PREM 19/1100

Future of the Post Office: Finances.

Industrial Relations.

Postal and telecommunication monopolies.

POST AND TELECOMMUNICATIONS.

Part 1: May 1979

Part 6: October 1982.

Referred to	Date	Referred to	Date	Referred to	Date	Referred to	Date
~~1.11.82~~		~~9.2.83~~					
~~9.11.82~~		~~14.2.83~~					
~~17.11.82~~		~~23.83~~					
~~24.11.82~~		~~14.3.83~~					
~~6.12.82~~		~~15.3.83~~					
~~9.12.82~~		~~22.3.83~~					
~~16.12.82~~		25.3.83					
~~22.12.82~~		— Pt Ends —					
~~12.1.83~~							
~~28.1.83~~							
~~4.2.83~~							
~~7.2.83~~							

PREM 19/1100

PART 6 ends:-

~~M/S Industry to M/S Trade 25/3~~

S/S Scottish Office to S/S Industry 29/3

PART 7 begins:-

S/S Industry to S/S Transport 12/4

TO BE RETAINED AS TOP ENCLOSURE

Cabinet / Cabinet Committee Documents

Reference	Date
L(82) 93	11.11.82
L (82) 16th Meeting, Minute 1	16.11.82
E(NI) (82) 33	15.12.82
E(NI) (82) 34	16.12.82
E(NI) (82) 10th Meeting, Minute 2	22.12.82
E(NI) (83) 4	7.2.83
E(NI) (83) 2nd Meeting, Minute 2	9.2.83.

The documents listed above, which were enclosed on this file, have been removed and destroyed. Such documents are the responsibility of the Cabinet Office. When released they are available in the appropriate **CAB** (CABINET OFFICE) CLASSES

Signed C Wayland Date 23 April 2013

PREM Records Team

RECEIVED IN
S.O.S. FOR
INDUSTRYS OFFICE

30 11:01

SCOTTISH OFFICE
WHITEHALL, LONDON SW1A 2AU

The Rt Hon Patrick Jenkin MP
Secretary of State for Industry
Department of Industry
Ashdown House
123 Victoria Street
LONDON
SW1E 6RB

TO Mr Ellison	COPIES TO
FOR ADVICE (AND DRAFT REPLY IF APPROPRIATE)	PS/PUS PS/PK PS/Sec Mr Croft Mr Solomon
PLEASE BY: N 6/4/83	

29 March 1983

Dear Patrick,

Thank you for sending me a copy of your letter of 11 March to David Howell about provisions of the Telecommunications Bill relating to road works. I have now seen David Howell's reply of 21 March.

I think we are all agreed about the need to strike an appropriate balance between the public interest in improving telecommunications, and the public interest in minimising traffic disruption and damage to the roads. We do not in Scotland have any provisions corresponding to section 181 of the Highways Act 1980, so I have no objection to your proposal to remove local authority licensing control over cable installation. I do, however, think it important that local highway authorities should be consulted and should have their views taken into account before you grant a licence to a telecommunication operator which would give him rights to carry out road works in their areas.

I understand that the Convention of Scottish Local Authorities does not particularly mind which Government Department carries out such consultation, so long as it takes place. Under your present proposals, you would consult me before granting a licence affecting Scotland. In addition to considering my own interest as trunk road authority, I would then have to consult the local highway authorities concerned. This would involve my Department in a certain amount of "post office" work.

I can therefore see the attractions in David Howell's proposal, set out in the sixth paragraph of his letter, that the Bill should provide for you to consult the highway authorities concerned. I would still have to be consulted as trunk road authority, but the local authorities could make their views known direct to your Department. Furthermore, while I am sure your undertaking to consult colleagues would be honoured in practice, I can see presentational advantages from the local authorities' point of view in having a statutory right to be consulted.

In conclusion, I think David Howell's suggestion is a useful one and I hope you will agree to table an amendment to the Bill accordingly. I shall, of course, be happy to join in any discussion on this subject.

I am sending copies of this letter to David Howell, Nicholas Edwards and Jim Prior.

Yours ever,

George

CC NO.
Bst letter

DEPARTMENT OF INDUSTRY
ASHDOWN HOUSE
123 VICTORIA STREET
LONDON SW1E 6RB
TELEPHONE DIRECT LINE 01-212
SWITCHBOARD 01-212 7676

6401

FROM THE
MINISTER OF STATE
FOR INDUSTRY AND
INFORMATION TECHNOLOGY
KENNETH BAKER MP

2

Prime Minister

Clause 42 is the clause which was alleged to place the burden of proof for incorrect charging onto the consumer instead of BT. MCS 29/3

Dr Gerard Vaughan MP
Minister for Consumer Affairs
Department of Trade
1 Victoria Street
LONDON SW1E OET

25 March 1983

Dear Gerry,

Thank you for your letter of 15 March about Clause 41 of the Telecommunications Bill (now Clause 42 in the print of 10 March) which continues an arrangement provided in earlier telecommunications legislation but adopts it to the new structure of telecommunications. I have also received letters from Gordon Borrie and from POUNC, both of whom press for Clause 42 to be removed from the Bill.

Because of the strength of feeling on this Clause, I have decided to write to Sir George Jefferson to advise him that I am considering withdrawing the Clause in the House of Lords. This will give him an opportunity to comment before we take action, and I suggest that we should take a final decision on the exclusion of the Clause from the Bill when we see what he has to say.

Meantime, I understand that good progress has been made on the drafting of the new Clause on the approval of metering systems. My officials hope to have a draft to show to yours within the next day or two. I have instructed my officials not to include the connection between Clause 42 and the approval of metering systems so that there need be no complications should we decide to remove Clause 42. I hope that you will agree that the new Clause on metering should be taken at Report on 28 March.

It would certainly be my intention that officials should explore in due course the question of which body should carry out the approvals and the number of staff required. I do not think this need hold up the provision in the Bill of the power to approve metering systems.

I am sending a copy of this letter to the members of E(TP), to John Biffen, Michael Jopling and to Gordon Borrie.

Yours ever
Kenneth

M84/M84ABK

KENNETH BAKER

Post + Telcomms: funding Post Office

Pt 6

Pt 7d

cc NO

JU299

DEPARTMENT OF INDUSTRY
ASHDOWN HOUSE
123 VICTORIA STREET
LONDON SW1E 6RB
TELEPHONE DIRECT LINE 01-212 3301
SWITCHBOARD 01-212 7676

Secretary of State for Industry

22 March 1983

Rt Hon Sir Geoffrey Howe QC MP
Chancellor of the Exchequer
HM Treasury
Whitehall SW1

2

Prime Minister

A further ~~the~~ attempt to explain BT's £568 m undershoot.

MCS 23/3

Dear Geoffrey,

Nat Ind: Policy Pt 7

I was asked by E(NI) on 7 December to circulate a breakdown of BT's undershoot for 1982-83 and to indicate the action proposed to remedy the causes of the undershoot. I have delayed writing until Leon Brittan and I had reached agreement on the BT EFL for 1983-84 since clearly a main piece of remedial action would have indeed to be the setting of a more realistic EFL for the coming year.

Nat Ind: Policy Pt 8

2 I now attach a table which gives the factors BT have advanced in explanation for the shortfall of £568 million which, as E(NI)(83)6 recorded, was thought last month to be the likely size of the undershoot. (It now seems that it may be somewhat larger still.) You will see that some of the factors reflect credit on BT (lower expenditure on accommodation, and certain current cost improvements), some reflect changed circumstances outside BT's control (lower prices, lower demand for investment, delays because of planning problems, lower interest payments, and, in the opposite direction, reduced turnover); and some cause concern about BT's performance and forecasting ability (late delivery of equipment and the shortfall on working capital).

3 There are, I suggest, three pieces of action that must be taken, all of which are in hand.

4 First BT's internal estimating and accounting system must improve. I have had a presentation from BT's consultants on this which gives a measure of reassurance: it is a huge and lengthy task to prise BT out of its civil service past into the commercial world into which we are to launch it, but the task is now being tackled with spirit.

5 Secondly, even though the sum of money involved may have been modest, the story of delays in delivery of equipment needed for modernisation must not continue. I am glad that Sir George

Jefferson took the opportunity of the annual dinner of the manufacturers' trade association last week to take them to task on this subject (although I would not maintain that BT themselves are blameless here). The delays were not to System X equipment. But what really matters in achieving the modernisation of the network is satisfactory progress with System X: Plessey now have the development under control and the first fully digital exchanges will be delivered next year. I am satisfied that there is no more we need to do on this matter.

6 Thirdly, we must ourselves set a financial regime for BT sufficient to place them under pressure to limit costs and such that, if successful in this, BT do not massively undershoot their EFL. I believe that a combination of the EFL of minus £100 million, the financial objective of a real return of 6.5% on net assets and the BT price undertaking (not to increase prices in 1983-84 by more than the average of 3.3% involved in the proposals BT put forward for implementation in November 1982, which have been postponed until at least July) do apply this element of discipline. E(NI) will have the chance of seeing how the position is developing in the context of the BT Corporate Plan in the early summer.

7 I am copying this letter to the Prime Minister and other members of E(NI) and also to Sir Robert Armstrong. I would of course be content for there to be a discussion of it in E(NI) if colleagues wish it.

Yours ever

Patrick

ANNEX 1

BREAKDOWN OF BT FORECAST UNDERSHOOT FOR 1982/3

ITEM	DEVIATION FROM BUDGET (£ million)
Fixed Capital Shortfall	
Reduction in prices	120
Reduction in expenditure on accommodation for training and service centres	70
Late delivery, mainly of exchange equipment	80
Reduced demand due to recession (mainly local line plant)	30
Other (including delays to CTO site and third earth station site because of planning problems)	73
Total Fixed Asset Shortfall	373
Working Capital Shortfall	108
Total Shortfall on Capital Requirements	481
Increase in Internal Resources	
Lower than forecast staff costs	84
Other current account improvements	107
Reduction in interest payments	67
Capital receipts and adjustments	8
offset by reduction in turnover	179
Total increase in internal resources	87
Total forecast undershoot	568

Post & Telecom
future of. Pt 6.

PS022220/83

cc NO

DEPARTMENT OF TRANSPORT
2 MARSHAM STREET LONDON SW1P 3EB

01-212 3434

The Rt Hon Patrick Jenkin MP
Secretary of State for Industry
Department of Industry
Ashdown House
123 Victoria Street
LONDON SW1E 6RB

21 March 1983

Dear Patrick

Thank you for your letter of 11 March about the provisions of the Telecommunications Bill which affect highway authorities and road users. I am grateful that you have given this your personal attention and that we are agreed about the need to strike the right balance between the interests of telecommunications services and those of highway authorities and road users. I remain concerned that insufficient weight is being given to the latter.

Let me first say that I am fully committed to our agreed policy that telecommunications systems need to be developed and without too much restriction. I should like however to set the record straight about what was agreed between us last July. Your letter and the accompanying document about the reform of the Telegraph Acts stated that

i. initially only British Telecom and Hull would be licensed;

ii. other licensees authorised to carry out the installation of apparatus would have conditions attached to their licences;

iii. with regard to local systems, you proposed to do nothing "to alter the existing arrangements under which highway authorities... are able to license the placing of telecommunications lines in streets."

It was on that basis - as well as on the promise of consultation - that I welcomed your proposals.

While I welcome your reassurance about consultations with colleagues, the Bill which is now before the House would give you power to license any number of telecommunications operators and would not require you to attach any condition to the licences. I note that you also say that the removal of British Telecom's powers to license private telecommunications operators to place apparatus in highways represents a "very

considerable improvement" in the safeguards enjoyed by highway authorities. But, of course, that power was originally granted to British Telecom when it was a Government Department; the only extant example of the use of the power is the authorisation of the Hull system 80 years ago and, if British Telecom had in the more recent past sought to license any other operator and grant it the powers of a statutory undertaker, we in this Department would probably have resisted such a move and sought a change in the law.

Another difficulty is that consultation with this Department would not be sufficient to safeguard the interests of local highway authorities. That is because I am the highway authority only for trunk roads: I do not have detailed knowledge of the roads for which local highway authorities are responsible and consultation with me would mean that I would have to seek the views of the highway authorities themselves.

With regard to the amendments I have proposed, my own strong preference would be to retain S.181 of the Highways Act but with a right of appeal. I accept however that our policy as a Government is that local authorities should not be in a position to hinder the development of the telecommunications systems and I accept also the argument that there would be a "bureaucratic muddle" if a person to whom a licence had been granted were required to seek a further consent. Provided therefore that some other safeguard is introduced, I will not argue with your proposal to amend the Bill to remove the S.181 powers from highway authorities when a licensed telecommunications operator has been authorised to use the telecommunications code. (But I should like the substance of the charging provision, S.181(10), to be retained; this might be achieved by amending Clause 9 with regard to the conditions which may be attached to licences.)

I must however maintain my proviso and ask you to agree to my other, less stringent, proposal. That is that the Bill should be amended to require the Secretary of State first, to consult the highway authority concerned before announcing that he proposes to grant a licence to which the Telecommunications Code would apply and secondly, to take account of reasonable objections by the highway authority in considering whether or not to grant a licence. If he decided to proceed with the licence, conditions should be attached to it which took account of reasonable representations by the highway authority. I do not believe that, even though consultation with colleagues is welcome, the consultation processes at present proposed in the Bill go far enough to protect the interest of highway authorities since, by the time they were set in motion, you would have already taken the view that you proposed to grant a licence.

Thank you for copying to me your draft reply to Councillor Sayers. I shall be glad if you will hold it over until we

have reached agreement between ourselves. When you do write, however, I suggest that you should drop the last sentence in the third paragraph - traffic preceded the telegraph and telephone companies!

I trust that you will be willing to amend the Bill in the way that I have proposed in paragraph 6 above. If however you see difficulty about that, let us have an early meeting together with Nicholas Edwards, George Younger and Jim Prior, to whom I am sending copies of this letter.

Yours ever

David

DAVID HOWELL

DEPARTMENT OF TRADE
1 VICTORIA STREET
LONDON SW1H OET

TELEPHONE DIRECT LINE 01 215 —
SWITCHBOARD 01 215 7877

From the
Minister of State
for Consumer Affairs

Mr Kenneth Baker MP
Minister of State for Industry
& Information Technology
Ashdown House
123 Victoria Street
London SW1E 6RB

15th March 1983

Dear Kenneth

TELECOMMUNICATIONS BILL CLAUSE 41

Thank you for your letter of 3 March. I am glad to see that, fundamentally, you share my view on this Clause. Although I understand your difficulties, I nevertheless believe that, on balance, it would be best not to press it.

The point that concerns us both is that, in effect, the consumer as defendant will have to prove that his telephone bill is wrong (in other words, that he is not liable) and, unless he takes special steps, he will have no opportunity to question anybody from the company.

It is clearly against the interests of consumers and against the general policy agreed by Patrick Jenkin and Arthur Cockfield. For example you explain that you need to extend the arrangements to other public telecommunications operators so that BT is not placed in a privileged position compared with its competitors. You see the present arrangements as giving BT an advantage over its customers which would create unfairness with its future competitors if they are not put in the same position. But surely the answer to this problem is to remove the privilege from BT, not extend it to other operators.

I can see that possibly the inadequacies of the systems of BT and other operators could make it difficult for them to rely on a witness providing evidence. But if they are to be Companies Act companies why should they not be faced with that discipline? To argue that excusing them this will save them money seems contrary to our reasons for privatisation. The normal discipline of the commercial world should lead them to put their own house in order.

It is because of these considerations that I see the development of better metering systems as complementary to the removal of Clause 41 rather than as linked to its retention.

On the question of better metering arrangements, are you sure that the monitoring system envisaged would necessarily require the use of Government manpower? Officials have agreed that it is technically feasible to have such a system but have estimated that it would probably need about 30 staff. I am advised that this is possibly an over-estimate. If you do go ahead then I hope you will agree to a study by officials, to consider more fully than has been done so far, which part of the government machine is best fitted to take on the administrative and technical tasks in question.

I am copying to recipients of the previous correspondence.

Yours

GERARD VAUGHAN

Post & Tels,
Future of
the Post Office,
Pt 6

DEPARTMENT OF INDUSTRY
ASHDOWN HOUSE
123 VICTORIA STREET
LONDON SW1E 6RB
TELEPHONE DIRECT LINE 01-212 3301
SWITCHBOARD 01-212 7676

JU220
Secretary of State for Industry

11 March 1983

The Rt Hon David Howell MP
Secretary of State for Transport
Department of Transport
2 Marsham Street
London SW1

PS/Mr Baker
PS/Mr Butcher
Mr Croft
Mr Solomon - T
Mr Macdonald - IT
Dr Thynne - IT
Dr Dobbie - T
Mr Ellison - T
ON FILE

Dear David,

Thank you for your letter of 1 March about the provisions in the Telecommunications Bill authorising licensed telecommunication operators to install their apparatus in highways. I am sorry that you and Lynda Chalker have not had replies to your earlier letters on the subject; the issues raised are complicated and those concerned have been pre-occupied with the progress of the Bill in Committee.

2 I entirely agree with you that we need to strike the right balance between the development of telecommunications and a free flow of traffic and the integrity of road surfaces. We did of course discuss this issue in some detail last summer and my letter to Willie Whitelaw of 16 July drew special attention to the problem created by people digging up road surfaces. I went on to stress that it was necessary for me to have the powers which BT has long possessed to authorise operators to place telecommunication lines but I undertook to consult my colleagues before using my licensing powers to avoid a proliferation of people digging up the highway. I also proposed new arrangements for imposing conditions on those who were authorised to do so. Your letter of 26 July positively welcomed both my general proposals and the reassurances I gave for protecting traffic flow.

3 We returned to the issue in Cabinet on 2 December when we considered and endorsed E(TP)'s conclusions on cable policy. (E(TP) had agreed that the General Development Order should be amended to include the laying and maintenance of cable systems as "permitted development" on the grounds that local authorities should not be able to impede cable development by use of existing planning etc powers. E(TP) also agreed that environmental safeguards should be included in licences or in the amendments to the GDO and not be left to local authorities.

4 These decisions clearly mean that as a Government we have decided to take control ourselves of the licensing of cable systems and that local authorities should not retain any licensing function or other power to hinder the installation of cables and other apparatus, whether by the exercise of planning control or by the withholding of permission to install apparatus. We cannot therefore meet the local authorities' main proposal that the installation of cable systems in or over maintainable highways should be the subject of local authorities licensing control under section 181 of the Highways Act. This suggestion has also been put forward by your own officials. This decision will be unwelcome to the associations and we must take care with the presentation of the issues.

5 In practice the local authorities' case is based on a misunderstanding of the existing law; they do not appear to realise that under the Telegraph Acts British Telecommunications has powers to licence private telecommunication operators to place apparatus in highways and that there could be a proliferation of people authorised to dig up highways under the existing law. Seen in this light the Bill represents a very considerable improvement in the safeguards enjoyed by highway authorities. First, the power to licence operators to install apparatus in highways is removed from BT and is transferred to the Secretary of State who is of course responsible to Parliament. Second, when an operator is licensed to use the provisions of the new Telecommunications Code to install apparatus in highways etc, this can be done subject to exceptions and conditions which, as I said in my letter of 16 July, can be designed to minimise any interference with road traffic and surfaces. This is an entirely new arrangement. Third, special safeguards are built in to the arrangements for modifying licence conditions under Clauses 10 and 13 of the Bill so that the Secretary of State can prevent modifications which he thinks undesirable on environmental or transport grounds. Fourth, before the provisions of the Code are applied to anyone so that they have powers to install apparatus in highways, public notice must be given of the intention and the Secretary of State is formally obliged to consider representations and objections. This arrangement gives the highway authorities an ample opportunity to raise objections and I would not propose to adopt your officials' ideas about a two stage public consultation procedure with highway authorities being consulted before the other interested parties.

6 These are significant safeguards on the face of the Bill. There is moreover the additional safeguard which you and I agreed on last summer that I would not exercise my powers to licence operators to dig up roads without consulting colleagues. This assurance should be particularly welcome to the local authority associations since your special status as a highway authority in your own right means that you will take account of their highways interests as well as your own when we discuss the granting of a

particular licence. I gather, however, that your officials are unhappy about an assurance and fear that it may be disregarded in time. I cannot recall an assurance like this being disregarded.

7 Finally, there is a technical problem in the drafting of the Bill. Under the Telegraph Acts the consent of the highway authority is required before apparatus is placed overhead in a highway but not when it is placed underground. Our Cabinet decisions mean that there should be no provision for local authorities to give any consent, whether the apparatus is placed overhead or underground. Unfortunately, Schedule 4 of the Bill as drafted includes provisions which require BT and other operators to whom the Telecommunications Code is applied to obtain highway authority licences before installing both overhead and underground apparatus. I shall need to make two small amendments to Schedule 4 at the Report Stage to rectify this mistake. The Associations know of the problem.

8 Against this background I think there is no reason to depart from our previously agreed policy line. I would propose to write ... to the local authority associations on the lines of the enclosed draft letter.

9 I am copying this to Nicholas Edwards, George Younger and Jim Prior.

Yours ever

Patrick

JW221

DRAFT LETTER TO SEND TO:

A L Sayers Esq
Chairman
Planning & Transportation Committee
Association of County Councils
Eaton House
66A Eaton Square
London SW1

TELECOMMUNICATIONS BILL

I am sorry that it has taken me some time to send you a full reply to your letter received here on 14 December about your Association's concern about the arrangements for authorising licensed telecommunications operators to install their apparatus in highways. The issues you raise are important and I have given them very careful consideration.

I share your fundamental concern. The new arrangements for telecommunications, including the arrangements for cable, must pay proper regard to the interests of highway authorities and users of the highway. There should be no unnecessary proliferation of people authorised to break open the surface of highways and those who are authorised to do so should be obliged to meet the reasonable costs of reinstatement. I am also concerned to avoid unnecessary interference to the free flow of traffic. All this is I think common ground between us.

I also hope that we share common ground about the vital importance of telecommunications not only to commerce and industry but also for social and domestic purposes. Local authorities, for example, have an interest in efficient tele communications for the emergency services. An improved range and quality of telecommunication services is expected over time to reduce the need for much business travel and so could reduce both the cost of road maintenance and the amount of traffic congestion. Moreover, we need to bear in mind that private telegraph and telephone companies had rights to install their apparatus in highways well before motor vehicles were invented.

Some conflict between the interests of highway authorities and those who use and rely on telecommunications is I fear unavoidable. I have been anxious to strike a proper balance between the two sets of interests.

