VRAs from which Government support is withdrawn, and invited him to maintain the pressure. He will report in October on the further steps he has taken.

Finally, the Sub-Committee broadly endorsed the action programme, item 7. The paper on the Scottish legal profession for the October meeting will be comprehensive like the paper being prepared by the Lord Chancellor on England. Paul Channon will prepare a paper for the autumn on the liberalisation of air services.

I am sending a copy of this minute to the other members of E(CP), and to Douglas Hurd, Peter Walker, Tom King and Malcolm Rifkind.



NORMAN FOWLER

Molan/minute/15

FROM: R MOLAN
DATE: 27 July 1988

PS/FINANCIAL SECRETARY

cc: PS/Chancellor
PS/Chief Secretary
Mr Lankester o/r
Mr Monck
Mr Mountfield o/r
Mr P G F Davis
Mr Burr
Ms Symes
Mr Wynn-Owen
Mr Tyrie

E(CP): QUANTITATIVE RESTRICTIONS ON IMPORTS INTO THE UK

Lord Young's letter of 26 July to the Chancellor rounds off an exchange of correspondence on a paper which will be considered by E(CP) in October.

2. The Chancellor wrote to Lord Young on 1 June suggesting that it would be desirable for E(CP) to be given the opportunity to consider the nature and extent of all restrictions on imports of non-agricultural goods into the UK as this world enable the Committee to consider effects of such restrictions on competition. Up until now the Committee have only considered those restrictions imposed by voluntary restraint arrangements reached on an industry to industry basis and not those imposed by government. To facilitate such a discussion in the Committee the Chancellor suggested that DTI produce a paper providing a overview of all such restrictions and explaining the justification for each measure and the arrangements for reviewing their continuation. He also asked that the paper examine the impact of such restrictions on consumers.

3. Lord Young replied on 15 June agreeing to circulate a paper in the autumn (for a meeting now fixed for 5 October) describing existing restrictions and informing the Committee of the work on them already carried out or planned for the future. The paper will also cover the voluntary restraint arrangements which continue at that time. He did add though that UK priorities in reviewing the remaining restrictions are largely determined by external factors such as the Uruguay Round and the completion of the single market.

4. Mr Fowler also wrote on 30 June to the Chancellor supporting his proposal and asking that the labour market implications of import restrictions would be one of the aspects which would be considered.

5. In his reply of 1 July to Lord Young the Chancellor acknowledged the importance of the Uruguay Round and the completion of the single market to this exercise. He noted the danger of 1992 giving rise to increased protectionism and commented that the Committee need to consider how consumer awareness of the implications of trade policy could be enhanced. He also suggested that Professor Silberston might be asked to update his analysis of the Multi-Fibre Arrangement, which regulates trade in textiles, and that the Enterprise and Deregulation Unit should have a look at the effects of import restrictions.

6. Lord Young's letter of 25 July satisfactorily ends the current exchange. He confirms that his paper will cover all restrictions on non-agricultural imports whether these are on a national basis or as part of a Community - wide arrangement. He says that some sectors may only be dealt with in general terms on the relevant detailed assessments will not be completed by autumn. This should not be a problem as we do not see this paper as a one off and so the Committee can return to this area at a later date. He agrees that the impact on the labour market and consumers should be considered and he welcomes a discussion on ways of creating a better informed consumer constituency. He accepts that the impact on business costs should also be looked at and the Enterprise Deregulation Unit will be consulted on this point. Most pleasingly of all he agrees that it would be helpful if Professor Silberston could update his report on the Multi-Fibre Arrangement. DTI will ask him whether he would be free to do this within a reasonable timescale. Failing that another suitable candidate for the task might be found.

7. In the circumstances there does not appear to be any need for Financial Secretary to reply to Lord Young's latest letter.

R MOLAN

FINANCIAL SECRETARY
REC. 28 JUL 1988
ACTION Miss G.M. Noble
COPIES TO PPS, EST
Mr. P. Russell
Mr. Neilson
Mr. Flanagan.

HOUSE OF LORDS,
LONDON SW1A 0PW

27 July 1988

Dear Nigel,

CONVEYANCING BY EMPLOYED SOLICITORS

On a number of occasions over recent years Ministers have considered the provision under the Building Societies Act 1986 for the recognition of conveyancing services by institutions and practitioners, and in particular the restrictions which should be imposed to safeguard the interests of the consumer.

The subject was mentioned again at E(CP) in January. Following that, Ministers suggested that officials should review the Government policy which was announced in 1985. That review has now taken place, and officials from the relevant departments have agreed the attached paper, which sets out the arguments for and against the current policy.

Colleagues will wish to consider the paper, in the light of the wider issues regarding competition policy in the legal profession which are under consideration by E(CP), although that may further delay the introduction of the conveyancing recognition system under the 1986 Act. I shall be interested to receive the views of colleagues.

I am copying this letter and attachment to the other members of E (CP) and Patrick Mayhew and to Sir Robin Butler.

Yours ever,

James.

The Chancellor of the Exchequer

FINANCIAL INSTITUTIONS AND CONVEYANCING

1. The question of banks' and building societies' powers to offer conveyancing services was discussed at E(CP) at the end of January. In subsequent correspondence, the Secretary of State for the Environment, the Economic Secretary and the Parliamentary Under Secretary of State for Corporate Affairs suggested that the opportunity be taken to reassess the proposed policy. They noted that there had been very rapid change in the provision of services for home buyers since the original policy had been agreed in December 1985, and it was not clear that the restrictions then envisaged were still appropriate. This paper, which has been agreed between officials of the Lord Chancellor's Department, Department of the Environment, Department of Trade and the Treasury, sets out the arguments for and against further relaxations.

Present policy

2. The current proposed policy was set out by the Solicitor General in a written answer on 6 December 1985 (copy attached at Annex A). He was reiterating statements by the Attorney General on 27 June 1985 and by himself on 17 July 1985 (Annexes B and C). These statements followed public consultation. They were confirmed by the Lord Chancellor during the passage of the Building Societies Bill on 10 July 1986 (Annex D). The policy proposed was that building societies and other financial institutions should be enabled to provide conveyancing, but not to their own borrowers; and the government would consider further the possibility of institutions owning minority stakes in firms of conveyancers. No figure has been given publicly for the size of this stake, but the Lord Chancellor's Department have had in mind less than 25 per cent. Schedule 21 to the Building Societies Act 1986, which provides the Lord Chancellor with the power to make regulations recognising institutions suitable to undertake the provision of conveyancing in England and Wales,

was enacted on the basis of this stated policy. Indeed it provides that the recognition rules may prescribe such conditions as appear to the Lord Chancellor to be appropriate for the purpose of "protecting persons for whom conveyancing services are provided by recognised institutions from conflicts of interest that might otherwise arise in connection with the provision of such services". The restrictions are not built into the primary legislation but the House was informed when the provisions were taken that the restrictions would apply.

Purpose of the restrictions

3. The proposed restrictions were intended to avoid the conflicts of interest which could arise if a solicitor employed by a bank or building society acts both for a society and for the borrower, between his duty to his employer and his duty to his client. Such conflicts could arise where the borrower reveals something to the solicitor which would reduce his chance of getting a loan if the information was passed to the lender. The separation also ensures that the solicitor is able to give independent financial advice to the borrower, about the type of mortgage which would be suitable to his circumstances, about the appropriate endowment policy, and whether he could secure better terms by going to a different bank, building society or other source for a loan.

4. The resulting conveyancing service that could be offered by institutions would not be particularly attractive to consumers. It would not, for example, allow a bank or building society to offer the "one stop" house buying service which they wish to offer and which customers appear to want, both as a matter of convenience and because the fewer people involved in the transaction the cheaper the service is likely to be.

5. The restrictions also seem to sit uneasily with recent proposals to expand building societies powers. Societies are already empowered to own estate agencies, sell insurance and give insurance advice. Under a package of orders which will come into

force on 30 August they will also be able to own or take an equity stake in a life insurance company, take an equity stake in a general insurance company (limited to 15 per cent for purely prudential reasons), provide pensions and fund management services, offer unit trusts, own a stockbroking firm, own removal firms, provide bridging finance, write wills, provide trustee and probate services and offer a wide range of housing and personal banking services. It might appear anomalous that they cannot offer the remaining key house buying service - conveyancing. On the other hand it can be argued that this service can be distinguished from the other services, on the grounds that, unlike them, conveyancing services would be offered to a borrower at a time when he is under pressure. He needs the mortgage and will not necessarily have the time or clear-sightedness to examine its terms adequately. This is why he will need particularly in this case to depend on reliable advice.