The first thing to say is that your letter may imply that many organisations are likely to be authorised to break open highway surfaces. This is not the case. There have of course been powers for operators to be authorised to break open street surfaces for many years but these powers have been used sparingly. Under the new telecommunications regime I expect little change. BT will of course need to be authorised subject to conditions to carry on installing its apparatus in highways and so will the City of Kingston upon Hull in its licensed area of operations. Apart from these two operators we have recently licensed the Mercury consortium to run a telecommunications network in competition with BT and I have it in contemplation to apply the provisions of the new Telecommunications Code to Mercury. No final decision has been taken on this and the public consultation procedures which I describe below will be followed. We have, as you know, announced that we do not intend to licence a further telecommunications network for the foreseeable future and Mercury itself is planning to use cellular radio in its local distribution network which will substantially reduce the need to install local cables or to dig up road surfaces. There is also the question of local broadband cable systems where we are currently working out our proposals and where fresh legislation will be required. I can therefore assure you that your members will not be confronted with a sudden large proliferation of companies authorised to dig up roads.

Apart from this the Bill itself contains a number of safeguards and since these are not widely understood it might be helpful if I explained them.

First, the present arrangements under which operators can be licensed by British Telecommunications to install apparatus in highways are clearly inappropriate; there is no provision for Parliamentary control and the interests of highway authorities can be completely disregarded. The Bill changes the position by removing BT's licensing powers and ensuring that only the Secretary of State can apply the provisions of the new Telecommunications Code to an operator. The Secretary of State will be answerable to Parliament and the arrangements for authorising any operator to dig up streets will be brought under proper public scrutiny and control.

Second, Clause 9 of the Bill introduces entirely new arrangements to place conditions and exceptions on the way that telecommunication operators exercise their rights under the Code. This provision has been included so that the Government can have

a flexible and effective power to protect environmental and other interests and in particular to minimise interference with road traffic and surfaces. I hope your Association will be able to offer us advice on these conditions and I return to this point later in this letter.

Third, telecommunication operators will be under the direct oversight of the new Director General of Telecommunications, who will have duties to monitor observance of licence conditions and to consider complaints. He will have a power to order licensees to honour licence conditions in any cases where they may breach them and these order-making powers have much the same effect as court injunctions. Breach of an order can lead to fines or even imprisonment. The position will be that highway authorities will be able to draw problems to the Director General's attention and he will be able to take corrective action when this is appropriate.

Fourth, special arrangements are built into the arrangements for modifying licence conditions to ensure that the Secretary of State can intervene to prevent modifications which he thinks undesirable on environmental or other transport grounds. The Secretary of State could use these powers to protect the interests of highway authorities.

Fifth, because of the concern we know that highway authorities and others feel about the possible impact of our authorising an operator to exercise the Telecommunications Code powers to dig up streets, we have made it a requirement that once the Bill is fully in force there must be a formal procedure involving public notice and a consideration of objections before such an authorisation can be given under Clause 9. This will give your Association and individual authorities an opportunity both to make objections to an authorisation and to suggest the inclusion of conditions in the licence to be issued to the operator concerned. The Bill requires the Secretary of State to consider such representations, thus ensuring that consultation is genuine and not a formality.

Finally, my colleague David Howell is as you say a highway authority in his own right and shares your concern. I have given him an assurance that no licence authorising use of the Telecommunications Code powers will be granted except after collective discussion among Ministers. This will ensure that the interests of highway authorities will not be overlooked.

These safeguards are in addition to the well established arrangements under the Public Utilities Street Works Act which enable highway authorities to take disputes about the installation of plant to arbitration.

Turning to the specific proposals in your letter, you are correct to say that in the Bill as printed sections 178 to 181 have been mistakenly applied so that telecommunication operators are subject not only to licensing by the Secretary of State but also to local licensing. This arrangement was not intended and it would be a bureaucratic muddle to have two conflicting licensing jurisdictions for the same activity. It is our firm intention to protect the interests of highway authorities by the inclusion of conditions in any licence issued by the Secretary of State. The Bill will need to be amended on this point.

We are, however, preparing amendments to the Bill to place beyond doubt our ability to require licensed operators to provide bonds so that members of the public and highway authorities are protected against damage cuased by an operator if the operator goes into liquidation or loses his licence.

Finally, we have included in the Bill a power to attach conditions to limit the use an operator can make of the provisions of the Telecommunications Code and we would want to use this power in a way which helped allay your concerns. The first licence to apply the provisions of the Code will be that granted to British Telecommunications later this year and we are turning our minds to the precise terms of the licence conditions. Could I invite you and your members to let me have, by the end of May, your detailed suggestions on the points, for example about reinstatement of surfaces, which you would wish to see covered in the BT licence.

I am writing in similar terms to the other local authority associations.

DEPARTMENT OF TRADE 1 VICTORIA STREET LONDON SW1H 0ET Telephone 01-215 7877

Post Tels
cc JV

NBPM

From the Secretary of State

MS 14/3

Jonathan Spencer Esq
Private Secretary to the
Secretary of State for Industry
Department of Industry
Ashdown House
123 Victoria Street
London, SW1E 6RB

11 March 1983

Dear Jonathan,

TELECOMMUNICATIONS BILL

My Secretary of State ~~has~~ will request if required now been able to consider the two papers dated 21 February which officials of our two Departments prepared. These followed my Secretary of State's letters to yours of 11 November and 3 December, and which your Secretary of State will also have seen.

So far as the functions of the two Directors General are concerned, my Secretary of State would be ready to agree to the form of concurrent jurisdiction set out in paragraph 11(b) of the relevant paper. Under this system of concurrent jurisdiction each Director General would be competent to exercise functions in relation to commercial activities connected with telecommunications, but only in consultation with the other. As to the stages at which consultation procedures would apply, it would probably be best if they were to apply only at the initial stage of a particular case. The two Directors would then consult one another before either of them first acted under Part IV of the Fair Trading Act or under the Competition Act in relation to a particular case.

You will remember that last year's correspondence between our two Secretaries of State also dealt with the separate issue of reports of the Monopolies and Mergers Commission on licence variation references. My Secretary of State will be writing to yours on this subject on his return.

I am copying this letter to the Private Secretaries to the Prime Minister, the Home Secretary, the Chancellor of the Exchequer, the Secretaries of State for Scotland, Northern Ireland and Wales, the Minister of Agriculture, Fisheries and Food, the Secretary of State for the Environment, the Chancellor of the Duchy of Lancaster, the Lord Privy Seal, the Chief Secretary, and the Chief Whip and to Sir Robert Armstrong and Mr Sparrow.

Yours sincerely,

JOHN RHODES
Private Secretary

Post & Tels
Future of the
Post Office, p46

cc JV

DEPARTMENT OF INDUSTRY
ASHDOWN HOUSE
123 VICTORIA STREET
LONDON SW1E 6RB
TELEPHONE DIRECT LINE 01-212
SWITCHBOARD 01-212 7676

6401

FROM THE
MINISTER OF STATE
FOR INDUSTRY AND
INFORMATION TECHNOLOGY
KENNETH BAKER MP

Dr Gerard Vaughan MP
Minister of State for Consumer
Affairs
Department of Trade
1 Victoria Street
LONDON SW1

3 March 1983

Dear Minister,

TELECOMMUNICATIONS BILL: CLAUSE 41 AND METERING

Thank you for your letter of 28 February about the linked issues of metering automatic use of telecommunication services and the procedures to be used in Court to prove that sums are due to public telecommunication operators for the services they have provided. Your letter arrived when I was on the point of writing to you about my detailed proposals on metering.

The working group of officials, which was established following my letter to you of 25 September last year, has confirmed that suitable arrangements can be made for approving the design and subsequent operation of the metering systems used by public telecommunication operators. Satisfactory arrangements can also be made to monitor and secure compliance with these arrangements. All these arrangements will be under the control of Ministers or the Director General of Telecommunications and thus quite independent of British Telecommunications and other operators. Matters have progressed so well that instructions for Parliamentary Counsel are now being prepared and I expect us to be able to introduce amendments to the Bill shortly.

Further work needs to be done, however, on the details of the arrangements and on the resources to be devoted to establishing and monitoring the metering arrangements. This will take some time to complete and proper metering arrangements cannot be brought into force until well after the Bill as a whole comes into effect.

The absence, at least in the short term, of independently verified telephone metering systems means that we have to continue for the time being with the long established arrangements set out in Clause 41 of the Bill. These as you say make it easier for the telephone operator to establish that sums

M81/M81AAH

are due to him than is the case with other services.

Clause 41 continues to place the burden of proof on the plaintiff rather than the defendant, ie the subscriber, but this has been the case under previous legislation, and does not appear to have been a source of complaint, nor is there evidence of this working to the disadvantage of subscribers in the past. But some such arrangement is necessary both because of the nature of telecommunication services and because of the existing arrangements for metering. Unlike gas and electricity, where there is a homogeneous supply of measurable quantities, in a single direction, telecommunication charges depend on the person who initiates a call, when in the day the call is originated the destination to which the call is addressed, whether the call is answered by the subscriber to whom it is addressed and the duration of the call. An indication of the problems of measuring telephone services can be seen in the fact that, until recently, people who fraudulently used telecommunication systems could only be prosecuted for stealing electricity, although this of course represented only a fraction of the value of the service provided. Telephone meters are fundamentally different from other meters and the approval arrangements which our officials have discussed concern the approval of systems as a whole rather than simply the approval of an individual dial-type meter.

Telephone metering arrangements also cause their own problems. Apart from the fact that it measures a complex service, a customer's meter is not activated when the customer lifts his own telephone; instead it is activated remotely when the telephone to which the call is addressed is lifted by a different customer. This means that meters must be located in the exchange where individual customers do not have access. In consequence customers have no objective way to check their actual consumption of telecommunication services and some arrangement where the operator informs the court about the meter reading is inevitable. The alternative to a certificate would be the attendance of witnesses in Court but, since they would merely say the same as was stated on the certificate, there would be no additional protection to the individual consumer but significant additional cost to the operator and hence to the generality of consumers.

In these circumstances the arrangements in Clause 41 are not a "privilege" as you suggest but a matter of practicability. Clause 41 applies equally to all public telecommunication operators and BT is not placed in any privileged position compared with its competitors. The arrangements are quite separate from the "exclusive privilege" of running telecommunications systems which BT currently enjoys by virtue of section 12 of the British Telecommunications Act and which Patrick Jenkin mentioned in his E(TP) paper last June. We are of course abolishing the statutory "exclusive privilege" under Clause 2 of the Bill.

Fundamentally, however, I share your distaste for Clause 41 as it stands and would like as soon as this is practicable to enhance consumer protection by qualifying the operators' ability to produce certificates in Court. I propose that we link the arrangements in Clause 41 to the approval of metering systems; once metering arrangements have been approved Clause 41 would only apply where both the operator conformed with the standards set by the Director and the Director's monitoring showed that this was indeed the case. If an operator's system failed to meet the standards, he could not rely on a certificate in Court. This arrangement could not, however, commence for several years.

I hope you can agree both to the metering arrangements agreed by officials and to my proposed amendment of Clause 41.

We also need to press ahead with the administrative and technical arrangements for metering and to decide in particular who should carry out the approval and subsequent monitoring. In view of your concern about consumer protection and metering generally, it seems to me that this task should be carried out by the staff of the National Weights and Measures Laboratory who could be appointed as a sub-contractors by the Director General of Telecommunications. Their experience in similar tasks would be of great benefit to the success of the project and would reassure consumers. The operators would of course meet the costs of approvals, monitoring etc but the staff members would I think need to count against the Department of Trade's manpower total. It is, however, too early to make a detailed estimate of the staff resources involved.

I am sending a copy of this letter to the recipients of yours.

Yours sincerely

Neil McPherson

for KENNETH BAKER

approved by the Minister, and signed in his absence.

M12/M12AES

Post & Tels
Future of the
Post Office, pt6

DEPARTMENT OF INDUSTRY
ASHDOWN HOUSE
123 VICTORIA STREET
LONDON SW1E 6RB
TELEPHONE DIRECT LINE 01-212
SWITCHBOARD 01-212 7676

6401

FROM THE
MINISTER OF STATE
FOR INDUSTRY AND
INFORMATION TECHNOLOGY

KENNETH BAKER'S OFFICE

Michael Scholar Esq
10 Downing Street
WHITEHALL SW1

(2)

Prime Minister

Not as bad as first it appeared to be.

MCS 3/3

3 March 1983

Dear Michael

Thank you for your letter of 2 March, following up our conversation last night on Clause 41 of the Telecommunications Bill.

You will by now have seen Mr Baker's reply to Dr Vaughan's letter of 28 February. As stated there, Clause 41 continues to place the burden of proof on the subscriber, but this does not change the position as it now stands under existing legislation, which has not been the cause of any complaint from customers, and there is no evidence that it has worked to the disadvantage of the consumer. Some arrangements on the lines of Clause 41 are necessary because the metering of telephone use presents problems which do not exist in the case of gas or electricity metering. Telephone meters are not on customers' premises, where they can be read by the subscriber. Some form of certification procedure is needed to demonstrate that meters have actually recorded the number of call units for which the customer has been charged.

If a customer complains that his telephone bill is excessive, the Bill introduces a number of new safeguards. First there will be an entirely new, and independent arrangement for verifying that telephone metering systems are accurate and that they are operated fairly from the customer's point of view. These arrangements do not exist at present and will take a little time to introduce. We will be introducing amendments to Clause 41 shortly to cover this.

If a customer thinks his bill is excessive, he will be able to complain to the Director General of Telecommunications, who will have new powers not only to investigate complaints but also to order the telephone company to take corrective action. There will also be a code of practice, similar to the one which exists

M81/M81AAJ

at present, under which anyone who complains that a telephone bill is excessive will be able to have his complaint examined in detail and if necessary submitted to independent arbitration without the expense of having to take legal action.

The procedures in Clause 41 will only apply where someone has failed to pay a telephone bill which is properly submitted and seeks payment for telephone calls actually made. Without Clause 41 it would be very much more difficult for any telecommunications operator to obtain a court judgement against a customer who defaulted on payment, and the extra cost of producing witnesses, who would in any case be unable to add much to the evidence represented by the certificate of use, would add to the cost of the telephone service and increase the bills of those who paid on time.

I attach for information a copy of Clause 41 as drafted at present.

I am copying this letter to recipients of yours.

Yours sincerely

Neil McMillan

N M McMILLAN
PRIVATE SECRETARY

M12/M12AES

Post & Tels. Future, pt6

PART II

Documentary evidence as to sums due for services.

41.—(1) A certificate of a public telecommunications operator that a specified sum is due to him from a specified person under an agreement with respect to telecommunication services provided by the operator shall (subject to any term of the agreement to the contrary), in any proceedings instituted by the operator against that person or his personal representatives or against the operator by that person or his personal representatives, be evidence (and, in Scotland, sufficient evidence) of that fact.

(2) In any proceedings instituted by or against a public telecommunications operator to which the rate at which a charge was levied at any time, in respect of a service, by a person outside the United Kingdom is material, a certificate of the operator that the charge was levied at that rate at that time in respect of that service by that person shall be evidence (and, in Scotland, sufficient evidence) of that fact.

Power of local authorities to contribute towards provision of facilities.

42.—(1) Where a local authority consider that it would be for the benefit of the whole or any part of their area that—

(*a*) any additional telecommunication facilities should be provided; or

(*b*) any existing telecommunication facilities should continue to be provided,

by a public telecommunications operator, whether within or outside the area to be benefited, the authority may undertake to pay to that operator any loss he may sustain by reason of the provision or continued provision of those facilities.

(2) In the application of this section to Scotland, nothing in subsection (1) above shall authorise the giving of an undertaking as respects the provision or continued provision of facilities outside the area to be benefited.

(3) In this section " local authority "—

(*a*) in relation to England and Wales, means a county council, the Greater London Council, a district council, a London borough council, the Common Council of the City of London, a parish council or a community council;

(*b*) in relation to Scotland, means a regional, islands or district council;

(*c*) in relation to Northern Ireland, means a district council.

Interpretation of Part II.

1973 c. 41.

43. In this Part—

" the 1973 Act " means the Fair Trading Act 1973;

" modifications " includes additions, alterations and omissions, and cognate expressions shall be construed accordingly;

CONFIDENTIAL

FILE HL

POST AND TELECOMS,

10 DOWNING STREET

From the Private Secretary

2 March 1983

Dear Neil,

Telecommunications Bill: Clause 41

The Minister of State for Consumer Affairs sent the Prime Minister a copy of his letter to your Minister of 28 February about Clause 41 of the Telecommunications Bill.

As I mentioned to you on the telephone earlier today, the Prime Minister would be grateful for clear advice as to whether Clause 41 of the Bill alters the law, shifting the burden of proof from the plaintiff to the defendant in cases which come before the courts when a customer refuses to pay his telephone bill on the grounds that it is excessive.

BF 10/3/83

The Prime Minister has commented that if this is the case, she is opposed to this Clause.

I am sending copies of this letter to the Private Secretaries to the other members of E(TP), to David Heyhoe (Lord President's Office), Murdo Maclean (Chief Whip's Office) and Richard Hatfield (Cabinet Office).

Yours sincerely,

Michael Scholar

Neil McMillan, Esq.,
Department of Industry.

CONFIDENTIAL

DEPARTMENT OF TRANSPORT
2 MARSHAM STREET LONDON SW1P 3EB

01-212 3434

The Rt Hon Patrick Jenkin MP
Secretary of State for Industry
Department of Industry
Ashdown House
123 Victoria Street
LONDON SW1E 6RB

RECEIVED IN
S.O.S. FOR
INDUSTRY'S OFFICE

1983 ☐ 2 13:38

1 March 1983

Dear Patrick

As I think you know, and as I mentioned in Cabinet, I am concerned at the wide powers which the telecommunications Bill would provide for licensed telecommunications operators to install their apparatus in highways and to inspect and repair it. I wrote to Kenneth Baker in December supporting the proposals of Councillor Sayers of the Association of County Councils for the amendment of the Bill to protect highway authorities by retaining Section 181 of the Highways Act 1980. Since then I know that Lynda Chalker has taken up the issue more than once with Kenneth Baker but she has had no reply. Neither has Councillor Sayers who has written again to Kenneth Baker and copied his letter to me.

Now that the Bill is making rapid progress in Committee, I am concerned at this lack of response. May I ask you to look at this yourself and let me know your views? I am sure you will agree that we need to strike the right balance between the development of telecommunications and the preservation of our highways. My view is that this is not achieved in the Bill as at present drafted.

Yours ever

David

DAVID HOWELL

TO Mr Ellison	COPIES TO
FOR ADVICE (AND DRAFT REPLY IF APPROPRIATE)	Mr Baker Mr Butler SoC Mr Croft
PLEASE BY: Noon	Mr Solomon
7/3	

Post + Telecom
Future
PA7.

cc RTA. CESU

DEPARTMENT OF TRADE
1 VICTORIA STREET
LONDON SW1H 0ET

TELEPHONE DIRECT LINE 01 215 5662
SWITCHBOARD 01 215 7877

From the
Minister of State
for Consumer Affairs

(2)

Prime Minister

This is a very poor letter. But, if true, it reveals an unacceptable position.

I will pursue with Mr Baker's office.

MCS 1/3

telephoned Mr Baker's office + Mr Jenkin's 2/3/83 MCS

Yes - urgently please

Mr Kenneth Baker MP
Minister of State for Industry
& Information Technology
Ashdown House
123 Victoria Street
London SW1E 6RB

28 February 1983

Dear Minister

TELECOMMUNICATIONS BILL: CLAUSE 41

I am writing to draw your attention to the effects of this Clause which will now be reached on Tuesday or Thursday.

The Clause would not only continue an existing privilege which BT have over their customers but extend it to all public telecommunications operators. I am advised that it alters the basic common law situation and shifts the burden of proof from the plaintiff to the defendant (the customer) in cases which come before the courts when a customer refuses to pay his telephone bill on the grounds that it is excessive.

At E(TP) on 30 June last year Patrick Jenkin, describing the shape of the Bill stressed that, as a Companies Act company, BT should cease to enjoy its present statutory privileges. The Sub-Committee agreed he should prepare an appropriate Bill in consultation as necessary with other Ministers. In an exchange of correspondence last November Patrick Jenkin (1 November) and Arthur Cockfield (11 November) agreed that the Billshould end the privileges which BT currently enjoys in its dealings with subscribers and that the rights of BT's customers must be secured.

This Clause - particularly Subsection (1) - appears to go against the general line agreed. The relevant Note says that the Clause is necessary because it is difficult for a telecommunications operator to demonstrate that his systems are secure enough to prevent errors and because, as a consequence, it would be sotly for him to present a satisfactory case in court. This line of argument is not particularly convincing.

Solely?

Following your letter of 28 September to me, our respective officials are jointly exploring whether it will be feasible to introduce a scheme to supervise and control the design, operation and maintenance of telephone metering systems. With or without Clause 41, this

would be a useful step to take. Whatever the outcome on those discussions, however, those proposals do not remove the objection in principle to Company Act telecommunciations operators having this statutory privilege over their customers.

Looking at the pattern of complaints from consumers I must admit that this does not seem to be known to many nor does it seem to influence decisions on whether to let disputes go to court. However we felt you would want to consider the point at least. If you do agree you could let the Clause fall when it is reached.

I am copying to the Prime Minister and to other members of E(TP), to John Biffen and to Michael Jopling.

Yours sincerely

Peter Walker

for Gerard Vaughan
(Approved by the Minister
and signed in his absence)

Future of PO: Post & Telecom Pt 6

Post & tel

HL

14 February 1983

Post Office prices

The Prime Minister commented "very good news" on your Minister's minute of 11 February, recording the reduced price increases which the Post Office is planning to go ahead with.

MICHAEL SCHOLAR

Neil McMillan, Esq.,
Department of Industry.

010

VCCJV

Prime Minister (2)

MCS 11/2

Very good news.

MT

RESTRICTED

PRIME MINISTER

POST OFFICE PRICES

On Wednesday I saw Ron Dearing, Chairman of the Post Office about postal profits and postal tariffs. In the last financial year, the Post Office made a profit of £92m and he told me that in the present financial year, it is likely to exceed £120m and it will be announced in July. This is of course good news and it reflects great credit upon his management which has been directed to reducing costs and particularly the massive number of hours overtime.