Possible conflict of interest

6. Although independent solicitors often act for both the lender and the borrower (at a significant saving for the customer), the solicitors accept instructions from them at a time after the mortgage terms have been considered and when the interests of the borrower and the lender are the same. They both wish the borrower to obtain good title. Until the mortgage terms are agreed their interests are not necessarily the same. The conflicts of interest which can arise are described in paragraph 3. While the borrower's interest is in a purchase which meets his particular requirements, the lender's interest is mainly in securing a commercially worthwhile transaction. So the concerns about conflicts of interest are legitimate enough. The questions for consideration are:

(a) whether, if the solicitor were actually employed by the lending institution, the conflicts of interest which would arise between lender and borrower would be recognised as such and would be sufficiently serious

and frequent to offset the perceived benefits of a more relaxed regime; and

(b) whether it is possible to provide sufficient safeguards to allow the customer at least a realistic and informed choice.

Possible safeguards

7. It would have to be made very clear to the borrower that the advice given by the society's solicitor is not independent. In addition lending institutions should not be able to insist that the borrower uses their solicitor. It should be possible to cover that in a suitable code of conduct, like the one which already exists for building societies. It would also have to be made clear at the outset that the employed solicitor could not represent his client in disputes with the society and may pass on any relevant information about the borrower to the society.

8. As for offering financial advice, any solicitor or conveyancer who wishes to advise on a particular endowment policy is covered by the Financial Services Act and will need to comply with its terms. Solicitors will be able to do this through their membership of the Law Society who will certificate them to do investment business. Conveyancers would have to apply either for membership of an appropriate self-regulating organisation or for direct authorisation by the Securities and Investments Board. (See Annex E for further details.)

9. This does not deal with possible conflict in advising about the particular terms of a loan contract. However, that is less of a disadvantage if the borrower knows that a solicitor or conveyancer is employed by, or is directly associated with, the institution making the loan and if there is an agreed code of conduct for stating particular items such as penalties or earlier repayment. An obvious parallel can be drawn with the arrangements for insurance brokers who must, under the Financial

Services Act, be either tied or independent. The consumer who buys from a tied broker knows that he will not receive impartial advice about products, but knows also that there are obligations to ensure, for example, that he is not sold inappropriate or unaffordable policies.

10. If it is felt that the risks of dealing with a solicitor or conveyancer employed by the lender are too great to give the customer the option, a further safeguard could be to require building societies to provide conveyancing services to borrowers only through a subsidiary or associated firm of conveyancers. The government has already said that it is prepared to consider allowing societies to own minority stakes in associated firms of conveyancers and, when Ministers discussed this issue briefly in January, it was suggested that an interest of up to 50 per cent might be reasonable (subject to checking commitments given to the House during the passage of the legislation).

11. In the case of building societies the risk of conflict of interest in the provision of estate agency services is already covered by a specific restriction. In that case societies can own the estate agents. Although these arrangements are unpopular with independent estate agents, there has been no evidence of problems or complaints from the customers and it is not clear why there should be any greater risk in the case of conveyancing where there would be the additional safeguard of professional codes of conduct.

The views of the Law Society and of the Marre Committee

12. The Law Society continues to believe that adequate safeguards are not possible. Although the Society is now prepared to allow lending institutions to refer clients to solicitors, it would not allow them to pay the solicitor's bills. It considers that this would dangerously restrict the solicitor's independence.

13. Any proposal to ease the restrictions envisaged in the Attorney General's original policy statement is likely to be

controversial and resisted by the legal profession. But it is clearly important that any restriction on institutions' ability to offer conveyancing services should be the minimum necessary to protect customers from the genuine risks of conflict of interest, and they should not be - or give the impression of being - a means of protecting the legal profession from competitive pressures to which other professions are exposed.

14. The recent Report of the Marre Committee on the Future of the Legal Profession expressed concern about the possibility of lending institutions becoming involved in the conveyancing process by offering a financial package to include legal services. Because of the conflicts of interest which may arise, and the absence of independent advice, they were concerned at the disadvantages that such arrangements would have for consumers. They referred to solicitors' experience in giving proper and impartial advice in connection with conveyancing transactions, including their financial aspects, and concluded that it must be of benefit to most people to employ solicitors in conveyancing transactions.