However I pointed out to him that there is considerable difficulty in justifying price increases to the public against a background of such large profits. Two months ago he proposed that the first class stamp should increase by 1p from 15½p to 16½p from 1 April and currently POUNC is looking at this. I suggested that he should look at this again carefully. He told us today that he proposes only to proceed with an increase of ½p from 1 April which will raise the first class stamp to 16p while the second class remains at 12½p. This will be announced on Monday 14 February.

I think this will be very welcome news and it should be presented as a contribution which the public sector can make to holding back costs borne by industry and the consumer, and to help our fight against inflation. The Union of Communications Workers is unlikely to welcome this as they will see it as reducing their scope for negotiation in the wage round which is about to start.

I am copying this to members of E(NI) and Sir Robert Armstrong.

K.B.

KENNETH BAKER

M77/M77AAZ

11.2.83

for E(NI) folder

CONFIDENTIAL

Prime Minister

MCS 8/2

PRIME MINISTER

BRITISH TELECOM RACAL AND INTERNATIONAL AERADIO LIMITED

The proposal that a joint BT/Racal bid for 100% of IAL be approved, should depend critically upon the issue of control. The suggested arrangement of a fifty-fifty split between BT and Racal raises many questions. In principle, neither would have control. But since Racal was quite willing to go ahead without control yet up to, say, 49% participation, is itself an interesting observation on how both Racal and BT construe their interests. Indeed it looks very much as though, from Sir George Jefferson's letter of 28 January, as though Racal is in it mainly for the protection of BT as "big brother" not merely in overseas markets but also in domestic developments.

But whether or not these suspicions are justified, I can see no argument against John Sparrow's point that one company should have control. With fifty-fifty arrangements there are likely to be many doubts about the question of who is the ultimate arbiter of the policy of IAL. Certainly before BT is completely privatised, it would be a mistake to put control in the hands of BT and allow them to build up on their existing advantages. Therefore I think it is right that Racal should have the controlling interest. If subsequent to privatisation of BT, they feel that it is in their market interest to acquire a controlling share of IAL, then so be it. It's up to them. Their shareholders will pay the price for any mistake then involved.

At present I cannot see why a minority interest by BT would inhibit the sort of joint ventures in overseas markets which Sir George Jefferson outlined in his letter. If there is a mutuality of interests and a dovetailing of expertise, then it clearly cannot be a critical matter to have a fifty-fifty ownership basis. Indeed most joint operations, so far as I am aware, do not have any such equal split.

I conclude, therefore, that in additon to conditions (ii) and (iii) suggested by the Chief Secretary, you also insist on the controlling interest being taken by Racal. Until BT is effectively privatised, the control should not be allowed to pass into the hands of BT.

AW

8 February 1983

ALAN WALTERS

CONFIDENTIAL

P.0959

PRIME MINISTER

Possible British Telecom Involvement in Purchase of International Aeradio Ltd: E(NI)(83)4

BACKGROUND

The Ministerial Sub-Committee on Nationalised Industries (E(NI)) considered the corporate plan of British Telecom (BT) in July 1982. It was told that BT might wish to acquire International Aeradio Limited (IAL), a subsidiary of British Airways (BA) which operates mainly overseas, providing (among other things) airport communications systems. BA is divesting itself of IAL as part of the privatisation programme.

2. While not reaching a final decision, E(NI) took a hostile attitude to the possibility, on the grounds that IAL's main activities were not closely linked with BT's; and that acquisition would represent an undesirable extension of BT's activities. The Sub-Committee's view was that there was a 'very strong presumption' against agreeing to acquisition, which could be removed only by 'new and persuasive arguments' (E(NI)(82)6th Meeting, Item 1).

FLAG A

FLAG B

3. The Secretary of State for Industry wrote to the Secretary of State for Trade on 6 January forwarding a letter from Sir George Jefferson, the Chairman of BT, asking that BT should be allowed to bid for IAL, now that BT was to be privatised. Sir George said that BT would aim at a 51 per cent holding, with the balance either widely spread or perhaps in the hands of a number of minority industrial partners. The Secretary of State for Trade opposed the request on the grounds that it would make the eventual privatisation of BT more difficult because it would entail a higher purchase price; that it would divert the attention of BT's management; and that it was absurd that BA should be required to divest itself of IAL in the interests of privatisation only to find IAL bought by another nationalised industry (even though intended for privatisation).

FLAG C /

4. The Secretary of State for Industry wrote again on 1 February, putting forward a revised proposal from BT, under which they would buy IAL in a joint

venture with Racal (which manufactures radio and data communication
FLAG D / equipment). Mr Sparrow's letter of 3 February suggests that the proposal is an improvement on the previous version; but that it is important to ensure that Racal has control of the joint venture. The Chief Secretary,
FLAG E / Treasury (letter of 4 February) also supports the proposal, subject to a rather less stringent condition concerning control of the joint venture, and provided that the management of IAL supports the move and that BT's monopoly in other fields is significantly reduced. The Secretary of State
FLAG F / for Trade's letter of 4 February, however, maintains his previous objections.

FLAG G 5. In his memorandum E(NI)(83)4 the Secretary of State for Industry suggests that the conditions laid down by the Chief Secretary either have been or will be met; but he rejects Mr Sparrow's suggestion that Racal should have control of the joint venture.

MAIN ISSUES

6. The issues before the Sub-Committee are as follows.

(i) Should BT be permitted to bid for IAL at all?

(ii) If so, what conditions should be attached to this permission?

Should BT be permitted to bid?

7. The arguments on either side are set out clearly in the correspondence. In favour of a bid:

(a) there is said to be industrial logic in linking BT with IAL, since IAL has overseas experience, which BT have not, while BT has technical expertise and 'clout';

(b) more precisely, 'clout' presumably means that a good many potential customers of IAL welcome the involvement of public untilities in the contracts they wish to let (they may indeed also want a Government or public sector stake - this is an argument which has been advanced with some force in the context of Cable and Wireless Ltd);

(c) It would demonstrate to BT's staff that privatisation can bring new opportunities.

8. On the other side:

(d) it would divert BT's management efforts;

(e) for this reason and others it might make privatising BT more difficult;

(f) it would be odd if an exercise intended to reduce the size of the public sector led to IAL's being transferred from one nationalised industry to another (or from one candidate for privatisation to another);

(g) to the extent that the arguments about 'clout' depend on BT's being a public sector body (or at least having a Government stake) they go against the aims of privatisation.

Conditions

9. It seems likely that if the Sub-Committee are willing to accept that BT should be allowed to bid for IAL at all, they will insist that it should be on conditions such as those suggested by Mr Sparrow and the Chief Secretary. They may also wish to explore whether it would be possible to strengthen the involvement of Racal, for example by insisting that the bid should be submitted by Racal as leader (though naturally with BT's support) and that Racal should have control at all stages.

HANDLING

10. You will wish to ask the Secretary of State for Industry to open the discussion. The Secretary of State for Trade, the Chief Secretary, Treasury and Mr Sparrow could then be asked to develop the points that they have made in the correspondence. Any of the other members of the Sub-Committee may wish to contribute.

CONCLUSIONS

11. You will wish the Sub-Committee to decide whether BT should be allowed to make a bid with Racal for IAL; and if so, on what conditions.

PLG

P L GREGSON
Cabinet Office.
8 February 1983

CONFIDENTIAL

cc JV

Prime Minister (2)

MIS 8/2

Treasury Chambers, Parliament Street, SW1P 3AG

Dr J P Spencer
Principal Private Secretary to
Secretary of State
Department of Industry
Ashdown House
123 Victoria Street
London SW1E 6RB

7 February 1983

Dear John.

TELECOMMUNICATIONS BILL: LITTLECHILD REPORT

Because of the urgency I telephoned through to you on Friday evening our comments on the draft statement on the Littlechild Report attached to your Secretary of State's minute to the Prime Minister of 3 February. This is to record the upshot of further discussions over the weekend between Mr Jenkin and the Chief Secretary which culminated in my agreeing an addition to paragraph 3 this morning with Mr Baker's office.

As a result of these discussions we agreed the following three amendments:-

(i) paragraph 2: after the second sentence add a new sentence as follows, "But expansion and growth must be based on a fairly earned return and not on monopoly profits".

(ii) paragraph 3: after the fourth sentence add a new sentence as follows, "It will be important for the precise formula to be soundly based and fair both to the consumer and BT and I intend to commission further work on this".

(iii) paragraph 8: end first sentence at the word "operators" deleting the subsequent words: "but I recognise that this could have considerable implications for BT's revenue".

The Chief Secretary was grateful for Mr Jenkin's acceptance of these changes, and for the further reference to improvement in BT's efficiency which I understand has been separately worked into the final sentence of paragraph 3. DOI and Treasury officials will now consult urgently on the two specific suggestions which, in the time available, Mr Jenkin was reluctant to include in the statement without further opportunity for consideration. These are, first, the proposal that the Monopolies Commission should be invited to review the scope for efficiency gains by BT and to make proposals for the prices formula; and secondly, that the guidelines in Section 3 of the Bill should be amended to require

the MMC and DG Tel to take the need for efficiency specifically into account. The Chief Secretary was content not to press these points on the understanding that the Secretary of State was sympathetic to the concept of an external assessment of the scope for cost savings in order to underpin the pricing formula eventually adopted, and would also be prepared to consider an amendment to Section 3 on these lines at Report Stage of the Bill.

I am sending copies of this letter to the Private Secretaries to the Prime Minister, Home Secretary, Foreign Secretary, Lord President of the Council, Secretary of State for Trade, and to Mr Sparrow and Sir Robert Armstrong.

Yours sincerely

JGt. Gieve

JOHN GIEVE
Private Secretary

Post & Telecom. Future Pt 6

cc Energy; Cross Channel Electricity Link June '80

pm.

WM 8/2

PRIME MINISTER

STATEMENTS ON TELECOMMUNICATIONS REGULATION AND CEGB VESSEL CHARTER

The House was fairly empty for both these statements.

Telecommunications

Stan Orme attempted to manufacture outrage on the grounds that Mr. Baker's statement directly affected Clause 3 of the Telecommunications Bill which the Standing Committee were still discussing. He called for the Bill to be suspended to allow time for discussion of the report and the Minister's statement. He said that the decision to allow competition on the prime instrument would put jobs in BT at risk, and would promote a flood of imports. He concluded that "Professor Walters' sticky fingers were all over this document". Opposition Members followed up the same theme, but also called for an assurance that rural services would not be put at risk.

Kenneth Baker had no trouble in dealing with Questions. He pointed out that the Government had always promised to publish the Littlechild Report, and that Mr. Orme had himself demanded its publication last week. There had been 80 hours of debate in Committee; the Opposition had made filibustering speeches of five hours in length; there were another 20 groups of amendments to be taken on Clause 3; and it was right that the Committee should continue to meet to discuss the Bill. The decision to allow competition on the prime instrument would extend consumer choice, and there was no evidence that it would lead to a flood of imports. It was a nonsense to say that only a public monopoly should be allowed to supply these instruments: why should the privilege of competing for jobs not be extended to the private sector? There was

/ an obligation

an obligation on British Telecom to provide telephony and telecommunications services. The access fees that BT would be able to charge competing public networks should generate enough revenue for BT to provide emergency, call box, and rural services. He felt Professor Littlechild was right to concentrate on price reductions since this was the area in which BT's monopoly power was felt most keenly by the public. The cuts in trunk rates made by BT showed the benefits of opening up the Corporation to competition.

CEGB Charter

John Moore had a slightly more difficult time. John Cunningham said that the shipbuilding industry was facing severe recession, and it was astonishing that a public Board had used public money to finance work in a Korean yard. He asserted that British Shipbuilders had not been given a chance to submit a detailed tender; that there had been no consultation with the Department of Industry; and that the CEGB were simply paying to the broker a sum equivalent to the capital cost of building a ship. He suggested that the French utilities involved in laying the cross-channel link had ensured that their cable-laying work had gone to French yards. The whole episode was a "stab in the back" for British shipyard workers.

John Moore said that there had been contacts with the Department of Industry, the Offshore Supplies Office of the Department of Energy and between the Chairman of British Shipbuilders and the CEGB; the tender had been conducted in the normal manner, and BS had been given full opportunity to make their views known; the CEGB had recognised its obligation to buy British where possible by repeating the tendering process when the first tender had failed to produce a suitable UK bid. He was not responsible for the French

/ Government's

Government's policy, but he understood that their utilities were chartering a Norwegian vessel for conversion in Marseilles. He emphasised that the CEGB were chartering, and not buying, this ship; that the cost of the contract was only 4 per cent of the £250 million UK share of the cross-channel cable contract; and that the Opposition should consider the effect on electricity prices of accepting a tender from a UK yard which was 50 per cent higher than the Korean tender. He quoted the MMC report which said that the CEGB generally pursued a buy-British policy where possible, and which reached the conclusion that the Board's "costs could have been lower .....".

The most difficult moment for Mr. Moore came when Anthony Nelson gave some support to the Opposition by questioning the Government's line on this contract.

WR

7 February 1983

Telecommunications Policy

3.30 pm

The Minister for Industry and Information Technology (Mr. Kenneth Baker): With permission Mr. Speaker, I will make a statement about telecommunications policy.

After privatisation, British Telecommunications should be able to develop and diversify in a dynamic manner not only in the area of existing telecommunications services but in the new information technology systems on a worldwide basis. This should benefit the customer, the country, investors, BT and its staff. The Government recognise the public concern that there should be no opportunity for BT plc to fix excessive charges to customers in the areas where it has a virtual monopoly for the time being. To this end my right hon. Friend the Secretary of State announced at the Second Reading of the Telecommunications Bill the appointment of Professor Stephen Littlechild of Birmingham university to carry out a study of these issues. Professor Littlechild's report is being published today and copies are available in the Vote Office. The Government are grateful to Professor Littlechild for undertaking this important task.

Professor Littlechild has made two major recommendations concerning the price regime after privatisation and the extent of competition. As regards pricing policy, he recommends that BT plc should be obliged for five years to keep below the increase in the RPI any increase in its prices for domestic rentals, local calls and other services of particular concern taken together. The Government accept this approach but will want to give further consideration to the range of services to be included within the price limitation, for example charges for installation and trunk calls. We shall also be considering the period for which it should apply. It will be important that the precise formula should be seen to be soundly based and fair both to the consumer and to BT. BT will be obliged to observe the arrangement finally determined and the powers of the Director General of Telecommunications under the Bill are adequate to ensure that it is complied with. These arrangements are aimed at securing a continuing improvement in BT's efficiency and a continuing reduction in the real cost of telephone services to the consumer across the country.

Professor Littlechild also says that competition is by far the most effective protection against monopoly. He sees his price limitation proposal as a safeguard that is required only until competition develops. The Government accept this approach and accordingly I can now announce further initiatives to promote competition.

First, customers who have standard BT sockets will be free to purchase from any supplier the first telephone for connection to direct exchange lines. I shall table an amendment to the Telecommunications Bill to give effect to this change. BT and the manufacturing industry need time to adjust, but I intend that by the end of next year all customers who want to exercise this choice will be able to do so.

Secondly, the maintenance of all new call routeing apparatus will be opened to competition by persons approved by the Secretary of State. BT itself will remain free to offer a maintenance service, but on a fair, commercial basis. I intend to introduce an amendment to the Telecommunications Bill to provide for licensing of those maintaining call routeing apparatus. I shall also be consulting BT, the industry and other interested parties on the phasing in of these arrangements, which I expect to be completed within three to four years. The ending of the prime instrument monopoly and of BT's monopoly over the maintenance of all call routeing apparatus, means that the entire market for new telecommunications apparatus will be open to competition.

Thirdly, the Government accept that the current restrictions on Mercury's supply of international services should be eased. This will require discussions with other Governments. A study on the provision of international services is nearing completion and after consultation with interested parties I shall make a further statement. I would hope to be able to do so by the end of April this year.

Fourthly, the Government accept the principle of reducing restrictions on the resale of capacity on private telecommunication circuits leased from BT and other public telecommunications operators, but I recognise that this could have considerable implications for BT's revenue. I shall want to consider the terms and timing of introducing the changes after consultation with BT and other operators.

Fifthly, the Government believe that competing public networks should have the right to interconnect on appropriate terms with BT's networks. In return BT must have the right to charge operators such as Mercury and the two cellular radiophone networks access fees on a non-discriminatory basis, which will contribute towards the cost of providing the national asset of our country-wide local networks. BT's own trunk and international divisions should also be subject to access fees on the same basis. These access fees will generate a significant revenue for BT to cover emergency 999 services, which are free, and any losses incurred on call boxes and other services, particularly those in remote and rural areas. The access fees will safeguard the continued provision of these services without subsidy from the taxpayer, thus maintaining the universal service.

The Government recognise the importance to the national economy of BT's vital role in telecommunications. We are phasing in these new measures of competition in step with progress towards moving BT out of the public sector and out of the present web of Government controls. This is an expanding and rapidly changing market, and the greatest benefits to Britain, the consumer and the telecommunications industry will come from fuller and fairer competition. The arrangements that I have announced today will help achieve this.

Mr. Stanley Orme (Salford, West): The Minister's statement has been made against the background of the Telecommunications Bill—a major measure—clause 3 of which is being debated in Committee. We were promised a draft licence by the Government, but did not get it. We were given only an outline. We have had three publications from the Government, called "Ringing the Changes", which have added confusion to the debates on the Bill. Does the Minister not think that to introduce Professor Littlechild's report in the middle of our consideration of the Bill is unprecedented in parliamentary terms?

The foreword to the report says that Professor Littlechild

"shall study and evaluate proposals to regulate BT's profitability, having regard to the objectives set out in Clause 3 of the Telecommunications Bill".

offer comparatively cheap tickets in addition to very expensive ones so that people of modest means can go to the Royal opera house.

Mr. Whitehead: In view of the Rayner connections of this group, will the right hon. Gentleman urge upon it that it does not follow the unhappy precedent of the recent Rayner report on the Victoria and Albert museum and that it visits the various institutions that it is surveying while they are open? will accountants' or consultants' fees that stem from this exercise come only after tendering for the work that has to be done?

Mr. Channon: No. I think that it has been decided who will undertake the scrutinies, as is the normal practice. Without accepting what the hon. Gentleman said about the scrutiny of the Victora and Albert museum, I can assure him that the scrutineers have every intention of making exhaustive visits to both organisations.

Arts Council (Touring Budget)

25. **Mr. Silvester** asked the Secretary of State for Education and Science whether any changes have been made by the Arts Council in the touring budget following his statement of 20 December 1982, *Official Report*, column 664-5.

Mr. Channon: The current allocation for touring in England in 1982-83 is £7·5 million, including an additional sum of £400,000 provided from the supplementary grant announced on 20 December 1982. The touring budget for 1983-84 is £7,865,000.

Mr. Silvester: I congratulate my right hon. Friend on his care about touring. Does he recognise that one of the distressing aspects of the saga of the visit of the Royal opera house to Manchester was its on–and-off nature, despite the great deal of investment and commitment that the operation received? Is he prepared to say that with the new arrangements people will be able much more to rely upon the visits taking place instead of the previous rather doubtful prospect?

Mr. Channon: I understand my hon. Friend's concern. I am pleased to say that the Royal opera company has been able to announce that its visit to Manchester will take place later this year. We must all hope that it will be a tremendous success. Future plans will be discussed in detail with everyone concerned, including the Greater Manchester council and the city of Manchester. I hope that we can avoid future uncertainties in this way.

Mr. Whitehead: Bearing in mind the outrage in greater Manchester when the Royal opera house originally called off its visit, does the right hon. Gentleman agree that we should say publicly in the House that we think it should be an annual obligation on the national companies to tour in this way, and that they should not merely return to touring when they have been bailed out by the payment of a one-off sum?

Mr. Channon: Most of the national companies tour extensively. The Royal opera house has special problems, including enormous costs. There are those who consider that the money could be better spent than on tours by the Royal opera house. I accept that the national companies have an obligation to tour.

Arts Council (Theatres Grant)

26. **Mr. Greenway** asked the Secretary of State for Education and Science what was the total Arts Council grant to theatres in the last year for which figures are available.

Mr. Channon: The Arts Council estimates that its grants to theatres in Great Britain in 1982–83 will total just under £26·3 million compared with the previous year's total of nearly £23·1 million.

Mr. Greenway: I welcome the increase that my right hon. Friend has mentioned and I thank him for it. Does he agree that the Royal Shakespeare company has given oustanding service to the arts in both London and Stratford on Avon and in tours around the world? What specific help is the Arts Council giving the company in grants this year?

Mr. Channon: I agree entirely with my hon. Friend about the Royal Shakespeare company. Last year it received an extra settlement of £850,000 from the supplementary grant that I announced on 20 December 1982. It is to receive grant this year of £3·6 million as opposed to £3 million last year. Extra money has been made available to it, exceptionally, of nearly £1½ million.

Mr. D. N. Campbell-Savours: Is it not true that there is a clear emphasis in allocation of Arts Council grants towards the more affluent areas, leaving the industrial areas very often culturally deprived? What will the Minister do to redress that imbalance, particularly as the quality of life is so closely linked to the pursuit and support of the arts?

Mr. Channon: I do not accept the hon. Gentleman's premise. He may be interested to know that this year the basic grant for the northern area was £1·72 million, which was a rise of 11 per cent. over last year, and that in addition it received a further £60,000 in supplementary grants. There has thus been a substantial increase for the North.

We have been discussing clause 3 for several sittings of the Committee, and the Minister now has the affrontery to introduce the report in the middle of those discussions.

The Minister probably saw the report yesterday in one of the Sunday papers about the confusion over pricing policy and whether the consumer might be subsidising sections of industry. We wish to discuss pricing and Professor Littlechild's complicated and detailed proposals in some detail. We feel it is wrong for the Minister to produce this report today and expect the Committee to go ahead tomorrow.

By breaking the prime instrument monopoly the Minister is, in effect, allowing outside contractors to provide the prime instrument, while still using the network. Will this not create confusion over breakdowns and repairs? Who will be responsible? What about the effects on jobs for thousands of workers in BT? Will not imports flood in? What has the Secretary of State to say about that? This measure is an open invitation to imports to flood in.

What effect will allowing Mercury on to the international market at this early stage have on BT's finances and future prosperity? May we have more details about the resale in relation to private telecommunications? Will someone be able to buy a series of outlets and relicense them? Will there be any control of those prices? How will the Government monitor that? A major change to the Bill is proposed. The Minister says that he will move amendments in Committee. This measure will further dismantle a crucial part of the public sector, and we see Professor Walters' sticky fingers all over this document. Indeed, he was probably the motivating force behind Professor Littlechild's appointment.