Timetable

15. The Lord Chancellor's Department has prepared an initial draft of part of the rules and had hoped to issue full draft rules for consultation before the summer with a view to implementing them around the turn of the year. That timetable has been delayed already following the correspondence suggesting reconsideration of the policy options (paragraph 1 above). If the current policy was changed there would clearly be further delay for the drafting needed to regulate the conduct of societies. Nevertheless, most banks and building societies would be content to live with the further delay if it resulted in more useful powers.

Summary

16. To summarise, the arguments for allowing a less restrictive regime are:-

i. Conveyancing is the only house buying service which the banks and building societies cannot offer; that is the only remaining obstacle to such institutions being able to offer the "one stop" service which consumers seem to want and find convenient.

ii. The circumstances in which potential conflicts of interest could do real harm to the customer are clear, although it cannot be certain how often they would arise in practice. At present, building societies frequently use the same (independent) solicitor as the borrower, at a significant saving for the customer - although only at a time when their interests coincide. The distinction between that and using the society's solicitor seems to be one of degree rather than substance, providing the customer is properly informed of the status of the solicitor, and given a clear choice.

iii. So far as offering independent financial advice is concerned, solicitors and conveyancers come within the scope of, and must comply with, the Financial Services Act if they offer advice on particular endowment policies. It is not clear that further protection is required.

iv. Although a society's solicitor would not be in a position to offer independent financial advice on the loan contract, a similar situation on insurance is dealt with by requiring the tied broker to inform his client clearly of his status.

17. Against that:-

i. A mortgage is likely to be the largest financial transaction in most people's lives. Borrowers need to be certain that they receive clear and impartial advice. This is at a time when they may be least likely to reach a reasoned decision on their own.

ii. The potential for conflict is greater when the borrower's conveyancer is employed than when he is instructed by the lending institution.

iii. The Government's current policy was agreed after public consultation and after intensive Ministerial discussions.

iv. The legislation was passed on the basis of clear and repeated statements of Government policy. It would be open to obvious criticism to change that policy after Parliament's reliance upon those statements, and at this late stage and without any indication in the intervening years that such a possibility was under consideration.

v. Any proposal to depart from the 1985 policy would be controversial and likely to cause further delay.

20 July 1988

Annex A

EXTRACT FROM HANSARD 6 DECEMBER 1985 Col. 354

Building Societies

Mr. Michael Forsyth asked the Chancellor of the Exchequer if he will make a further statement about the proposed building society legislation referred to in the Gracious Speech.

The Solicitor-General [*further to the answer given by the Minister of State, Treasury*, on 7 November 1985, c. *3*]: I can provide the following information.

The Government issued a consultation paper last year seeking views on the way in which conflicts of interest and anti-competitive practices could be avoided if building societies and other financial institutions were to offer conveyancing services to the public. Following that consultation, the Government have concluded that there is no difficulty in principle in such institutions providing conveyancing to persons to whom they are not also offering a loan. However, the Government are not satisfied that lending institutions could safely be permitted to offer both conveyancing and a loan in the same transaction. It is therefore proposed to prohibit lending institutions from providing conveyancing, either directly or through a subsidiary company in which they hold a majority stake, to those who are also borrowing from them.

The Government are also examining the possibility of estate agents providing a combined service of sale and conveyancing to vendors, and of lending institutions providing conveyancing to borrowers from them through associated companies in which the lender holds only a minority shareholding. Consultation on those matters is not yet complete.

It is also proposed to set a number of other conditions to ensure proper consumer protection. In particular, institutions will be required to ensure that their conveyancing work is supervised by a qualified person; and adequate arrangements will have to be made to protect the consumer against negligence or fraud on the part of those providing the service. Details will be announced in due course, after further consultations with the interests concerned.

Annex B

EXTRACT FROM HANSARD
27 June 1985, Cols 136 & 137

The Attorney General:...Our commitment is to permit financial institutions such as banks and building societies to offer conveyancing services, and to do so in a way that does not prejudice the consumer through conflicts of interest or anti-competitive practices. Both limbs of that commitment are important and both will be honoured....
The problem is that the arrangements for a loan are an integral part of most conveyancing transactions. The lender's employee cannot properly advise the borrower about the loan....
We remain firm in our resolve to find the correct solutions so that we can honour both limbs of our commitment.