We want parliamentary time to discuss the Littlechild report, and therefore we ask that consideration of the Bill be suspended so that we can discuss this issue. It involves a major British industry and affects 250,000 workers. It also affects the telecommunications system of the United Kingdom. The hon Gentleman has dropped this report on the House when the Bill is in the middle of its Committee stage, and he therefore has no right to proceed with the measure. We ask him to withdraw the Bill.

Mr. Baker: The right hon. Member for Salford, West (Mr. Orme) has pressed me consistently in Committee for more information, and I have assisted the Committee by providing an almost unparalleled amount of information for our discussions upstairs. Only last week he demanded that I publish the Littlechild report. On Second Reading my right hon. Friend the Secretary of State for Industry said that we had asked Professor Littlechild to report and that we would publish the report.

I remind the right hon. Gentleman that there have been more than 80 hours of debate in Committee. We have been subjected to speeches lasting as long as five, four and three hours. An outrageous filibuster has been going on upstairs. So far we have debated only three groups of amendments to clause 3. There are another 20 groups of amendments to clause 3 to debate. It so happens that we are approaching the pricing part of clause 3, and so it is entirely appropriate that the Committee should meet tomorrow to debate this subject further.

The right hon. Gentleman says that this measure represents a major change of policy, but it is an extension of the policy that my right hon. Friend the former Secretary of State for Industry announced in July 1980, and which I extended in July 1981.

The right hon. Gentleman asked me various questions about the prime instrument. After the Bill has been enacted, the choice available to consumers will become greater as more sockets are fitted by BT. Consumers will be able to choose whether to buy or rent, and they will be able to buy from whoever they want. I do not see how that can damage our system. Indeed, the measure represents an extension of choice and competition that will benefit the industry.

The right hon. Gentleman asked whether there would be a flood of imports. Since the approvals system was set up 18 months ago there have been about 32 approvals involving 12 companies in relation to telephone hand instruments. The right hon. Gentleman should know that 11 are manufactured entirely in the United Kingdom, that 15 are manufactured substantially in the United Kingdom and that six are modified to be manufactured in the United Kingdom. Therefore, as a result of the policy there will be work for people in the United Kingdom.

The right hon. Gentleman also asked me about Mercury, I shall make a statement by 30 April on the changes on international access for which Mercury has asked and which we shall grant on the international lines. Resale is a very important issue and I shall need time to consider the terms and conditions. However, it is regrettable that the right hon. Gentleman's reaction should be to say that only the public sector and a state monopoly can provide such services. That is just not so. The right hon. Gentleman cannot accept that services can improve as a result of competition and choice. Why should it be the exclusive privilege of BT and its employees to provide such new advanced services? Surely that privilege should be extended to other workers, companies and operations.

Mr. Michael Marshall (Arundel): Will my hon. friend accept that his statement is of the greatest importance and that we shall naturally want to study the Littlechild report in detail? At first hearing it would seem that the domestic competition under Littlechild presents the system in this country with a fair and reasonable opportunity to grow and flourish. I declare an interest in Mercury Communications Ltd. Does my hon. Friend accept that international switching is vital if fair and free competition is to be extended into that area as well?

Mr. Baker: I agree with my hon. Friend. For some time—for more than a year—Mercury has been asking for access to switched international services. Professor Littlechild recommends that. I shall make a further statement on that policy within the next three months.

Mr. Geraint Howells (Cardigan): I am sure that the Minister is well aware that those who live in rural areas are very worried about the privatisation of BT. Will the hon. Gentleman give an assurance both to the House and to those who live in rural areas that the service will be kept intact? If the Minister cannot get all the fees required from the access service, what will happen to the rural kiosks?

Mr. Baker: In Committee, the hon. Gentleman's fellow countryman—although not his fellow party member—the hon. Member for Caernarvon (Mr. Wigley) has been very eloquent in representing the views of rural and remote areas. We gave the Committee assurances on

[Mr. Baker]

this issue repeatedly last week. There is an obligation on BT plc to provide a universal telephone service. The obligation goes wider than that and extends to telecommunications services. That is not included in the present Act. That obligation will have to be policed not only by BT—as it is now—but by the Director General of Oftel. Indeed, the Secretary of State also has a responsibility to ensure that that universal service is provided.

The hon. Gentleman asked about services in remote and rural areas, but BT is unable to say whether it makes money—such is the state of the allocation of cost accounting within BT. The latest indication from BT is that the remote and rural areas contribute profits to the centre, because the systems are often easier and simpler to run than complicated city systems. To the extent that money may be lost, the access fees will be set at a level that will ensure that BT's social obligations are met. All those with a telephone or telephone service now can be assured that it will continue. Indeed, I refer the hon. Gentleman to the long debates that were held last week in Committee on this issue.

Mr. Michael Grylls (Surrey, North-West): Does my hon. Friend accept that we cannot move too fast to increase competition in the telecommunications industry, and that the more he does the greater consumer choice will be and the more jobs will be created in new firms?

Mr. Baker: I entirely accept that. The speed with which we are moving should be recognised. In four years we have moved significantly to broaden competition from a position in which BT had total dominance in standard setting, equipment approval, equipment supply and the issuing of licences to would-be competitors. That has had a good effect on BT. It is reported on all sides that BT has become much more conscious of its consumers and subscribers and does not take them for granted. That in itself is good, quite apart from the effect on Britain's domestic industry.

Mr. Ian Wrigglesworth (Thornaby): Professor Littlechild's report recommends that BT should be obliged to keep price increases below the retail prices index for five years. The Minister has told the House today that the Government accept that approach. Does that mean that BT's prices will not increase by more than the RPI during the next five years, or do some of the Minister's other words mean that is not the case?

Secondly, will the Director General of Oftel have any say on prices? When will his office be established? What involvement will he have in considerations of this nature?

Mr. Baker: Needless to say these matters have been well covered in debate upstairs, the appointment of the Director General of Oftel and the establishment of the office will depend upon the progress of the Bill through the House.

On prices, Professor Littlechild recommends that the Director General concentrates on the two areas where there will be a virtual monopoly—domestic rentals and domestic tariffs. For most domestic consumers that is the main part of their bill. Prices should be limited to ensure that they do not increase more rapidly than the RPI. They will increase over five years by RPI minus a certain amount. That means that after privatisation the ordinary telephone subscriber can look forward to his bill going up by less than the rate of inflation. There is a real cost reduction.

Mr. Peter Hordern (Horsham and Crawley): Will British Telecom have the sole right to test telephone equipment? Has my hon. Friend's attention been drawn to an article in *The Economist*, which said that one small firm that wanted to try out a PABX system was to be charged £30,000 for it, in contrast to the American system, where about $1,500 appears to be the charge? What is the position?

Mr. Baker: When the approval system was set up, the only test laboratories were those of BT. It had the only testing engineers and the only test approval systems—and, of course, no standards existed. During the past 18 months, with the assistance of the British Standards Institution, we have commissioned a series of standard writing exercises which have now been approved for much of the telephone apparatus. A separate test laboratory is being set up by the independent board to test the equipment, because it is inappropriate for BT to test equipment from its competitors. We are trying to accelerate that process as much as we can. I ask my hon. Friend to appreciate the fact that one cannot overnight end a monopoly that has lasted for 70 or 80 years. We are moving at a very fast pace, and I want to reach my hon. Friend's objective just as quickly as he does.

Mr. Dafydd Wigley (Caernarvon): Will the Minister confirm that paragraph 14.7 of the report suggests three specific modifications to the Bill now in Committee, and that one of them concerns the possibility of funds from the Government to help to relieve the costs of

"public call box services, emergency services and services in rural areas"?

As the Government rejected amendments in Committee to that end, will he now say whether the Government are prepared to consider the matter further in the light of this report?

Mr. Baker: The debates that we are likely to reach tomorrow on clause 3(1)(*b*) will cover both those recommendations and whether there should be an Exchequer subsidy for the social obligations imposed on BT. We believe that the system of access charges, which I briefly sketched this afternoon, will provide a significant and substantial revenue to BT, which will reward BT for the fact that it has extensive local domestic networks. Anyone who wants to plug in to Mercury, Hull, and the radio telephone networks will have to pay that access fee, and the revenues from that will go to meet the social obligations of the call boxes, emergency services, and any other social obligations.

Mr. Timothy Smith (Beaconsfield): Is it not preposterous that the right hon. Member for Salford, West (Mr. Orme) complains about the length of time that we have spent in Committee on the Telecommunications Bill when he and his right hon. and hon. Friends have been conducting the most outrageous filibuster, and when after 80 hours, we have reached only clause 3?

As the main purpose of regulation, according to the Littlechild report, is to protect domestic and small business subscribers against BT's dominant market position, is there not a certain undeniable logic to the local tariff

reduction scheme as proposed by Professor Littlechild? Will not the Government's proposals restrict monopoly, promote competition, and above all, protect the consumer in a very effective manner?

Mr. Baker: Yes. My hon. Friend has put it very well. Professor Littlechild's proposals, by concentrating on the domestic area, where there is a monopoly, and by imposing a limitation of price there, is concentrating on the area that affects most people, where there is a monopoly, and where BT must not be allowed to charge what it wishes. The corollary, of course, is that there should be competition in the other services, the trunks and international, and competition has already reduced prices there. Trunk rates were cut in 1981 and in 1982. I do not believe that those cuts would have taken place if we had not pursued the policy in telecommunications that we have pursued since 1980.

Several Hon. Members *rose*——

Mr. Speaker: Order. If hon. Members are brief, I propose to call those hon. Members who have been rising from the beginning, and then the Front Benches.

Mr. Ken Eastham (Manchester, Blackley): As a result of the Minister's statement this afternoon, have any estimates been made in his Department of imports of telephone equipment?

Mr. Baker: The hon. Gentleman is far too pessimistic. If he believes that as a result of competition we shall be flooded by imports, that is a grave reflection on the telecommunications industry in this country. We have a substantial telecommunications industry, but because of the rather cosy relationship between that industry and BT it has not been as forceful and competitive as it could have been. However, during the past 18 months it has responded vigorously. It has introduced new models, which have been competitively priced, and the market is beginning to take off again.

Mr. Richard Page (Hertfordshire, South, West): I congratulate my hon. Friend and his Department on their positive reaction to the Littlechild report. On the matter of upening up the market to international competition, will the negotiations be undertaken by his Department, Oftel, BT, or the companies involved?

Mr. Baker: They will be undertaken by my Department in discussions with BT and Mercury.

Mr. D. N. Campbell-Savours (Workington): Despite the fact that the Minister said that there is a weighting in approval, will he assure us that the weighting in terms of imports is the reverse of what he said before? Will he also say what downstream support he is giving to telecommunications equipment producers in the form of sectoral aids, over and above what is already available from the Department of Industry?

Mr. Baker: The answer to the hon. Gentleman's latter question is that the telecommunications operators, the major companies in this country, qualify for general support under our support for innovation. For example—here I speak from memory—they applied for support in the development of fibre optics and opto-electronics. On the question of weighting in favour of domestic manufacturers, because three or four years ago BT had such a grip on the market and the approvals procedures, we had to set up an interim approvals procedure, which has been regulated by my Department. In that interim approvals procedure we have given precedence wherever possible to those pieces of equipment that either are made or will be made in this country.

Mr. Tim Eggar (Enfield, North): I give a particularly warm welcome to the decision to provide increased competition for supply and for BT. Is my hon. Friend satisfied that the provisions relating to price increases and the RPI are right? Is it not possible that BT is already getting too high a return? Is it not further possible that there will be technological changes that will decrease the costs of providing the service? Therefore, should not the Director General have a right to look at costs as well as to expect increases below the RPI?

Mr. Baker: Yes, indeed. In setting the access fee, the Director General will have the right to look at costs and be able to make determinations arising from the costs. The lesson of the American experience in the regulation of public utilities and prices and profits has led me and Professor Littlechild to believe that the system in America is breaking down—and has, in effect, broken down—and that the system of cost allocations and of trying to determine which parts are profitable do not work. Professor Littlechild has devised a new, and, in my opinion historically important, method of controlling the price of what, in effect, is a private monopoly.

Mr. Gerry Neale (Cornwall, North): I join in the congratulations to my hon. Friend. It is because he refuses to close his mind to new reports and comments that he is earning increased respect on the Conservative Benches. Will he nevertheless be alerted by the fact that following three years of sustained argument from the telecommunications industry that there should be greater competition in prime instrument policy and maintenance, he is now likely to come under immediate pressure to try to make the period of phasing shorter and more definite, to ensure that suppliers can offer immediate choice to the consumer?

Mr. Baker: I appreciate my hon. Friend's impatience. I have tried in this whole area to move as quickly as I can. If one can improve on the period of 18 months or two years in relation to the prime instrument and a completion period of within three or four years on maintenance, following discussions with the industry I shall see what can be done.

Mr. Gary Waller (Brighouse and Spenborough): Does my hon. Friend recognise that the more forward-looking managers within BT are anxious that BT should respond to the new challenges and welcome the opportunities presented to them? Is it not regrettable that a great deal of misleading information is being circulated among employees of BT, leading to unjustified fears?

Mr. Baker: I hope that the fears are unjustified. Many people in BT recognise that this is such a rapidly changing and expanding market that they should seize the opportunities. It is no way to seize opportunities to act in a dog in a manger fashion. We are creating opportunities and choice on an unprecedented scale.

Mr. Richard Shepherd (Aldridge-Brownhills): The Littlechild report specifically says that the prevention of excessive profits to shareholders is not a relevant consideration. Is my hon. Friend convinced—I take up the point of my hon. Friend the Member for Enfield, North (Mr. Eggar)—that this is the best way of ensuring the lowest possible prices for consumers, and also that the rate

[Mr. Richard Shepherd]

of return is reasonable and fair? Should not these duties be laid upon the Office of Telecommunications in the Bill rather than peripherally by way of licence?

Mr. Baker: I am asked whether I consider the Littlechild approach is fair in concentrating price limitation on a local tariff index as opposed to a profit ceiling. My hon. Friend will find that Professor Littlechild deals with this matter in detail. He also deals, in paragraph 14.6, with the possibility of having local tariff index control and profit control as well. He concludes that

"to impose a profit ceiling on a local tariff reduction scheme is both unnecessary and undesirable."

I appreciate that there will be different views on this aspect of Professor Littlechild's report. I believe that he sets out convincing reasons why we should accept his recommendations. I assure my hon. Friend that the Director General of Oftel will not have a supine role. He will have a monitoring role. The whole purpose of Oftel, apart from improving the consumer interest, is to monitor the licence.

Mr. Orme: Does the Minister agree, following the exchanges on a very complicated report, which hon. Members have not had a chance to read in detail, that, before proceeding tomorrow morning to deal with clause 3 of the Telecommunications Bill we should have time to study the report? Is he aware that clause 3 is referred to in the report and is cental to some of Professor Littlechild's recommendations? Does the Minister agree also that he has never talked about a filibuster upstairs and that when my hon. Friend the Member for Newcastle-under-Lyme (Mr. Golding) made an extensive and well-reasoned speech he congratulated my hon. Friend?

Mr. Baker: I was following the normal courtesies of the House. The right hon. Gentleman has not appreciated the sense of gratitude, expressed in my voice, that a six-hour speech came to an end. I assure the right hon. Gentleman that there will be opportunities tomorrow and in the coming debate on the Bill upstairs to discuss these matters fully. I want them debated fully. I want them debated extensively. We should start tomorrow.

Cross-Channel Electricity Cable

4.5 pm

The Under-Secretary of State for Energy (Mr. John Moore): With permission, Mr. Speaker, I wish to make a statement. In connection with the 2,000 MW cross channel electricity cable project, the Central Electricity Generating Board sought competitive tenders from a number of British shipping firms for the hire of a vessel to lay cables between England and France. The lowest tender was submitted by a British firm, International Transport Management, of Middlesborough, from which the vessel will be chartered. I would emphasise that the cable-laying barge will not be purchased or owned by the CEGB, but by the British firm concerned.

The CEGB must of course be conscious of its obligations to provide electricity as cheaply as possible. As a nationalised industry, it is also conscious of the Government's wish that, wherever possible, it should buy British.

However, when the CEGB received the first tenders for this project some months ago, the price differences were so great it appeared inevitable that the shipbuilding work would go abroad. The board, naturally concerned over this, then asked the firms to tender again, and expressed a clear preference—other things being equal—for vessels supplied by United Kingdom yards.

Regrettably, the second tenders showed such a huge price difference that the board had no choice but to accept the bid from ITM, involving the construction of a vessel in a Korean yard. Other bids to the CEGB, I understand, were at least 50 per cent. higher.

The Government do, of course, provide financial assistance to help United Kingdom shipbuilding firms to gain orders, but even with Government assistance the difference in bids would have been unbridgeable. Hon. Members who have repeatedly stressed the importance to industry and consumers of low-cost electricity will understand this decision.

Questions on the shipbuilding industry, including matters relating to assistance from the shipbuilding intervention fund are, of course, matters for my right hon. Friend the Secretary of State for Industry.

Dr. John Cunningham (Whitehaven): I thank the Minister for making the statement. Is it not astonishing, in the middle of the worst slump in shipbuilding this century, that a British publicly financed board should be involved in a contract to spend British taxpayers' money to build a vessel in a Korean shipyard?

I wish to ask the Minister a number of specific questions. Is it correct that ITM at no time invited British Shipbuilders to make a detailed tender for this work? Is it also correct, notwithstanding what the Minister says about the ownership of the vessel, that the CEGB engaged naval architects to draw a detailed and complex specification for this vessel, which was tantamount to meaning that it was designing the vessel for its own particular purposes? Is it also the case that, in terms of the financial arrangements of the deal, the CEGB contribution will be a capital expenditure contribution? Does this not reinforce the point that it is paying for the vessel to be built?

Will the Minister say what the French utilities are doing to fulfil their part of the contract for the cable laying? Will not all their contracts be placed in France? Will he explain

2 Mr's cc

DEPARTMENT OF INDUSTRY
ASHDOWN HOUSE
123 VICTORIA STREET
LONDON SW1E 6RB

TELEPHONE DIRECT LINE 01-212 6401
SWITCHBOARD 01-212 7676

FROM THE
MINISTER OF STATE
FOR INDUSTRY AND
INFORMATION TECHNOLOGY
KENNETH BAKER'S OFFICE

POOL

Michael Scholar Esq
10 Downing Street
LONDON SW1

7 February 1983

Dear Michael,

LITTLECHILD REPORT ON TELECOMMUNICATIONS

My Secretary of State's minute of 3 February to the Prime Minister attached a draft of the statement which Mr Baker intends to make today on the Littlechild report.

I now attach a final version of the statement, which will be delivered some time after 3.30 today.

Copies of this go to the Private Secretaries to the Home Secretary, the Foreign Secretary, the Chancellor, the Leader of the House, the Chief Whip, the Secretary of State for Industry, John Sparrow, Sir Robert Armstrong and Bernard Ingham.

Yours sincerely

Neil McMillan

N M McMILLAN
Private Secretary

M76/M76AAQ

STATEMENT

TELECOMMUNICATIONS REGULATION

1. With permission Mr Speaker I will make a statement about telecommunications policy.

2. After privatisation, BT should be able to develop and diversify in a dynamic manner not only in the area of existing telecommunications services but also in the new information technology systems on a world-wide basis. This should benefit the customer, the country, investors, BT and its staff. But the Government recognises the public concern that there should be no opportunity for BT plc to fix excessive charges to customers in the areas where it has a virtual monopoly for the time being . To this end my Rt Hon Friend the Secretary of State announced at the Second Reading of the Telecommunications Bill the appointment of Professor Stephen Littlechild of Birmingham University to carry out a study of these issues. Professor Littechild's report is being published today and copies are available in the Vote Office. The Government is grateful to Professor Littlechild for undertaking this important task.

3. Professor Littlechild has made 2 major recommendations concerning the price regime after privatisation and the extent of competition. As regards pricing policy, he recommends that BT plc should be obliged for 5 years to keep below the increase in the RPI any increase in its prices for domestic rentals, local calls and other services of particular concern taken together. The Government accepts this approach but will want to give further consideration to the range of services to be included within the price limitation for example charges for installation and trunk calls. We will also be considering the period for which it should apply. BT will be obliged to observe the arrangement finally determined and the powers of the DG of Telecommunications under the Bill are adequate to ensure that it is complied with. These arrangements are aimed at securing a continuing improvement in BT's efficiency and a continuing reduction in the real cost of telephone services to the consumer across the country.

4. Professor Littlechild also says that competition is by far the most effective protection against monopoly. He sees his price limitation proposal as a safeguard only required until competition develops. The Government accepts this approach and accordingly I can now announce further initiatives to promote competition.

5. First, customers who have standard BT sockets will be free to purchase from any supplier the first telephone for connection to direct exchange lines. I will table an amendment to the Telecommunications Bill to give effect to this change. BT and the manufacturing industry need time to adjust, but I intend that by the end of next year all customers who want to exercise this choice will be able to do so.

6. Second, the maintenance of all new call routing apparatus will be opened to competition by persons approved by the Secretary of State. BT themselves will remain free to offer a maintenance service but on a fair, commercial basis. I intend to introduce an amendment to the Telecommunications Bill to provide for licensing of those maintaining call routing apparatus. I will also be consulting BT, the industry and other interested parties on the phasing in of these arrangements, which I expect to be completed within 3-4 years. The ending of the prime instrument monopoly and of BT's monopoly over the maintenance of call routing apparatus, means that the entire market for new telecommunications apparatus will be open to competition.

7. Third, the Government accepts that the current restrictions on Mercury's supply of international services should be eased. This will require discussions with other Governments. A study

on the provision of international services is nearing completion and after consultation with all interested parties, I will make a further statement. I would hope to be able to do so by the end of April this year.

8. Fourth, the Government accepts the principle of reducing restrictions on resale of capacity on private telecommunication circuits leased from BT and other public telecommunications operators, but I recognise that this could have considerable implications for BT's revenue. I will want to consider the terms and timing of introducing the changes after consultation with BT and other operators.

9. Fifth, the Government believes that competing public networks should have the right to interconnect on appropriate terms with BT's networks. But in return BT must have the right to charge operators such as Mercury and the 2 cellular radiophone networks access fees on a non-discriminatory basis which will contribute towards the cost of providing the national asset of countrywide local networks. BT's own trunk and international divisions should also be subject to access fees on the same basis . These access fees will generate a significant revenue for BT to cover emergency 999 services, which are free and any losses incurred on call boxes and other services particularly those in remote and rural areas. The access fees will safeguard the continued provision of these services without

subsidy from the taxpayer, thus maintaining the universal service.

10. The Government recognises the importance to the national economy of BT's vital role in telecommunications. We are phasing in these new measures of competition in step with progress towards moving BT out of the public sector and out of the present web of Government controls. This is an expanding and rapidly changing market, and the greatest benefits to Britain, the consumer and the telecommunications industry will come from fuller and fairer competition. The arrangements I have announced today will help achieve this.

F

CONFIDENTIAL

DEPARTMENT OF TRADE 1 VICTORIA STREET LONDON SW1H 0ET Telephone 01-215 7877

cc J.V.

From the Secretary of State

The Rt Hon Patrick Jenkin MP
Secretary of State for Industry
Ashdown House
123 Victoria Street
London
SW1

4 February 1983

Dear Patrick,

IAL

with PM

Thank you for your letter of 1 February.

I have very considerable reservations about the suggested joint bid by British Telecom and Racal which smacks to me too much of an attempt to sidestep E(NI)'s decision not to allow British Telecom to bid for IAL. The more so because Sir Ernest Harrison admitted that Racal had considered making a bid themselves but had decided not to do so. Nor did I find the reasons he gave for the joint venture approach at all convincing. The advantages he claimed would flow from collaboration with British Telecom could just as easily have been obtained if Racal themselves had bought IAL. Indeed one was left with the impression that the motivation was much more one of giving British Telecom the opportunity of expanding overseas.

The joint bid therefore leaves me with the same fundamental reservation that I - and indeed most of our colleagues - had about the original bid, namely that it would be diverting British Telecom from the most important task of all, namely pulling its own socks up prior to privatisation.

I have read John Sparrow's letter of 3 February. I find it sits very oddly with what was said in the recent CPRS paper on State Monopolies. But were the bid to be allowed to go ahead it would certainly be essential that it should be subject to stringent conditions of the kind he suggests. There might well be other conditions

From the Secretary of State

that needed to be imposed as well, as indeed Leon Brittan indicates in his letter of 4 February.

We are already concerned about the delay in disposal of IAL. We need the proceeds by 31 March. We will need therefore to continue to process other bids and we could not hold up a decision once that point is reached pending settlement of this particular proposal.

I would think that as we are effectively considering reversing a decision taken by E(NI) the issue ought now to go back to that Committee.

I am sending copies of this letter to the members of E(NI), Sir Robert Armstrong, and to John Sparrow.

Yours,

Arthur.

LORD COCKFIELD

E CONFIDENTIAL

cc JV.

Treasury Chambers, Parliament Street, SW1P 3AG

The Rt Hon Patrick Jenkin MP
Secretary of State
Department of Industry
Ashdown House
123 Victoria Street
London SWiE 6RB

4 February 1983

Dear Secretary of State

SALE OF INTERNATIONAL AIR RADIO

Thank you for sending me a copy of your letter of 1 February to Arthur Cockfield together with a copy of Sir George Jefferson's letter to you of 28 January containing a fresh proposal that BT should buy only 50% of IAL the other half being acquired by Racal.

This is certainly an improvement on the previous proposal whereby BT acquired at least 51%, the balance being either widely spread or spread among a number of minority industrial partners. It hangs together better in commercial and industrial terms. I would be ready to agree to it provided that:

(i) control is genuinely shared ie. there is nothing in the arrangement with Racal which gives or would if invoked give BT ultimate control over IAL;

(ii) it is clear that the IAL management support the move as in the best interests of the company - obviously it would be extremely difficult for the Government to defend, if they did not;

(iii) we are able to agree in the next few days moves which represent "a significant opening up of the BT monopoly" - this seems to me an important part of the bargain with BT and they should not be left in any doubt that our willingness to allow them to expand their horizons is dependent on it. The Government's position must surely be that BT cannot be allowed to expand and diversify on the basis of monopoly profits.

I am copying this letter to Arthur Cockfield and to other members of E(NI), and to Sir Robert Armstrong and John Sparrow.

Yours sincerely

(approved by the Chief Secretary & signed in his absence)

pp LEON BRITTAN

CONFIDENTIAL

CONFIDENTIAL

Pl B

bc Alan Walters

POST AND TELECOMS.

10 DOWNING STREET

From the Private Secretary

4 February 1983

Telecoms Liberalisation

Thank you for your letter of 3 February, with which you enclosed a draft statement which Mr. Baker hopes to make in the House of Commons on Monday.

The Prime Minister is generally content with these proposals, and that Mr. Baker should publish the Littlechild Report and make a statement on these lines.

I am sending copies of this letter to John Halliday (Home Office), Brian Fall (FCO), and Richard Hatfield (Cabinet Office).

M. C. SCHOLAR

Jonathan Spencer, Esq.,
Department of Industry,

CONFIDENTIAL

D Prime Minister (2)

John Sparrow tells us Cabinet Britain are in favour of a joint BT-Racal bid for IAL.

cc JV

2 pps

CABINET OFFICE
Central Policy Review Staff
70 Whitehall, London SW1A 2AS Telephone 01-233 7765 MCS 4/2

From: John Sparrow
CONFIDENTIAL

Qa 06247

3 February 1983

The Rt Hon Lord Cockfield
Department of Trade
1 Victoria Street
S W 1

Dear Arthur,

International Aeradio Limited

PM's Box

I have seen Patrick Jenkin's letter to you of 1 February, and the earlier correspondence. Having been unenthusiastic about BT's initial request to bid for 100 per cent of IAL, I find the present proposal that they should be permitted to bid jointly with Racal more attractive.

Sir George Jefferson has put forward in his letter of 28 January and in his earlier letter of 17 December some persuasive commercial reasons for BT to have an interest in IAL. The main reasons advanced against the initial request from BT (i.e. division of BT management, transfer of IAL from one public sector owner to another) to a large extent fall away under this new proposal for a joint venture with Racal. However, I think it is important that in addition Racal should assume control of the Board of IAL, for example, by having the exclusive power to appoint the Chairman. This would have the following advantages:

(a) it would be clear that IAL was passing out of the public sector, regardless of the planned privatisation of BT at a later date;

(b) a dispute over policy or management issues would in the last resort be capable of being settled within IAL (often 50/50 joint ventures experience problems because no one has the final say);

(c) BT would not control IAL and therefore the extension of its monopoly would be limited.

I therefore suggest that you should permit Racal and BT to make a joint bid for IAL, provided that the terms are structured in such a way that Racal has control of the joint venture if the bid is successful.

I am sending copies of this letter to the Prime Minister, the other members of E(NI), and to Sir Robert Armstrong.

Yours sincerely,

John.

John Sparrow

Post eTels: the future of the post office, pt 6

SECRET

cc to Security: Intercept Parties

10 DOWNING STREET

From the Principal Private Secretary

3 February 1983

Dear Jonathan,

TELECOMMUNICATIONS BILL: LITTLECHILD REPORT

The Prime Minister discussed with your Secretary of State, Mr. Baker and other Ministers and officials this afternoon the statement attached to your Secretary of State's minute of 2 February about the Telecommunications Bill.

The conclusion of the meeting was that the opening to competition of maintenance of all new call routing apparatus should be phased in gradually over a period of at least three years, and four years if possible. The Prime Minister asked your Secretary of State to arrange for the draft statement to be amended in consultation with the Home Office (Mr. R.J. Andrew), the Foreign and Commonwealth Office (Mr. P.R.W. Wright), and Sir Robert Armstrong and for a revised draft to be circulated with your Secretary of State's minute of 2 February as soon as possible.

I am copying this letter to John Halliday (Home Office), Brian Fall (Foreign and Commonwealth Office), John Lyon (Northern Ireland Office) and Sir Robert Armstrong.

Yours sincerely,

Robin Butler

Jonathan Spencer, Esq.,
Department of Industry.

CONFIDENTIAL

MR. SCHOLAR

TELECOMMUNICATIONS BILL: LITTLECHILD REPORT

Following the Prime Minister's meeting this afternoon, the statement attached to the Secretary of State's minute of 2 February below is to be revised in one respect. His office will be circulating a revised draft as early as possible tomorrow.

The Prime Minister has indicated in general that she is content with the proposal that Mr. Baker should publish the Littlechild Report and make a statement on these lines. In view of his earlier association with the subject, you may like to show the minute and the revised statement to Alan Walters. Provided that he is content, you could then write to Jonathan Spencer giving the Prime Minister's go-ahead.

Jonathan Spencer would find it useful to have a minute from the Prime Minister in the course of tomorrow if possible, copied to other recipients of the Secretary of State's minute, giving the go-ahead.

MS

F.E.R.B.

I think this is almost the best outcome we could have expected

AW 4/2

3 February 1983

DEPARTMENT OF INDUSTRY
ASHDOWN HOUSE
123 VICTORIA STREET
LONDON SW1E 6RB
TELEPHONE DIRECT LINE 01-212 3301
SWITCHBOARD 01-212 7676

JU855
Secretary of State for Industry

3 February 1983

CONFIDENTIAL

Michael Scholar Esq
Private Secretary to the
Prime Minister
10 Downing Street
London SW1

Dear Michael,

TELECOMS LIBERALISATION

You and the copy recipients of this letter received a minute addressed to the Prime Minister from my Secretary of State on telecommunications liberalisation on 2 February, enclosing a statement which he hoped Mr Baker would make in the House of Commons early next week.

2 I should be grateful if you would substitute the attached minute and draft statement, which have been revised to take account of the outcome of the Prime Minister's meeting today, and the series of meetings with Sir George Jefferson which were foreshadowed in paragraph 9 of the earlier minute. I am sending copies of this letter and enclosures to John Halliday (Home Office), Brian Fall (FCO), and Richard Hatfield (Cabinet Office).

Yours sincerely,

Jonathan Spencer

J P SPENCER
Private Secretary

CONFIDENTIAL

JH 776

PRIME MINISTER

TELECOMMUNICATIONS BILL: LITTLECHILD REPORT

You will recall that at E(TP) on 30 June 1982 we asked officials to consider options for regulating BT's profitability under the new regime to be established under the Telecommunications Bill. On Alan Walters' suggestion I invited Professor Littlechild to review these options and make recommendations.

2 This he has now done. He recommends against either a maximum rate of return or an output related profits levy. Instead, he proposes a Local Tariff Reduction Scheme to ensure that charges for local calls and for renting a telephone fall in real terms - by adopting, he suggests, a formula based on "RPI minus X".

3 Professor Littlechild's central argument is that the exent to which regulation of BT will be necessary will be dependent on the extent of competition in telecommunications markets. If effective competition with BT could be achieved in all sectors of the market, controls on profits could be dispensed with entirely. However, BT is not likely to face serious competition in local services for the foreseeable future; hence the justification for some protection for subscribers in this limited area. At

the same time Professor Littlechild recommends Government action to increase competition in several significant areas - shared use and resale of capacity on leased lines, international liberalisation, ending the prime instrument monopoly, encouragement of network operators using alternative technologies to those used by BT and Mercury, and action within the context of the Telecommunications Bill to promote market entry (for example, there should be no discrimination in respect of access to the public network or in respect of charges for specific services).

4 Both Alan Walters and John Sparrow have welcomed the central thrust of Littlechild's approach - minimum regulation coupled with maximum competition - and I must say it reinforces all we have been seeking to do in telecommunications since July 1980. The focussing of controls on charges for local services where BT's monopoly is least open to competition is logical and presentationally attractive. The real price objective scheme is very similar to what we had in mind at the time of the Buzby bond and makes least administrative demands.

5 We must now decide on the publication of the Report and the Govenment response in light of the serious difficulties which Ministers are facing in Standing Committee. Progress on the Bill has been very slow. Our supporters have been outspokenly critical of our apparent inability to lift the restrictions inhibiting genuine competition to BT. They also remain anxious

about the implications of privatisation for services in the rural areas. Both sides of the Committee have made it clear that they will block progress on Clause 3 of the Bill until they have seen Littlechild. We have now spent over 80 hours in Committee and are nearing a guillotine.

6 To win the wholehearted support of our side of the Committee, we will have to come clean and make as positive a statement as we can on the totality of the Littlechild recommendations outlined in the paragraph above. Outside the Bill, we have been making good progress on further stages of liberalisation; I am confident we can meet many of the specific recommendations made by Littlechild.

7 BT's introduction of a new plug and socket programme makes it practicable to unwind the prime instrument monopoly on a step by step basis. We have already planned for the liberalisation of the maintenance monopoly on digital SPC PABXs. We are now working on a scheme to extend this to all call routing apparatus. The Department's study on Mercury's case for international switching is nearing completion. Professor Beesley recommended resale of leased circuits two years ago. Our VANs general licence moved a long way in this direction; we are now in a position to contemplate the next logical step.

8 There is one major recommendation of Littlechild's we cannot accept - namely a direct subsidy for social or uneconomic

services. Sir George Jefferson himself has turned this approach down and I think we can adequately cover BT by requiring all licensed public telecommunications systems operators to pay BT an access charge for the privilege of interconnection to the public switched network. Mercury have already agreed such an access charge with BT.

9 I recognise that colleagues will wish in due course to consider the implications of a specific price formula, but meanwhile I would like Kenneth Baker to publish the Littlechild Report and make a statement on the lines of the attached draft on Monday 7 February.

10 I am copying this to Willie Whitelaw, Francis Pym, Geoffrey Howe, John Biffen, Arthur Cockfield, John Sparrow and Sir Robert Armstrong.

PJ

P J

3 February 1983

Department of Industry
Ashdown House
123 Victoria Street

DRAFT STATEMENT

TELECOMMUNICATIONS REGULATION

1. With permission Mr Speaker I will make a statement about telecommunications policy.

2. It is the Government's aim that after privatisation, BT should be able to develop and diversify in a dynamic manner not only in the area of existing telecommunications services but also in the new information technology systems and services, on a world-wide basis. This will be good for the customer, the country, investors, BT and its staff. Equally the Government recognises that there is public concern that there should be no opportunity for BT plc to fix excessive charges to customers in the areas where it has a virtual monopoly for the time being and where thererfore users of telecommunications services do not have a choice of supplier. To this end my Rt Hon Friend the Secretary of State announced at the Second Reading of the Telecommunications Bill the appointment of Professor Stephen Littlechild of Birmingham University to carry out a study of these issues. Professor Littechild's report is being published today and copies are available in the Vote Office. The

M76AAA

Government is grateful to Professor Littlechild for undertaking this important task.

3. Professor Littlechild has made 2 major recommendations concerning the price regime after privatisation and the extent of competition. As regards pricing policy, he recommends that BT plc should be obliged for 5 years to keep any increase in its prices for domestic rentals and local calls and other services of particular concern taken together below the increase in the RPI. The Government accepts this approach but will want to give further consideration to the range of services to be included within the price limitation for example whether to include installation charges and charges for trunk calls. BT will be obliged to observe the arrangement finally determined and the powers of the DG of Telecommunications under the Bill are adequate to ensure that it is complied with. The aim of these arrangements will be to ensure a continuing reduction in the real cost of telephone services to the consumer across the country.

4. Professor Littlechild also considers that there need be no more onerous regulation but he recommends a substantial increase in competition in telecommunications. The Government has been progressively introducing competition as quickly as possible. In response to Professor Littlechild and in continuation of this process I can now announce further initiatives to promote

competition.

5. First, customers who have standard BT sockets will be free to purchase from any supplier the first telephone, connected to direct exchange lines. All apparatus will have to be approved for connection. I have asked BT to accelerate its programme of fitting standard sockets and my aim is that by 31 December 1984 this choice will be available to customers who want to exercise it. Thus the prime instrument monopoly will then be at an end.

This is agreed with PM MCS 4/2

6. Second, over a period of 4 years maintenance of all new call routing apparatus will be opened up to competition by persons approved by the Secretary of State. BT themselves will remain free to offer a maintenance service but on a fair competitive basis. I intend to introduce shortly amendments to the Telecommunications Bill to provide for licensing of those maintaining call routing apparatus. I will also be consulting BT, the industry and other interested parties on the phasing in of these arrangements.

7. Third, the Government accepts that the current restriction on Mercury's supply of international services should be eased. This will require discussions with other Governments. A study on the provision of international services is nearing completion and after consultation with all interested parties, I will make a further

statement.

8. Fourth, the Government accepts the principle of reducing restrictions on resale of capacity on private telecommunication circuits leased from BT and other public telecommunicating operators, but I recognise that this could have considerable implications for BT's revenue. I will want to consider the terms and timing of introducing any change after consultation with BT and other operators.

9. Fifth, the Government believes that competing licensed networks should have the right to interconnect on appropriate terms with BT's and Hull's networks. But in return BT must have the right to charge such networks as Mercury, Hull and the 2 cellular radiophone networks access fees on a non-discriminatory basis which will include a contribution towards the cost of providing the national asset of countrywide local networks. BT's own trunk and international divisions should also be subject to access fees on the same basis . These access fees will generate a significant revenue for BT to cover emergency 999 services, which are free and any losses incurred on call boxes and other services particularly those in remote and rural areas. The access fees will safeguard the continued provision of these services and the universal service, without subsidy from the taxpayer.

10. The Government recognises the importance to the national economy of BT's vital role in telecommunications. We are phasing in these new measures of competition in step with progress towards moving BT out of the public sector and out of the present web of Government controls. This is an expanding and rapidly changing market, and the greatest benefits to Britain, the consumer and the telecommunications industry will come from fuller and fairer competition. The arrangements I have announced today will achieve this.

CONFIDENTIAL

JH 776

PA

Prime Minister

This minute goes wider than the subject of this particular meeting but sets out the full proposal

Are you content that the Littlechild report should be published and that Mr. Baker should make the attached statement? (I find the statement clearer than the covering minute!)

FER 2.2.

PRIME MINISTER

TELECOMMUNICATIONS BILL: LITTLECHILD REPORT

You will recall that at E(TP) on 30 June 1982 we asked officials to consider options for regulating BT's profitability under the new regime to be established under the Telecommunications Bill. On Alan Walters' suggestion I invited Professor Littlechild to review these options and make recommendations.

2 This he has now done. He recommends against either a maximum rate of return or an output related profits levy. Instead, he proposes a Local Tariff Reduction Scheme to ensure that charges for local calls and for renting a telephone fall in real terms - by adopting, he suggests, a formula based on "RPI minus X".

3 Professor Littlechild's central argument is that the exent to which regulation of BT will be necessary will be dependent on the extent of competition in telecommunications markets. If effective competition with BT could be achieved in all sectors of the market, controls on profits could be dispensed with entirely. However, BT is not likely to face serious competition in local services for the foreseeable future; hence the justification for some protection for subscribers in this limited area. At

the same time Professor Littlechild recommends Government action to increase competition in several significant areas - shared use and resale of capacity on leased lines, international liberalisation, ending the prime instrument monopoly, encouragement of network operators using alternative technologies to those used by BT and Mercury, and action within the context of the Telecommunications Bill to promote market entry (for example, there should be no discrimination in respect of access to the public network or in respect of charges for specific services).

4 Both Alan Walters and John Sparrow have welcomed the central thrust of Littlechild's approach - minimum regulation coupled with maximum competition - and I must say it reinforces all we have been seeking to do in telecommunications since July 1980. The focussing of controls on charges for local services where BT's monopoly is least open to competition is logical and presentationally attractive. The real price objective scheme is very similar to what we had in mind at the time of the Buzby bond and makes least administrative demands.

5 We must now decide on the publication of the Report and the Govenment response in light of the serious difficulties which Ministers are facing in Standing Committee. Progress on the Bill has been very slow. Our supporters have been outspokenly critical of our apparent inability to lift the restrictions inhibiting genuine competition to BT. They also remain anxious

about the implications of privatisation for services in the rural areas. Both sides of the Committee have made it clear that they will block progress on Clause 3 of the Bill until they have seen Littlechild. We have now spent over 80 hours in Committee and are nearing a guillotine.

6 To win the wholehearted support of our side of the Committee, we will have to come clean and make as positive a statement as we can on the totality of the Littlechild recommendations outlined in the paragraph above. Outside the Bill, we have been making good progress on further stages of liberalisation; I am confident we can meet many of the specific recommendations made by Littlechild.

7 BT's introduction of a new plug and socket programme makes it practicable to unwind the prime instrument monopoly on a step by step basis. We have already planned for the liberalisation of the maintenance monopoly on digital SPC PABXs. We are now working on a scheme to extend this to all call routing apparatus. The Department's study on Mercury's case for international switching is nearing completion. Professor Beesley recommended resale of leased circuits two years ago. Our VANs general licence moved a long way in this direction; we are now in a position to contemplate the next logical step.

8 There is one major recommendation of Littlechild's we cannot accept - namely a direct subsidy for social or uneconomic

services. Sir George Jefferson himself has turned this approach down and I think we can adequately cover BT by requiring all licensed public telecommunications systems operators to pay BT an access charge for the privilege of interconnection to the public switched network. Mercury have already agreed such an access charge with BT.

9 Without pre-empting the more detailed discussions I will need to have with BT and colleagues in E(TP) on the price formula and on the phasing in of competition, I would like Kenneth Baker to publish the Littlechild Report and make a statement (on the lines of the attached draft which is still being discussed with BT) not later than Tuesday 8 February.

10 I am copying this to Willie Whitelaw, Francis Pym, Geoffrey Howe, John Biffen, Arthur Cockfield, John Sparrow and Sir Robert Armstrong.

J.P. Spencer

M. PATRICK JENKIN
(Approved by the Secretary of State and signed in his absence)

2 February 1983

Department of Industry

DRAFT STATEMENT

TELECOMMUNICATIONS REGULATION

1. With permission Mr Speaker I wish to make a statement about telecommunications policy.

2. The Government is progressively introducing competition so that consumers and other users of telecommunications will have a choice of supplier. However, BT will continue to be the dominant supplier of services for some time and the Government is concerned that while this remains the case there should be no opportunity for BT to fix excessive charges to consumers where it has a virtual monopoly. To this end my Rt Hon Friend the Secretary of State announced at the Second Reading of the Telecommunications Bill the appointment of Professor Steven Littlechild of Birmingham University to carry out a study of these issues. Professor Littechild's report is being published today and copies are available in the Vote Office. The Government is grateful to Professor Littlechild for undertaking this important task.