Our conclusion is that we should bring forward amendments to the legislation which currently prevents all bodies corporate - including building societies - from offering conveyancing services. The amendments will enable the Lord Chancellor to exempt from the relevant restrictions those bodies which can properly be permitted to offer the service. The Lord Chancellor would have the power to impose any general conditions on the way in which the services were provided, to ensure that the consumer's interests are not prejudiced....

We see no difficulty in lending institutions offering the service in transactions where they are not providing the loan as well....
We are not at present - I emphasise at present - satisfied that lending institutions could provide a combined package of loan and conveyancing without risking unacceptable conflicts of interest. It is unrealistic to separate the arrangements for the transfer of title, on which the interests of the lending institution and the purchaser will generally coincide, from those for the loan. The loan is an integral part of the transaction. Lending institutions are commercial organisations and their interests in the arrangements for a loan are not the same as the borrower's. We have not as yet - I emphasise "as yet" - found a way round that, but my noble and learned Friend the Lord Chancellor recently met the Chairman of the Building Societies Association to discuss the matter.

We are still considering other possibilities. Lending institutions could perhaps provide the service through companies in which they held a minority share interest. It is possible that that would only dilute, rather than overcome, the conflicts, but we are examining that matter with the greatest care. (Administration of Justice Bill, Standing Committee D).

Annex C

EXTRACT FROM HANSARD
17 JULY 1985, Cols 379 and 380

The Solicitor General:... I wish to make clear the Government's position on conveyancing by employees of building societies and other financial institutions. We are committed to introducing legislation to permit banks and building societies to offer financial services and we are committed to doing so in a way that does not prejudice the consumer through conflicts of interest or anti-competitive practices. Both limbs of that commitment are important and both will be honoured.

The problem is that arrangements for a loan are an integral part of most conveyancing transactions and the lender's employee is inhibited in advising the borrower about the loan, because he owes his primary duty and his livelihood to his employer....

We have decided to amend the legislation that prevents all corporate bodies, including building societies, from offering conveyancing services. The Lord Chancellor will be empowered to exempt individual corporate bodies from the restrictions and to impose general conditions on the way in which the services are provided, to ensure that the consumers' interests are not prejudiced. The legislative mechanism will have to be flexible enough to enable new ideas to be implemented quickly and without the need for further primary legislation....

We welcome measures to reduce the number of agencies that a purchaser has to deal with when moving house, subject to the overriding need adequately to protect the public from conflicts of interest. We see no difficulties arising if lending institutions offer services in transactions where they are not also providing a loan.... Lending institutions are commercial organisations and their interest is in the arrangements for the loan, as distinct from ensuring good title, and is not the same as that of the borrower.... and one possibility under examination is that lending institutions might provide the services through subsidiary companies in which they hold only a minority stake.
(Administration of Justice Bill, Standing Committee D).

Annex D

EXTRACT FROM HANSARD
10 JULY 1986, Col. 559

Lord Chancellor:...The Government do not at present intend to allow lending institutions to offer conveyancing services to their borrowers. But if our worries over conflict of interest can be allayed, it will be possible for the then Lord Chancellor to bring forward the necessary amendment to the rules. The aim of those rules will be to ensure that the consumer is properly protected, but not to such an extent that unnecessary restrictions are imposed on those wishing to enter the conveyancing market.
(Building Societies Bill debate)

EFW

Annex E

BUILDING SOCIETIES AND CONVEYANCING WITH REFERENCE TO THE FINANCIAL SERVICES ACT 1986

The Financial Services Act 1986 is concerned with investments and investment business as defined in Schedule 1 of the Act. Mortgages are not included in these definitions although endowment insurance policies are. Building societies offering such policies and/or advice on such policies fall within the Act and are bound by rules made under it. In the case of a building society which was authorised by the Securities and Investments Board, it would, for instance, have to declare whether it was tied to one particular insurance company or whether it was offering independent advice. Even when tied the building society would still be obliged to consider the suitability of the investment for the particular customer.

Conveyancing, of itself, would not appear to include the provision of investment advice and therefore the provision of conveyancing services, whether in-house or through a subsidiary, would not be a matter for the Financial Services Act 1986. It should be noted however that a person who is approached to provide conveyancing services and then offers advice on investments may need to be authorised or exempted under the Act. A subsidiary company specialising in conveyancing which gave investment advice to customers leading them to the parent company could be in breach of the Financial Services Act unless properly authorised. This could also apply to independent solicitors who recommend potential house-buyers to take out a particular endowment policy or who arrange for them to do so.