3. Professor Littlechild has made 2 major recommendations concerning the price regime after privatisation and the extent of competition. As regards pricing policy, he recommends that BT plc should be obliged for 5 years to keep any increase in its prices for domestic rentals and local calls and other services of particular concern taken together below the increase in the RPI. The Government accepts this approach but will want to consider in particular whether it should apply to a wider range of services for example by including installation charges and charges for trunk calls. In its licence BT will be obliged to observe this arrangement and the DG of Telecommunications will have powers under the Bill to ensure that it is observed. This arrangement will ensure that privatisation will lead to a reduction in the real cost of telephone services to the consumer across the country. This price limitation is focussed on those services where BT's monopoly is least subject to competition. Otherwise BT will be free to develop and diversify in a dynamic manner to provide cost-effective and competitive information systems and services on a world-wide basis.

4. Professor Littlechild also recommends a substantial increase in competition in telecommunications. In response I can now announce five new initiatives to promote competition.

5. First, customers who have standard sockets fitted by BT will be free to purchase from any supplier the first telephone, connected to direct exchange lines. This will end the prime instrument monopoly. All apparatus will have to be approved for connection. I will consult the manufacturing industry about the timing of this change but I have asked BT to accelerate its programme of fitting standard sockets and my aim is that by 1 June 1984 this choice will be available to customers who want to exercise it.

6. Second, maintenance of all new call routing apparatus will be opened up to competition by persons approved by the Secretary of State. I intend to introduce shortly amendments to the Telecommunications Bill to provide for the licensing of those maintaining call routing apparatus. These new arrangements for maintenance will come into force after the appointed day when details of licensing have been determined in consultation with all interested parties.

7. Third, the Government accepts the principle of easing the current restrictions on competition in the supply of international services. This will require discussions with

other Governments. A study on Mercury's position is nearing completion and after this I will consult all interested parties to determine a date when Mercury will be allowed to supply switched international services.

8. Fourth, the Government accepts the principle of ending the restrictions on resale of capacity on private telecommunication circuits leased from BT, but I recognise that this could have considerable implications for BT's revenue and I will want to decide the terms and timing of introducing any change after consultation with BT.

9. Fifth, the Government believes that competing networks should have the right to interconnect with BT's networks. But in return BT must have the right to charge such networks as Mercury, Hull and the 2 cellular radiophone networks as well as any future resale operators access fees on a non-discriminatory basis to contribute towards the cost of providing the national asset of countrywide local networks. BT's own trunk and international divisions should also be subject to the same access fee. These access fees will generate a significant revenue for BT to cover emergency 999 services, which are free and any losses incurred on call boxes and other services particularly those in remote and rural areas. The access fee will secure the provision of the universal service, including the social obligations without subsidy from the taxpayer.

10. The Government recognises the importance to the national economy of BT's vital role in telecommunications, but this is an expanding and rapidly changing market, and the greatest benefits to Britain, the consumer and the telecommunications industry will come from fuller and fairer competition. The arrangements I have announced today will achieve this.

CONFIDENTIAL

DEPARTMENT OF INDUSTRY
ASHDOWN HOUSE
123 VICTORIA STREET
LONDON SW1E 6RB
TELEPHONE DIRECT LINE 01-212 3301
SWITCHBOARD 01-212 7676

JF2579
Secretary of State for Industry

1 February 1983

The Rt Hon Lord Cockfield
Secretary of State for Trade
Department of Trade
1 Victoria Street
LONDON
SW1H 0ET

Prime Minister (2)

To see X

MCS 1/2

Dear Arthur,

You and Leon Brittan wrote to me on 11 and 12 January respectively with comments on my proposal that British Telecom (BT) be allowed to bid for International Airadio Ltd (IAL). Notwithstanding my views, you both felt that the balance of arguments lay against the proposal, for reasons including the differences in nature between the two enterprises, the fact that the acquisition would make BT still bigger and so more difficult to sell, and of course the fact that the acquisition would at least for the time being have left IAL within the public sector. I understand these arguments, but I do not entirely accept the conclusion you both draw from them. I would in particular not agree that BT's management, if a BT bid were successful, would be unacceptably diverted from its main task, given the strength of IAL's existing management team.

2 The situation, as you will know, has now changed in that BT want to make a joint bid with Racal. I attach a copy of a letter from Sir George Jefferson dated 28 January asking "in the next two or three days" for authority to make a bid. I should like to give him that authority. I expect to put proposals to E(TP) very shortly involving a significant opening up of BT's monopoly and an element of regulation in the interests of the consumer that BT will find unpalatable: permitting BT and Racal to make this bid would give BT's top management the spur and encouragement they need to continue to work vigorously to make this the really successful example of privatisation we all want. I do hope that on reflection you and colleagues can agree. One feature of the proposal in its present form is of course that it would take IAL out of the public sector.

3 I am copying this letter and enclosure to the members of E(NI), Sir Robert Armstrong and John Sparrow.

Yours ever
Patrick

Post & Tels:
Future of the
Post Office, pt 6.

cc JV

British TELECOM

British Telecommunications
2-12 Gresham Street
LONDON
EC2V 7AG

Telephone
National 01-432 4020
International + 44 1 432 4020

Telex 883051

Prestel Page 383

from the Chairman
Sir George Jefferson CBE

IN STRICTEST CONFIDENCE

RECEIVED 28 JAN SECRETARY OF STATE FOR INDUSTRY

The Rt Hon Patrick Jenkin MP
Secretary of State for Industry
Ashdown House
123 Victoria Street
LONDON
SW1E 6RB

28 January 1983

Mr Sharp
PLEASE BY: ASAP please
COPIES TO
PS/KB
PS/JB
PS/Sec
Mr Croft
Mr Solomon
Mr Ellison

Dear Patrick

IAL

Following our discussion yesterday, I said I would let you have an outline of our current thinking on the possibility of a joint purchase, with Racal, of IAL, and the industrial logic which we believe underlies it.

In my letter to you of 17 December I set out, in broad terms, the reasons for believing that a British Telecom purchase of IAL would make good sense for both companies. A copy of my letter is attached for ease of reference.

I believe that a joint purchase with Racal would potentially increase those benefits, while at the same time remove some of the objections to the original proposal.

Let me first set out the kind of arrangement which Racal and ourselves envisage, subject to closer study and discussion between us. We have in mind a joint 50/50 ownership. However, I should stress that we would wish to keep IAL together, as a separate operating subsidiary, and specifically not break it up and merge the different parts in our own businesses.

However, it may well be that the balance of IAL's current activities is ready for change. Although they have hitherto operated predominantly in the aviation market, their communications activities, although still of lesser importance, have now begun to develop significantly. Moreover, their profits from the aviation business are declining in real terms. Given, inter alia, the difficulties of the aviation market, I believe that the present management of IAL would support the view that that company will need to develop much more into the telecommunications and related markets if it is to grow and maintain profitability. An association with the expertise, experience and resources of two companies like British

/Telecom

Telecom and Racal - the former with its recognised skill in telecommunications technology, the latter with its management and financial skills and entrepreneurial drive - would greatly aid IAL through what might otherwise be a difficult transitional period, and help it to develop in new fields. I know that Sir John King would endorse the industrial logic of that approach.

Racal and British Telecom themselves have largely complementary skills. British Telecom in research, developing and operating telecommunications systems - but largely within the UK. Racal is a world leader in the supply of radio and data communication equipment, and over 72% of its sales are to overseas countries. IAL's particular ability is the operation of electronics systems in overseas countries.

One of the most important developments in telecommunications is cellular radio. In the United Kingdom, Racal has been chosen by the Government as the operator of a second radiotelephone system, in competition with a British Telecom-Securicor consortium. Cellular radio has, however, immense potential beyond the relatively narrow field of the car-phone services currently in question. It is likely to be of increasing significance in the development of local, as well as national, communications, particularly in rural areas.

The combined abilities of British Telecom and Racal, using IAL as an operating company in overseas countries, could give the UK an opportunity to become a world force in the development of cellular radio. It is difficult to see in what other way, or by what other means, the UK can establish a significant foothold in this developing market. IAL's presence, and experience of establishing operations, in overseas countries would be particularly valuable in this context, since it would short-circuit the need for Racal or British Telecom to develop this expertise.

Another area in which the combination of skills offered by Racal, British Telecom and IAL could be of great benefit to the UK is the development and operation of cable systems in overseas markets. Racal is likely to become more active in this field in the UK and, through the Racal Oak company, in the USA. IAL could greatly benefit in this field from a combination of Racal's and British Telecom's expertise.

We would of course, compete vigorously in the cellular radio market in the UK. I do not think this is in any way incompatible with co-operation in overseas markets, particularly as we are both being required to adopt the same technical system. We will therefore essentially be competing for market share through tariffing and marketing initiatives, rather than through any fundamental difference in the type of service being offered. There are plenty of examples of competitors in domestic markets co-operating,

/for the

for the sake of the UK, in overseas countries. Moreover, in our case, the use of a separate entity - IAL - for our co-operation in overseas markets would enable us to maintain separation in the domestic market and ensure that a cosy relationship did not develop there.

These are necessarily initial thoughts. We will clearly need to have much more detailed discussions, and a much closer examination of IAL's books. We believe, however, that the arrangements which I have outlined in this letter provide a basis for an arrangement of great potential benefit to the parties concerned, and to the UK. If we are to proceed, it is now of the greatest urgency that we should be given the authority to do so in the next two or three days.

Sir Ernest Harrison has seen this letter, and fully endorses the content.

Yours sincerely

George

SIR GEORGE JEFFERSON

cc JV

(2)

Prime Minister

Patrick Jenkin is hoping to have 10-15 minutes with you, tomorrow or Wednesday, to discuss the Parliamentary handling of this issue. He will be looking out for you after the Vote at 10.1

MS

CABINET OFFICE
Central Policy Review Staff
70 Whitehall, London SW1A 2AS Telephone 01-233 7765

From: John Sparrow
CONFIDENTIAL

Qa 06237

28 January 1983

* you may like to see the attached letter by Alan Walters on the subject.

The Rt Hon Patrick Jenkin MP
Department of Industry
ASHDOWN HOUSE
S W 1

Dear Patrick,

BT Regulation - Littlechild Report

I have now read Professor Littlechild's report which provides an excellent survey of a difficult issue. I am in broad agreement with his conclusions. In particular, the MRR, output-related tax and ceiling rate of return schemes all appear to have disadvantages which rule them out.

Suspect it is an attempted bounce.

That leaves no explicit constraints (NEC) and Littlechild's suggested local tariff reduction (LTR) as the only runners. The report highlights the advantages of NEC on four out of five criteria but on the monopoly issue quite justifiably voices fears that NEC may provide inadequate protection, particularly for domestic and small business subscribers. It is tempting to argue that prevention of monopoly abuse could be handled by existing mechanisms in respect of BT as it is for other private sector monopolies, but I have to admit that I do not find the case convincing. LTR is an attempt to deal with this problem and in effect offers NEC, constrained only by a measure to hold local tariff increases at or below the rate of inflation. There is a danger that this will exacerbate the problem of cross-subsidisation within BT, in that the rate of return on local services is already low but it seems reasonable to believe that there is sufficient scope on the cost side to make LTR attractive both in terms of monopoly control and efficiency promotion. I am not sure that it would not be more clearly understood by customers and investors if it were expressed as a limitation on price

MLS 31/1

increases in nominal terms, but a view on that would amount to a view on inflation rates which may be too difficult to foretell. A further possibility, which I commend, would be to express the maximum increase as a proportion of the increase in the RPI rather than at an absolute margin below the rate of increase in the RPI.

This would lead to the adoption in principle of the Littlechild proposals, tilted as far as possible towards NEC. This might be done by -

(a) removing all constraints to entry, to encourage competition. Littlechild recommends relaxation of the monopoly to permit resale of capacity on leased lines, international liberalisation and ending the prime instrument monopoly. I agree with these. I also consider that the possibility of introducing competition for voice telephony in cable networks should be looked at again. To limit this to Mercury will restrict competition unduly;

(b) ensuring against anti-competitive practices and monopoly abuses in the short term by providing for references to the MMC. The Bill and draft licences should provide for the Director-General of Telecommunications to acquire sufficient information to track the behaviour of BT. Consideration will need to be given to speeding up MMC references and strengthening the Commission to deal effectively with any complaints;

(c) providing some safeguard in the short term, say five years, for local subscribers, along the lines discussed above.

Although BT will have an effective monopoly over trunk and international operations while competition develops, it is unlikely that they will abuse this position for fear of being referred to the MMC or of Government intervention. However, it is important to encourage competition to develop, as it is to remove legislative and other barriers, and this will require further thought.

I am sending copies of this letter to the Prime Minister, the Chancellor of the Exchequer, Alan Walters and Sir Robert Armstrong.

Yours sincerely,

John.

Post & Telecom: Future: pt 6

MR. SCHOLAR

10 DOWNING STREET

The Right Honourable
Patrick Jenkin, MP,
Department of Industry,
Ashdown House,
123 Victoria Street,
London, SW1.

27 January 1983

Dear Secretary of State,

LITTLECHILD REPORT

In my view Stephen Littlechild has done a good job. His analytical work is sound, and he has brought to bear a great deal of experience from America and elsewhere. Yet the discussion is incisive and well directed towards the conclusions on policy. I think it is as good an account of the relative advantages of regulatory systems as we are ever likely to get. (I would describe it as masterly, were it not that I feel inhibited from heaping such fulsome praise on my old student!)

His criticism of the maximum rate of return method is quite devastating. It goes far beyond the many inherent faults which I, in my amateurish way, mentioned during last summer. It amply demonstrates the wisdom of the rethinking which has taken place over the last few months. Broadly speaking, if the maximum rate of return is effective it is bad; if it is ineffective then it is otiose.

His analysis of the Output Related Profits Levy covered a lot of ground in such a short time. (I must confess that I did not believe that it was a new idea when I put it forward! I thought that someone surely must have thought of this sort of control before.) But it is clearly a somewhat complex system and needs much more research before it is inflicted on suffering humanity. I agree, however, with Littlechild's finding that it scores quite well, and certainly much superior to the various versions of maximum rate of return, on all criteria except "understandability" to the City and the investor. I agree entirely with that judgement. But I think the ORPL has done its job in inducing further thought on the regulation system and in giving rise to the much improved present proposals.

I did take the opportunity to discuss with Littlechild the local tariff reduction scheme, before he completed his report. It meets most of our desiderata, and I think would be politically popular. There is, however, some additional work that needs to be carried out. It may be better, for example, to state the tariff reduction in nominal terms rather than in real terms; or it may be a good idea to state it both in nominal and real terms, taking whichever is the lower as the binding constraint. These sorts of possibilities,

/as well as

as well as the actual numbers, need further exploration. Similarly, the requirement to supply services, such as call boxes and rural services, needs to be developed in detail. A policing method needs also to be outlined. But within the general framework I can see no difficulty in settling such matters. I suspect, however, that colleagues on E will want to have a fairly detailed account of both the promises on tariffs and the preservation of services.

I am copying this letter to the Chancellor of the Exchequer, John Sparrow (CPRS) and Michael Scholar here.

Yours ever

Alan Walters

ALAN WALTERS

Post & telecommns

Prime Minister (2)

Both Lord Cockfield and Mr Brittan are against allowing BT to buy IAL.

MCS 15/1

Treasury Chambers, Parliament Street, SW1P 3AG

Rt Hon Patrick Jenkin MP
Secretary of State
Department of Industry
Ashdown House
123 Victoria Street
London SW1E 6RB

12 January 1983

Dear Patrick,

SALE OF INTERNATIONAL AIR RADIO

Thank you for sending me a copy of your letter to Arthur Cockfield of 6 January reopening the case for BT being allowed to buy IAL.

In Box

It seems to me that with a company as diverse as IAL industrial logic will probably support most of the bids for it. I would myself be wary about BT being allowed to swallow every company it takes a fancy to. Like AT & T it is only at the very beginning of getting away from its philosophy of "one company, one policy, universal service". A company as centralised and monolithic as BT currently is, is hardly likely to provide the best conditions for the diversity and enterprise of an IAL to flourish in.

Meanwhile the priority is for BT's management to concentrate on getting its own house in order, and, as we discussed recently at E(NI), this is going to take all the time it has.

I have no doubt that BT has and will continue to have the cash with which to outbid everyone else in this sort of instance but that does not take away from thefact that there will be no public expenditure benefit from a sale by BA to BT. More importantly, IAL, which clearly ought to be detached from the financial problems of its parent and free to compete in the private sector would have to remain in the public at least until after the next General Election.

For all these reasons I believe it would be wrong to reverse the view already taken against allowing BT or any other public sector body to bid for IAL.

Yours ever
Leon

LEON BRITTAN

CONFIDENTIAL

Post & Tels, Future of the Post Office, Pt 6

DEPARTMENT OF TRADE 1 VICTORIA STREET LONDON SW1H 0ET Telephone 01-215 7877

cc JV

Prime Minister

Lord Cockfield argues against Patrick Jenkin's suggestion that BT should be allowed to bid for International Aeradio.

From the Secretary of State

The Rt Hon Patrick Jenkin MP
Secretary of State for Industry
Department of Industry
Ashdown House
123 Victoria Street
London
SW1E 6RB

11th January 1983

WR 12/1

Dear Patrick,

INTERNATIONAL AERADIO

You wrote to me on 6 January suggesting that British Telecom (BT) should, after all, be allowed to bid for International Aeradio (IAL). I still do not feel that we should allow such a bid to be made.

I would not think it right to extend the frontiers and activities of a nationalised industry, even though it was the firm intention to privatise that industry in due course. Even assuming that no delay occurred in the plans to privatise BT - and there are many precedents to the contrary - I would have thought that by increasing the "ante" it would make privatisation more difficult: and that ownership of IAL would divert the attention of BT's top management at a time when they need to concentrate every effort in putting their own house in order as a prelude to privatisation.

Additionally, it does seem to me to be inherently absurd that BA should be expected to divest themselves of IAL as part of the process of privatisation, only to find IAL snapped up by another nationalised industry on the argument that it is consistent with privatisation of that organisation.

The effect on the EFL is primarily a matter for the Treasury, although it could be argued that BT ought never to have been allowed so big an EFL in the first place. Here again it seems to me to be a bizarre situation that BA should be selling IAL to avoid their having to ask for an inflated EFL, whilst BT should then be permitted to buy IAL because they were given an inflated EFL. This seems to me

From the Secretary of State

to place the quirks of book-keeping in a position of eminence they do not deserve.

I am copying this to recipients of your own letter.

Yours,
Arthur

LORD COCKFIELD

Post & Telecomms.

Future of

Prime Minister

CABINET OFFICE
Central Policy Review Staff
70 Whitehall, London SW1A 2AS Telephone 01-233 7765

From: John Sparrow

Qa 06213

CONFIDENTIAL

10 January 1983

The Rt Hon Patrick Jenkin MP
Department of Industry
ASHDOWN HOUSE
S W 1

Dear Patrick,

Telecommunications Bill

Over the last few weeks my staff have had discussions with your officials and with British Telecom and the Monopolies and Mergers Commission on certain aspects of the new framework that is being established for regulating BT.

On a few key issues I believe that further consideration is necessary before legislation and the framework are finalised.

Guidelines

Clause 3 of the Bill is fundamental to the development of telecommunications in the UK and to effective regulation of licensees. This clause sets out the guidelines which the Secretary of State and the Director General of Telecommunications shall take into account, and which the MMC shall have regard to, when considering licence conditions and amendments.

I am concerned that these guidelines, as drafted, do not take sufficiently into account the need to provide modern services, particularly in view of the rapid technological changes that are experienced in this industry. In order to ensure that modern services are provided, the rate of return on capital will need to be sufficiently large to attract capital and stimulate investment, so that the 'telecommunications services' referred to in Clause 3(i)(a) can be as up-to-date as the customer is prepared to pay for.

I am also concerned that sufficient incentive should be given to BT to improve its efficiency - in the interest of consumers. For some time, despite present efforts to introduce competition, BT will have a monopoly in most of its markets and will be able to pass on additional costs caused by inefficiency, restrictive working practices and poor management in the form of higher prices. BT management needs to be given some incentive to remove these inefficiencies through increased financial reward to shareholders (and possibly also to themselves by linking remuneration to performance).

Although the guidelines contain (in Clause 3(i)(c)) the requirement to have regard to 'the desirability of promoting the interests of consumers', I consider that 'the desirability of promoting efficiency' should be specifically spelt out. The advice currently being sought from Professor Littlechild will have a direct bearing on the form of regulation, and I would suggest that the determination of the mechanism for promoting efficiency and the precise wording of Clause 3 be deferred until his report has been considered by Ministers.

Right of appeal to the MMC

Where the Director General of Telecommunications wishes to amend a licence but cannot obtain the agreement of the licensee, he is empowered to refer the matter to the MMC. However, licensees do not appear to have similar rights where in their view licence conditions become too onerous, with the passing of time, and where they cannot persuade the Director General that modification of the licence is necessary.

I consider that licensees should have the right to appeal to the MMC in such instances.

I am sending copies of this letter to the Prime Minister, other members of E(TP), and to Sir Robert Armstrong.

Yours sincerely,

John.

John Sparrow

Post & Tels, Future of the Post Office, A6

CONFIDENTIAL

Prime Minister (2)

MCS 7/1

DEPARTMENT OF INDUSTRY
ASHDOWN HOUSE
123 VICTORIA STREET
LONDON SW1E 6RB
TELEPHONE DIRECT LINE 01-212 3301
SWITCHBOARD 01-212 7676

JF2359
Secretary of State for Industry

6 January 1983

The Rt Hon Lord Cockfield
Secretary of State for Trade
Department of Trade
1 Victoria Street
LONDON
SW1H 0ET

Dear Arthur,

I attach a self-explanatory letter from Sir George Jefferson about International Air Radio.

2 You will remember that when this was discussed in E(NI) last July the matter was not finally concluded against BT but it was left that if BT could make an overwhelming case for buying IAR they would come back to Ministers at a later stage. Since then, we have introduced the Bill to privatize BT and the legislation is currently in Standing Committee. You will know that it is our intention, as soon as possible after the next election, to offer shares in BT to the public with the intention that the Government's holding should become a minority one. While the decision to privatize BT was taken shortly before the E(NI) dicussion on IAR, progress with the legislation since then seems to me to put BT's interest in IAR in a more clearly private sector context and although I realize it is somewhat late in the day, I would hope very much that you would be able to let BT have the prospectus and make a bid which would be considered along with the others you are receiving.

3 For me, a purchase by BT would make a good deal of industrial logic. It could be used as a lever to force more competition both internationally and internally on BT, something that we are all very anxious to see. It is also worth pointing out that an acquisition by BT this year would help to reduce the large BT undershoot on their EFL though I would not regard this last point as a major argument in their favour.

/4 ..

CONFIDENTIAL

4 I am copying this letter to the members of E(NI) and Sir Robert Armstrong.

Yours ever

Patrick

British TELECOM

British Telecommunications
2-12 Gresham Street
LONDON
EC2V 7AG

Telephone
National 01-432 4020
International + 44 1 432 4020

Telex 883051

Prestel Page 383

from the Chairman
Sir George Jefferson CBE

IN STRICTEST CONFIDENCE

The Rt Hon Patrick Jenkin MP
Secretary of State for Industry
Ashdown House
123 Victoria Street
LONDON
SW1E 6RB

Previous papers see - ICB 93 1982

Mr Wimbott
COPIES TO
PS/Mins
PS/Sec
Mr Sterling
Mr Croft
Mr Isell
Mr Solomon
Mr Sharp
6/1/83

17 December 1982

RECEIVED
21 DEC
SECRETARY OF STATE FOR INDUSTRY'S OFFICE

Dear Patrick,

INTERNATIONAL AIR RADIO

I wrote to you in June this year expressing the interest of BT in having an opportunity to consider a bid to acquire International Air Radio, as a positive step towards the development of our ability to operate in an international telecommunications business environment.

The eventual outcome was that I was advised by Warburgs that they were not authorised to supply information to us, as the policy of the Government would not permit a sale to a public sector corporation. I did not wish to burden you with further pressure on this issue and I have therefore let the matter lie.

However, it is my understanding that various matters have complicated and delayed the issue of prospectus document until the New Year, and in the meantime the Government has confirmed its intention to privatise BT and currently has legislation before Parliament to give the necessary powers to effect that change.

It is against this background that I am raising this issue once more, since I believe that a BT acquisition of IAL would make considerable industrial logic for both companies.

BT has immense resources of skill and experience in Telecommunications, runs an international consultancy, and of course has major international communications links with every country in the world; however, it has little experience of operating and managing contracts within overseas countries. We believe that, given the right resources, considerable potential exists to develop business based on the design, installation and operation of systems overseas, thus not only selling services abroad, but also facilitating the sale of British telecommunication equipment and other British equipment in those markets. This would be

/similar to the

IN STRICTEST

similar to the kind of operations performed so successfully by British Aerospace in their field, and of which, as you know, I have considerable experience.

IAL, for their part, have the kind of overseas skills and experience which BT lacks, but do not have the technical and expertise and clout to back them in the field of telecommunications; and I believe it would be counter-productive for them to be closely associated with any individual supplier.

I am confident it is not only my view that a union with BT would make industrial sense; it is also Jim Utterson's and I am writing to you at this time with his knowledge and, I believe, encouragement.

It might be helpful if I were to give some idea of the practical arrangements we would have in mind.

We would not wish to absorb IAL into BT, since that would bbe counter-productive. Rather, we would see it as a subsidiary company, with BT probably having an ultimate holding of 51%, the balance either widely spread, or perhaps with a number of minority industrial partners - depending on the views of IAL itself and of course the interest of others.

Whilst it could be argued that it would be more logical, in some respects, for such an acquisition to take place after privatisation, there are not in practice many opportunities of the kind presented by the sale of IAL, and one has to take these when they arise.

Should the Government wish, it could make it a condition of our acquisition that in the event of BT not being privatised, for whatever reason, the Government would have the option - after say five years - of requiring BT to divest itself of the company.

You will recall that in my letter of 22 June, I referred to the fact that IAL handle a number of important and politically sensitive contracts in Saudi Arabia, associated with the MOD.

I think it highly possible that the Saudi Government and other such customers would strongly prefer BT ownnership to some other possible purchasers, and it is possible that this would be a helpful factor both to IAL and to MOD sales.

As a final point, you are aware that there are many people within BT who feel that privatisation is likely to lead to its decline and deterioration. Clearly, it is the Government's intention to introduce competition within the UK in most of the profitable areas of BT's activities. In leading this organisation through these turbulent times, I need to convince our staff, as intelligent people, that

/privatisation

privatisation will open new doors for BT to develop new markets for its telecommunications skills. Were the Board free - if it so decided - to seek to acquire IAL, it would give tangible evidence to counter some of the fears expressed by many staff and Unions at this time.

Naturally, if we received the go-ahead from you, the Board would wish to consider the case for acquiring IAL much more closely than has hitherto been possible. However, I believe that such an acquisition would be very likely to lead to a significant development of the UK's strength in the international telecommunications market.

May I therefore renew my plea that BT be permitted to examine the prospectus documents and, should it then so decide, submit, in consultation with your Department, a bid for IAL?

Yours sincerely

George

Post & Tels. Future of the Post Office, pt 6

CONFIDENTIAL

cc JV

Prime Minister (2)

MCS 22/12

Treasury Chambers, Parliament Street, SW1P 3AG

The Rt Hon Patrick Jenkin MP
Secretary of State
Department of Industry
Ashdown House
123 Victoria Street
London SW1E 6RB

22 December 1982

Dear Secretary of State

POSTAL PRICES

I very much share the concern that you express in your letter of 9 December that the Post Office should be led to bargain more responsibly on pay than the 5% settlement assumed in their tariff proposals.

Given that such a settlement is already allowed for in their calculations and that the likely overshoot of this years profit target may well work its way through into an easier financial position for next year than the Post Office are currently assuming, it may be necessary to take further steps closer to the time in order to ensure that the Post Office approaches its next wage negotiations against a background of taut financial discipline.

I am sure that you and Kenneth Baker will continue to press for tight pay bargaining, but exhortation may not be enough. Should POUNC propose that the Post Office defers or modifies its tariff proposals, we should consider sympathetically such a move - which would have the desirable effect of importing some financial stringency.

If they do not, then particularly if it becomes apparent that the Post Office position at the end of 1982-83 would allow for an even more generous pay settlement for 1983-84 than their present unacceptable 5%, we may have to consider what other steps we might need to take to underpin the message that you are already giving them that they should seek to settle at a level significantly below 5%.

On that understanding, I am content that, as you propose, the Post Office's tariff proposals should now be referred to POUNC.

I am copying this letter to the recipients of yours.

Yours sincerely

J.S. Grieve

for LEON BRITTAN
(Approved by the Chief Secretary)

Post & Telecomms

Future of Post office

pp. WM 31/12

Prime Minister

The note you asked for.

MT

WR 21/12

LIBERALISATION OF TELECOMMUNICATIONS: MR BUTCHER'S INTERVIEW ON RADIO 4

BACKGROUND NOTE

1. The two central complaints were:

a. that the fees for approval of apparatus were unreasonably high and would prevent small firms entering the market; and

b. that by being allowed to carry-out the approval tests, British Telecom was being put in a position where it could squeeze out its potential competition.

2. The testing of telecoms equipment is expensive because of capital costs and qualified engineering time spent on the task. BT has tended not to charge up to full costs. This fact is appreciated by the majority of manufacturers although there have been some complaints, notably from those smaller distributors who are hoping to supply apparatus manufactured overseas but who do not themselves possess substantial financial and engineering resources.

3. Applications are presently being received for approval of items of small telephone call routing apparatus, the test fees for which have been estimated at between £20,-30,000. Capital expenditure for test gear for this particular apparatus is over £160,000 and the microprocessor controlled apparatus needs a good deal of software testing expertise as well - and this is expensive. This 'high cost' has prompted the recent complaints. However, these fees do not appear to have discouraged small and medium sized firms since about 35-40% of the applications so far received are within that category.

4. When the liberalisation programme was announced in 1981, it was made clear that it would be phased over a three year period, to allow British manufacturers time to adapt to the new market conditions. Under these arrangements a new procedure is being developed for independent standard-writing, testing and approval of apparatus. This is already in operation for more straightforward apparatus. In order to bring the benefits of liberalisation to the user as soon as possible however, the Department of Industry has introduced several interim measures, such as that referred to above for call-routing apparatus, for approving a limited number of items of equipment. The only laboratories that are currently properly staffed and equipped to carry out the testing of complex telecoms equipment are those of British Telecom. But the schemes are run by the Department of Industry and testing procedures are monitored by DoI to ensure fair play.

LINE TO TAKE

I should be most concerned if I thought that small firms were not being allowed fair opportunity to compete in this important growth area. The Government's programme for the liberalisation of telecommunications has already allowed small firms to earn profits and create jobs in the telecoms industry and I expect to see this increase considerably as the programme rolls on. 35 to 40% of the applications for small call routing apparatus are from small firms who understand the reasons for testing costs.

Brite
JCB

10 DOWNING STREET

MR. MOUNT

British Telecom and the Monopolies and Mergers Commission

The Prime Minister has written on your note of 17 December "I take the view that denationalisation must not be jeopardised".

MCS

Review.

20 December 1982

c. CO DTemp. DTeng. DI CS-HMT DTrans DTrade DSC SO DEnv. HMT

File

CONFIDENTIAL

bc. F. Mount.

10 DOWNING STREET

From the Private Secretary

20 December 1982

Dear Jonathan,

BRITISH TELECOM AND THE MONOPOLIES AND MERGERS COMMISSION EFFICIENCY INVESTIGATION

The Prime Minister saw your Secretary of State's paper for E(NI) Committee, E(NI)(82)33, on this subject over the weekend.

She has commented as follows:

"I take the view that denationalisation must not be jeopardised".

I am sending a copy of this letter to the Private Secretaries to the other members of E(NI) and to Richard Hatfield (Cabinet Office).

Yours sincerely,

Michael Scholar

Jonathan Spencer, Esq.,
Department of Industry.

CONFIDENTIAL

I take the view that denationalisation must be jeopardised not.

Prime Minister

MCS 17/12

2

17 December 1982

Policy Unit

PRIME MINISTER

BRITISH TELECOM AND THE MONOPOLIES AND MERGERS COMMISSION

We are in a tangle. I suspect this is because we are trying to do two things at the same time when we ought to be doing only one.

Either we prepare to privatise British Telecom and use that stimulus to improve its efficiency.

Or we leave it in the hands of the state and send in the MMC.

Naturally, after privatisation if BT is still performing badly and abusing the monopoly powers it will still enjoy, then it would be right to send in the MMC.

But to send in the MMC now would be the very worst time, because the nature of those monopoly powers - their statutory underpinning, their relationship with Mercury etc - will be changing fast. Many of the MMC's recommendations would be out of date almost as soon as they were written. And it would be almost impossible to hypothesise about how a privatised BT would perform.

I think this is probably a stronger objection than the damage that an MMC report would do to the flotation or the amount of BT management time which it would consume.

An MMC report on the telephone service would make absorbing reading. But I don't think that now is the moment for one.

FM

FERDINAND MOUNT

MR MOUNT

cc Mr Scholar

MONOPOLIES AND MERGERS COMMISSION EFFICIENCY INVESTIGATION INTO BRITISH TELECOM

I do not think the Prime Minister will care very much for the attached paper for E(NI) next Wednesday. Mr Jenkin argues that the launching of the proposed MMC Investigation into BT will damage the prospects for flotation; and quotes the views of bankers in support. He concludes that we can leave it to BT to put their own house in order.

But the give-away is in paragraph 4: to remedy the existing serious deficiencies in BT would delay flotation for a substantial period, or lower the share price. So the DoI is now arguing what we have argued all along - that there is no point in privatising an inefficient monopoly: we must get it efficient first.

I suspect that when the Prime Minister sees this paper she will conclude that the MMC should go ahead, and flotation should be delayed. That may be right: but the Government has invested considerable political capital in privatising BT, and it is the major piece of legislation this session. There may be a middle course. MMC investigations are not black and white affairs, and the reference of BT to the MMC could perhaps restrict the extent of the inquiry in a way which would limit the damage to BT's market prospects.

The immediate question is what to do about the E(NI) discussion. The Prime Minister could Chair it herself; but it might be best to encourage E(NI) to do the necessary preparatory work, and to report the outcome to her. I understand that both the Chancellor and the Secretary of State for Trade are sceptical of DoI's case, and are being briefed to argue vigorously against it. If you agree, I will so suggest to Michael Scholar. Meanwhile I am sending him a copy of this note to keep him in the picture.

16 December 1982

010

CONFIDENTIAL

POST AND TELECOM

cc JV

DEPARTMENT OF INDUSTRY
ASHDOWN HOUSE
123 VICTORIA STREET
LONDON SW1E 6RB
TELEPHONE DIRECT LINE 01-212 3301
SWITCHBOARD 01-212 7676

JF2177
Secretary of State for Industry

9 December 1982

(2)

The Rt Hon Leon Brittan MP
Chief Secretary
HM Treasury
Treasury Chambers
Parliament Street
LONDON
SW1P 3AG

Prime Minister

3.5% increase in postage etc.

MCS 9/12

Dear Leon,

POSTAL TARIFF INCREASES

The Post Office has sought our approval to put to the Post Office Users' National Council proposals for tariff increases averaging 3.5%. They would take effect from 5 April 1983. The increases would entail 1p on a first class letter, but no increase on the basic rate second class letter, although there would be small increases averaging some 2% on the higher weight steps. There would be increases on inland parcels and on overseas mails averaging about 6% and 5% respectively.

2 The last increase, averaging about 9.3%, took place on 1 February 1982, and the current proposals are therefore well within the likely increase in the RPI between 1 February 1982 and 5 April 1983. The additional income arising from the increases would enable the Post Office to make a return of 2½% on turnover in 1983/84 and to meet its external financing limit of -£43m.

3 In order to meet its financial objectives with the package, the Post Office will require a productivity improvement of 2% in 1983/84, on top of increases of 3.3% in 1981/82 and 3.5% in 1982/83, together with a volume increase of 1% over and above the 2% forecast for 1982/83.

4 The Corporation is on target for its real unit cost objective in the mails area, although it may have some difficulty overall in meeting the target in the light of a shortfall in the counters area.

/5 On ..

CONFIDENTIAL

5 On pay the Post Office has assumed an increase of 5% in the next round. Kenneth Baker has told Mr Dearing that we regard this assumption as excessive and that somewhere in the region of 3½% would be more appropriate, and I shall be pressing this point during the run up to the postal pay negotiations.

6 I believe that the proposed tariff increases are reasonable and that the Post Office's achievement in confining them to 3.5% over a fourteen month period is commendable. Although the pay assumptions on which the proposals are based are higher than we would wish, the assumptions on increases in volume and productivity may be difficult to achieve without a great deal of effort on the Post Office's part. The proposed tariff increases do however represent a modest increase and I am minded to tell the Chairman that he is free to put the proposals to the Post Office Users' National Council.

7 Mr Dearing would like to put the proposals to the Users' Council by 1 January 1983 in order to give customers at least three months' notice. I should therefore be grateful for any comments as soon as possible.

8 Copies go to the Prime Minister, to members of E Committee, and to Sir Robert Armstrong.

Yours ever

Patrick

CONFIDENTIAL

PR

MR. SCHOLAR

BRITISH TELECOM: THE REGULATORY FRAMEWORK

We shall shortly be looking at the Littlechild report on possible regulatory systems for a privatised British Telecom. I expect that Littlechild will show that my suggested regulatory system, with the output-related profits tax and little or no regulation of costs, price etc, as desirable in many respects. It will promote the growth of output, encourage cuts in price, etc. Indeed the one criticism that Littlechild has brought to bear, namely that it would result in greater oscillations of output, can easily be countered by rebasing the output measure each year.

Nevertheless, notwithstanding all these great advantages, my scheme has a crucial - perhaps fatal - disadvantage. The City don't like it. The reasons for their dislike, whether irrational or rational, are largely immaterial. The merchant banks are influential with institutions and could put a blight on the marketability of the stock. I am persuaded therefore that, if City opposition persists, then we should drop any suggestion of an output-related profits tax.

The output-related profit tax, however, has largely served its purpose. It has induced substantial, if not revolutionary, changes in the regime being promoted by the Department of Industry. They have dropped their original idea of a maximum profits tax, with its 100% marginal rate, and they are now very much more concerned to minimise the regulatory impact of their proposed new agency. I still believe there is considerable danger of over-regulation, however, even with the present ideas of the Department of Industry.

I have not been informed of the Department of Industry's timetable, for deciding on these issues. I know, however, that Littlechild is proposing to report before the Christmas break. Presumably the decisions will have to be presented to E Committee during the course of January.

6 December 1982

ALAN WALTERS

CONFIDENTIAL

CONFIDENTIAL

JH 452

cc JV
Post & Telecom

Prime Minister (2)

MRS 6/12

DEPARTMENT OF INDUSTRY
ASHDOWN HOUSE
123 VICTORIA STREET
LONDON SW1E 6RB
TELEPHONE DIRECT LINE 01-212 3301
SWITCHBOARD 01-212 7676

Secretary of State for Industry

6 December 1982

Rt Hon Leon Brittan MP
Chief Secretary
HM Treasury
Parliament Street
London SW1

Dear Chief Secretary,

BRITISH TELECOM: 1982-83 UNDERSHOOT

Thank you for your letter of 29 November.

2 I attach a table giving the BT explanation of the forecast underspend of £520m.

3 We did, of course, already know that the underspend would be of the order of £320m and suspected it might be higher, but I do agree that the shortfall on the BT estimate is now pretty glaring.

4 You mentioned that until recently you were prepared to accept that the underspend was due to creditable factors such as lower prices and some progress in making real cost savings. I would urge you to agree that that is no less true now and that a number of the items in the list are very much to BT's credit - eg securing lower prices from their suppliers, and making savings on accommodation. Other items are outwith BT's control - eg reduced demand due to the recession. On the other hand, BT themselves are most disturbed at the late delivery of exchange equipment in view of the priority they give to the need to improve the network and they are discussing with suppliers why the delays have arisen and how to avoid them in future.

5 For the rest there are two separate respects in which the BT performance is seriously deficient. First, they still do not possess adequate accounting systems to assess what is happening within the business - BT have made no secret with us of their deficiencies here and of the fact that despite all their efforts it will take years rather than months to put this to rights. We have a draft of Coopers & Lybrand's long form report prepared in the context of the bond issue which demonstrates how much remains to be done; and Sir George Jefferson has just told me that he is

seeking to accelerate the development of better systems.

6 Second, BT's forecasting, on the basis of the last two years, has contained too much fat. BT having been rebuked for exceeding their limit by a small margin in 1980-81, regard their EFL very literally as a limit and not in any way as a target. I am taking this up with them, but I confess to having some sympathy with their view that an undershoot is in principle less serious than an overshoot.

7 Sir George Jefferson is already seeking additional specific capital investment which would be of long term benefit to the business and which could be implemented this year. I have written to him welcoming these efforts. I have also asked him to consider a lower EFL next year in the light of the evidence of inadequate forecasting in the past.

8 I am copying this to the Prime Minister and Sir Robert Armstrong.

Yours sincerely,

Jonathan Spencer

M. PATRICK JENKIN

(approved by the Secretary of State
and signed in his absence)

JU321

BREAKDOWN OF BT FORECAST UNDERSHOOT FOR 1982/3

ITEM	DEVIATION FROM BUDGET (£ million)
Fixed Capital shortfall	
Reduction in prices	90
Reduced expenditure on accommodation for training and service centres	65
Late delivery, mainly of exchange equipment	80
Reduced demand due to recession (mainly local line plant)	20
Other (including delays to CTO site and third earth station site because of planning problems)	85
Total Fixed asset shortfall	340
Working Capital shortfall	100
Total shortfall on capital requirements	440
Increase in internal resources	
Lower than forecast staff costs	80
other current account improvements	70
Reduction in interest payments	60
offset by	
reduction in turnover	(130)
Total increase in internal resources	80
Total forecast undershoot	520

Post & Telecom : Future of PT 6

DEPARTMENT OF TRADE 1 VICTORIA STREET LONDON SW1H 0ET Telephone 01-215 7877

Prime Minister (2)

From the Secretary of State

MCS 3/12

CONFIDENTIAL

The Rt Hon Patrick Jenkin MP
Secretary of State for Industry
Department of Industry
Ashdown House
123 Victoria Street
London
SW1E 6RB

3 December 1982

Dear Patrick,

TELECOMMUNICATIONS BILL

Thank you for your letter of 29 November about our outstanding points of difference on the Telecommunications Bill. I have also seen John Sparrow's letter of 15 November. TPM

I am glad that we have been able to reduce the areas of difficulty. But, as you say, two major points remain at issue: the boundary between the responsibilities of the Director General of Telecommunications (DGTel) and the Director General of Fair Trading; and the reporting point for the Monopolies and Mergers Commission (MMC) on references concerned with variation of licences.

At E(TP) on 30 June we agreed a regulatory authority for monitoring licenced telecommunications systems. We also recognised that a boundary would have to be drawn between the responsibilities of DGTel and the DGFT and MMC. The root of my concern is that the Bill as drafted gives the DGTel far wider powers than was contemplated when the regulatory authority was agreed in June. I believe that this issue must be settled before we can preceed to a conclusion on the demarcation of boundaries.

From the Secretary of State

CONFIDENTIAL

As the Bill stands, at present, it would provide the DGTel with the Competition Act and anti-monopoly powers in relation to, for example:-

i the supply of services which necessarily involve the running of a telecommunications system; this could be a very wide field indeed; and

ii the production, supply and export - as well as the installation and maintenance of - telecommunications apparatus, whether or not connected to a licenced system. Again, the Bill's very wide definition suggests that even ordinary portable tape recorders could be caught.

In short, the effect of the Bill as presently drafted would be to transfer from the DGFT to the DGTel competition authority over the already wide, and ever increasing, field of telecommunications-related activities. There would be real dangers of inconsistent application of competition policy between different parts of the economy.

For the DGTel to be a general competition authority, over and above a regulator of licence activities, goes further than any decision we have taken, or indeed I have seen any justification for taking. In his 15 November discussion with Gerard Vaughan, Kenneth Baker suggested that the problem of over-lapping responsibilities might be resolved by both Directors General having concurrent jurisdiction over part of the telecommunications field. Each would then act with the consent of the other, with provision for disputes to be resolved by Ministers. I am not attracted to this idea, which would be widely misunderstood. If we are to continue to have a unified and consistent

competition policy, the DGFT should have primacy.

In so far as it is essential to supplement the agreed powers of the DGTel to regulate the licensed activities through licensed conditions, by some use of the Competition Act and monopoly process, we should aim first for as precise a demarcation as possible of the DGTel's powers. We should narrow any grey area between the two Directors General, by setting the definitions of "activities connected with telecommunications" and "telecommunications apparatus and services" as narrowly as possible. But we should be clear that the DGFT has primacy in cases requiring a decision within the remaining grey area.

There is the separate issue of the reporting point of the MMC on licence amendment references. I am afraid that John Sparrow's comments do not resolve my doubts. Licensed conditions will cover not only rate of return regulation and pricing, where I do understand the arguments against introducing Ministerial discretion. The conditions will also bar some anti-competitive practices - so that the MMC would, on your proposal, report on amendment of these to the DGTel, while reporting to the Secretary of State if the general competition law was used against other anti-competitive practices. The conditions will also impose social obligations; a change in these will alter the burden - upwards or downwards - borne by subscribers generally to the benefit of particular groups, such as the uses of pay 'phones in rural areas. I believe this is something on which Parliament will look for Ministerial accountability.

I consider both the remaining points of difficulty as very important. It is quite contrary to the policy of this Government to set up bodies, largely unaccountable either to Ministers or Parliament, with wide-ranging and all pervasive powers which are

From the Secretary of State

CONFIDENTIAL

unnecessary either in their own right or because they are duplicating existing powers elsewhere. I know that our officials are in touch, and hope that a satisfactory solution can be found.

I am copying this letter to the Prime Minister, the Home Secretary, the Chancellor of the Exchequer, the Secretaries of State for Scotland, Northern Ireland and Wales, the Minister for Agriculture, Fisheries and Food, the Secretary of State for the Environment, the Chancellor of the Duchy of Lancaster, the Lord Privy Seal, the Chief Secretary and the Chief Whip, and to Sir Robert Armstrong and to John Sparrow.

Yours,

Arthur

LORD COCKFIELD

DEPARTMENT OF TRADE 1 VICTORIA STREET LONDON SW1H 0ET Telephone 01-215 7877

cc JV

Prime Minister ②

MCS 3/12

From the Secretary of State

The Rt Hon Patrick Jenkin MP
Secretary of State for Industry
Department of Industry
123 Victoria Street
London SWI

2 December 1982

Dear Patrick,

MONOPOLIES AND MERGERS COMMISSION: REFERENCE OF BRITISH TELECOMMUNICATIONS

I should like to announce before the Recess the 1983 programme of efficiency investigations of nationalised industries by the Monopolies and Mergers Commission. Nicholas Ridley told the House of Commons on 30 November 1981 that the Government would announce a programme of references annually for the year ahead.

My proposals for 1983 depend on a decision on the inclusion of British Telecom. When E(NI) committee discussed the matter on 26 July, they felt that the balance of advantage was firmly in favour of a reference of BT to the MMC in the first six months of 1983; and you were invited to discuss the Government's intention in this sense with Sir George Jefferson. I should be grateful if you could let me know as soon as possible where matters now stand.

I am sending copies of this letter to members of E(NI), Sir Robert Armstrong and John Sparrow.

Yours ever,

Keith

LORD COCKFIELD

Prime Minister (2)

This will take some answering.

MCS 29/11

Treasury Chambers, Parliament Street, SW1P 3AG

Rt Hon Patrick Jenkin MP
Secretary of State
Department of Industry
Ashdown House
123 Victoria Street
London SW1E 6RB

29 November 1982

Dear Patrick,

BRITISH TELECOM: 1982-83 UNDERSHOOT

We shall be discussing the Quarterly Monitoring Returns for the nationalised industries as a whole at E(NI) shortly. They are dominated by the extremely large undershoot by BT of its EFL. This amounts to £520 million.

Geoffrey Howe wrote to you on 20 April last proposing a mid-term review of BT's ambitious capital plans and I assume that these figures stem from that. Certainly it is useful to have had the information about underspend earlier this year than last. But it is a pity that we were not able to take account of it in our public expenditure discussions last month. We knew then that there was likely to be some underspend, as indeed we have suspected throughout the year, but these figures show that it is likely to be several hundred million higher than we thought.

I was prepared to accept, in relation to the earlier figures that, in part at least, the underspend was attributable to creditable factors such as lower prices and some progress in making real cost savings. However, the overall shortfall on fixed asset expenditure is now glaring. The EFL was based on an increase in fixed asset expenditure of 28 per cent (on BT's new accounting policies). But the estimated outturn is only 9 per cent and even this depends on a halving of the variance from budget in the second half of the year, so there may well be further underspend to come. We cannot ignore the implications of this, nor indeed of the other factors which have led to the undershoot. For instance next year's EFL is besed on assumed capital expenditure of £2,012 million, some 22 per cent higher than the outturn now anticipated for this year.

It would be extremely helpful in advance of the E(NI) meeting to have a more detailed explanation of this year's undershoot, drawing on the results of the review which the Chancellor requested. In particular, we need to know what faults in BT's management systems

have led to the persistent overfunding; what is being done to correct them urgently; and what size of cash surplus BT is now generating as a result.

Secondly, I must now reopen with you the question of the £96 million external financing provision for BT for next year. On grounds of investment realism alone, it looks as though this should now be negative, but there are other factors such as the continuing underestimation of profitability which need also to be taken into account. I would be grateful if you would consider this and let me have your proposals.

There may be wider issues which I shall need to take up with you, in the light of your response. But in the first instance we need an urgent analysis of the situation and your proposals on next year's EFL.

I am sending copies of this letter to the Prime Minister and to Sir Robert Armstrong.

Yours ever
Leon

LEON BRITTAN

Post ~~office~~ etc, Pay Negotiations, April 1980.

Post & Telecoms c/c JV

DEPARTMENT OF INDUSTRY
ASHDOWN HOUSE
123 VICTORIA STREET
LONDON SW1E 6RB
TELEPHONE DIRECT LINE 01-212 3301
SWITCHBOARD 01-212 7676

JF2133
Secretary of State for Industry

29 November 1982

The Rt Hon Lord Cockfield PC
Secretary of State for Trade
Department of Trade
1 Victoria Street
LONDON
SW1H 0ET

Prime Minister (2)

MCS 30/11

Dear Arthur,

Thank you for your letter of 11 November about the detailed points in the Telecommunications Bill which continue to cause you concern. We were unable to meet before Legislation Committee discussed the Bill but Gerry Vaughan and Kenneth Baker had a long and constructive meeting on 15 November and our officials have met on more than one occasion.

2 On most of the points you have raised there is complete agreement between us. The Bill, which has been prepared in some haste, will require amendment in Committee and officials have never been in any doubt about the need to tidy up various points.

3 You asked about proposals for ensuring that BT is efficient. I intend that the performance of BT plc will be subject to reviews which will take account of its efficiency. The precise arrangements will depend on Professor Littlechild's report on Alan Walters' scheme for an output related levy. For the present, however, I am working on the basis that BT plc's licence will contain a condition limiting its maximum rate of return on capital in the regulated business and that this will be reviewed every five years by the Monopolies and Mergers Commission on the basis of a licence variation reference. Clause 11(1) empowers the Director General to specify in a reference "any matters which relate to the supply of telecommunication services or telecommunication apparatus" and I shall give the Director General guidance under Clause 49(1) to have particular regard to efficiency when making such references. The precise arrangements were worked out in the Bradbury Working Group, in which your officials participated, and Kenneth Baker will explain our proposals in Committee.

/4 So ....

4 So far as consumer protection is concerned, the Bill is a significant step in the right direction; it does much to secure the rights of BT's customers and to remove BT's privileges and it has been welcomed in the press. I intend to introduce proposals on metering in Committee which will provide an opportunity to consider the provisions in Clause 41 about documentary evidence for sums due. I deleted the provisions about performance targets because they represented too much potential interference by Whitehall in the affairs of private companies but I shall explain on second reading that the Director General will play much the same role as the Post Office Users National Council in relation to performance targets. Clause 47(5) contains the provision you requested about payments to Postal and Telecommunication Adivsory Committees.

5 There are, however, two areas of disagreement between us. The boundary between the functions of the Director General of Telecommunications and the Director General of Fair Trading is a genuinely difficult problem;and you have raised the question whether it is right for the MMC to report to the Director General and not to Ministers on licence variation references. Our officials are in touch about these issues and I shall write to you again shortly.

6 I am copying this letter to the recipients of yours.

Yours ever

Peter

Post & Telecomms
Future of:

CONFIDENTIAL

Ref. No: PIC(82) 7

TELECOMMUNICATIONS BILL

2nd Reading

Monday 29th November 1982

Contents

Conservative Research Department,
32 Smith Square,
London SW1
Tel. 222 9000

Enquiries on this brief to:
LYNDA ROUSE x 2512

Purpose of the Bill

Information Technology (IT) is a rapidly growing and rapidly developing sector of the economy. Its development demands access to a modern telecommunication network. The Government is determined that:

* the telecommunications supply industry should not be held back unnecessarily in responding to expanding IT markets;

* that BT should be free to participate on equal terms with private sector companies in this expansion;

* that BT's customers should be relieved of the need to finance investment through charges, where this could be done by the markets;

* that BT's customers should benefit from free and fair competition in the supply of telecommunications services.

Already, telecommunications is being liberalised. Arrangements are being made for users to have a choice:-

- of network - Mercury and the private sector radio telephone company will give business and some other users a choice of telephone company for their calls;

- of services - users will have a choice of company when they want a service provided over the telephone.

- of apparatus - users will have the choice of whether to buy or rent most of their telecommunications apparatus from BT or other suppliers.

The present Bill will take the process of liberalisation to its logical conclusion.

Provisions of the Bill

BT will be changed from a nationalised industry to a public limited company, BT plc. All its existing assets and liabilities will be tranferred to the successor company. After the next general election, the Government plans to sell 51% of the shares.

The present exclusive privilege of BT to run the telecommunications system will end. BT and the other operators will run under licences issued by the Secretary of State, and BT will no longer have powers to license other operators.

Operating licences will contain certain conditions. In particular, because BT will operate what is by far the largest and most important network, its licence will be negotiated with particular care. There will be a condition that all reasonable demands in all parts of the UK (rural areas, City of London etc) should be provided. BT will also be required to operate kiosk and emergency services.

BT's licence will also protect rights of connection to its network of apparatus from other suppliers which meets approved standards,

and of other licensed systems. Other conditions will ensures fair competition and fair pricing.

A new Office of Telecommunications will be set up. Among other things, OFTEL will:

* ensure fair and free competition in telecommunications;
* monitor compliance with licence terms and conditions;
* investigate consumer complaints;
* advise the Secretary of State on telecommunications matters.

At present, BT does not generally provide services under contract, and customers cannot normally sue BT for negligence etc. The Bill will require BT to provide services under contract and remove immunity in most cases from civil action. Customers will be able to sue BT just as they can sue shops which, for example, supply faulty goods.

The Bill also provides for the Telegraph Acts, most of which date from the nineteenth century, to be replaced by a new Telecommunication Code, which will provide for telecommunication operators to be authorised to install their plant in private land, streets etc. The Code has been drafted so as to make sure that no person should unreasonably be denied access to a telecommunications system because of difficulties in connecting his home or business to a public telecommunications system.

The Bill also seeks to amend some provisions in the Wireless Telegraphy Acts.

BT Results

	1979	1980	1981*	1982
Turnover £m	3,243.9	3,558.9	4,554.2	5,708.1
Profit/(loss) £m	336.4	129.1	123.9	457.8
Capital requirement £m	1,045.8	1,352.1	985.0	1,837.6
Self-financing ratio	106.1	79.2	111.9	88.8
Capital employed £m	11,995.1	13,540.1	14,574.6	15,285.4
Return on capital employed at replacement cost:				
Target %	6.0	5.0	5.0	5.0
Achievement %	6.9	4.6	4.4	6.5
Tariff index (1970 = 100) adjusted for inflation	82.6	74.0	76.8	82.5

*Accounting policies were modified in 1981, so some figures are not strictly comparable .

The Corporation reduced its real unit costs by an average of 2.9% pa in the four years 1978-9 to 1981-2, and the figure in 1981-2 was 2.1% below that in 1980-1. The target set in 1978 (currently under review) was a reduction of 5% pa, over the five years 1978-9 to 1982-3.

The target real rate of return for 1982-3 and 1983-4 is 5½%, and the EFL for 1982-3 has been set at £320 million.

Points to make:

Rural areas - The Government has made a commitment that anyone who has access to a phone under present arrangements will continue to do so under the new ones. BT's board has publicly accepted a continuing responsibility to provide services to rural and outlying areas.

BT is at present under no obligation to maintain a universal tariff structure. For example, some rural connection charges are more expensive than the average. Under the new arrangements OFTEL will ensure that there will be no undue discrimination; nor will rural areas be charged unreasonable prices. Apart from the initial connection of remote subscribers, there is no evidence that rural services are more costly than others to provide.

Consumer protection

The introduction of competition is an effective curb on prices. For example, BT has already reduced charges on its 100 most densely used trunk routes, and there has been a significant reduction in the price of telex teleprinters following liberalisation.

Customers will also benefit from the fact that the extent to which investment is financed from revenue will probably fall, once BT has access to financial markets. However, the Government accepts that BT will dominate some telecommunications sectors. The terms of its licence will include conditions on the real rate of return on capital that BT is able to earn on these activities. This will be fixed so as to maintain pressure on BT to improve efficiency, while providing incentives for expansion. OFTEL will ensure that no unreasonable prices are charged, and that there is no undue discrimination against certain classes of customers.

The Post Office Users' National Council (POUNC) will no longer deal with telecommunications once BT becomes a plc. OFTEL will effectively take over these responsibilities. Unlike POUNC, OFTEL will, through its monitoring of licence conditions, be able to enforce its suggested remedies for consumer problems. OFTEL will take over the POUNC role of agreeing performance targets with BT, and extend this to other telecoms operators.

The provisions already described to introduce legal redress for consumers will also be of benefit to them.

The Sale

The precise method of sale will be decided in the light of market conditions at the time. The issue will be the largest ever carried out in this country. The Government hopes that many of BT's 250,000 employees and 18,000,000 subscribers will buy shares. Ways of encouraging them are being considered.

The Articles of Association of BT plc will prevent foreign or domestic take overs. The claims of BT, the pre-1969 pension deficiency and the taxpayer will be considered in relation to the proceeds of the sale.

The Workforce

Telecoms is a major growth area. The removal of restrictions on

on financing will allow BT to take maximum advantage of this, along with the other telecoms firms. There should be more, not fewer, jobs than if BT carried on as a nationalised industry.

There has been talk of a cut of 45,000 in BT jobs. It is certainly true that BT does need to improve its efficiency. It could provide the present level of services with fewer people. But, the BT Bill offers the prospect of an expansion in output.

The telecommunications manufacturing industry has lost 40,000 jobs in the last ten years. That shows that the mixture of monopoly and protection does not pay. Since liberalisation, the prospect of an expanding industry has been to hand:

(1) On the equipment side, new market entrants such as Mitel, GTE/Ferranti, Harris, have already put down plants and are generating new jobs in manufacturing. Retailers such as Discoms, Tandy, and many other smaller people are already expanding into the liberalised market and are recruiting new staff.

(2) As regards valued added services, this is a whole new industry and there is a build up of businesses wishing to offer new services on the network. It is expected that over the next 3 to 4 years several thousand new jobs will be created as we witness the rapid growth in this service sector already manifest in the United States. BT itself has created a new job centre in Telecom Gold.

(3) Mercury itself will create new jobs as well as pull through new jobs on the supply side. BT in response has created new posts to provide competitive digital services.

The legislation will safeguard existing employee pension rights, and will in no way disadvantage employees or weaken their pension position. The Government cannot guarantee how pension arrangements will evolve in the future even in the nationalised industries.

Political Points

* Nationalisation has been increasingly unpopular since the 1950s. A recent survey by NOP (August 1982) showed that 63% of the electorate - and, indeed, 35 per cent of Labour voters as well as 68 per cent of Alliance voters - want no more nationalisation.

* Despite this unpopularity, Labour want to extend nationalisation, and return to the use of public sector monopolies. Labour's Programme 1982 says:

  "We will restore the public monopoly in the field of post and telecommunications, and return 'Project Mercury' to British Telecom".

* Labour's attitude to new technology is to nationalise it. The first point in their list of proposals for new technology published in Labour's Programme 1982 is:-

"Through INMOS we have a publicly owned company manufacturing and developing silicon chips. We will extend public ownership in electronics through the National Enterprise Board. GEC, which occupies a pivotal position in the British electronics and electrical engineering industries, will form an integral part of our public ownership programme".

* Labour plays lip service to the need for technological development, but cannot escape the Luddite inclinations of many in the Party. Tony Benn, for example, has changed his mind since his days at MINTEC, in the forefront of the "white heat of technology" movement. In a film made by the Education Media Group, released on 25th February 1982, he says that the microchip could cause unemployment, social disruption and "tyranny in the guise of liberation" (A report in the Financial Times, 26th February 1982).

* Labour's Programme 1982 promises to encourage unions to negotiate New Technology Agreements. However, the objective is not to promote new technology; it is to promote the power of the unions. The Programme states:

  "Trade unions have been relatively successful over the post-war period in extending joint control over day-to-day decisions in the enterprise. Although progress has been uneven, they have in many places extended the frontier of negotiation beyond terms and conditions of employment to include issues formerly within the managerial prerogative. Among these issues are the organisation and pace of work; staffing levels; recruitment and deployment of labour; demarcation and labour flexibility; quality, stock and financial control; grievances and discipline; and health and safety. Workforce influence in these areas has been enlarged mainly through developoments in the scope of collective bargaining. Much of the impetus for these developments has come in recent years from the negotiation of New Technology Agreements. These have been accompanied by significant changes in trade union structure. The shift to plant and company bargaining has led to the growth of Joint Union Committees which have strengthened the ability of workforce representatives to pressurise management on key issues relating to the organisation of production".

* Under Labour, BT was starved of investment. Under the Conservatives, investment has increased substantially:

Capital Requirement £m

Outturn					
1976-7	1977-8	1978-9	1979-80	1980-1	1981-2
816	844	993	1,215	1,545	1,898

Plans		
1982-3	1983-4	1984-5
2,380	2,725	2,960

PEWP, Cmnd 8494-11 1982

* Labour set the target (in 1978) for BT of a 5% per annum reduction in real unit costs for 1978-9 to 1982-3. The average so far has been a reduction of 2.1%. The following extracts from a letter from BT's Chairman to his staff, dated December 1981 illustrate the problems:

"In the past, management hasn't laid sufficient emphasis on labour efficiency and output...

"...over 40 per cent of field supervisors' time is spent on paperwork. There's more emphasis on reporting up than on securing useful and timely information for the work in hand.

"We've been hampered by things like inter-union arguments on operating computer terminals in mixed clerical/engineering work areas...

"...For every two hours spent on installation in the field, one hour is spent in control, line plant allocations and replacements. The number of survey officers has remained unchanged for 20 years, although the need for them has reduced. In America, AT & T installation and maintenance staff average seven visits a day, compared with our average of three.

"... despite reductions in such things as travelling time over the last two years (ineffective time) still represents 40 per cent on cost.

"In exchange maintenance, studies show that manning levels could be reduced by better work organisation.

"Over 70 per cent of maintenance staff in Strowger exchanges are graded as TOs; the figure should be nearer 50 per cent.

"Then there's grade drift - people being paid a grade or so higher than their work deserves.

"The problems are compounded by:
- demarcation problems;
- inflexible work practices;
- rigidity on manning levels; and
- slowness to accept change.

"A succession of surveys show that BT salaries are generally above the average; at best, they're near the very top of the market.

"In addition to the staff's contribution of 6% of salary, BT also contributes to the Pension Fund at the rate of 15½% - much more than most other large organisations.

"There are many other ways in which the business overspends, eg:

- THQ staff has grown by over 10 per cent since 1978.
- Over 30 per cent extra SSS staff (half of them in THQ) in the same period.
- There are 25,000 THQ staff, some 8000 RHQ staff, to say nothing of Area HQs.
- Over-generous accommodation, compared with commercial firms, particularly with so many HQ staff in London.
- Slow and expensive promotion and appointments procedures, with seniority often more influential than merit."

* The SDP think that they can devise a scheme, where others have failed, which will accurately simulate the pressures of the market place. This flies in the face of all past experience.

* Since the war, the accumulated loss through grants and capital write offs of the nationalised industries is, in today's money, around £40,000 million. Yet Roy Jenkins has said: "Many of the early nationalisation measures are right. They have remained part of the social fabric. I favour measures of this type" (Hansard, 10th November 1982, col. 579).

"Alliance" Voting Record on Nationalisation/Privatisation

	Voted with the Conservatives	Voted with Labour
Industry Bill Second Reading (NEB) 17-18.2.75	Brocklebank-Fowler Liberals	Owen (L) Jenkins (L) Rodgers (L) Williams (L) Wrigglesworth (L)
BL Bill Second Reading 21.5.75	Liberals	Owen (L) Williams (L)
Aircraft & Shipbuilding Industries Bill Second Reading 2.12.75	Liberals	Jenkins (L) Owen (L) Rodgers (L) Williams (L)
Civil Aviation Bill: British Airways Second Reading 19.11.79	Brocklebank-Fowler (C) Liberals	Owen Wrigglesworth
British Aerospace Bill Second Reading 20.11.79	Liberals Brocklebank-Fowler	Owen (L) Wrigglesworth (L)
Transport Bill: National Freight Corporation 27.11.79	Liberals Brocklebank-Fowler	Rodgers Wrigglesworth

British Telecommunications Bill Second Reading 2.12.80	Brocklebank-Fowler (C) Two Liberals:- Ross Howells	Owen Wrigglesworth Rodgers (No Liberals)
Debate on the Address, Nationalised Industries 10.11.81	Liberals abstained	Owen Rodgers Wrigglesworth
Transport Bill: British Transport Docks Board & BR Subsidiaries Second Reading 13.1.81	Brocklebank-Fowler (C) Liberals	Owen Wrigglesworth
Oil & Gas Enterprise Bill Second Reading 19.1.82		Owen Wrigglesworth Williams Liberals
Transport Bill: National Bus Company 9.2.82		Liberals Brocklebank-Fowler Owen Williams
Debate on the Address Public Enterprise 9.11.82	Liberals SDP	
British Shipbuilders Bill Second Reading 17.11.82		Owen Rodgers Williams Liberals

Conservative Research Dept
32 Smith Square LONDON SW1

LMR/CR
26.11.82

010

DEPARTMENT OF INDUSTRY
ASHDOWN HOUSE
123 VICTORIA STREET
LONDON SW1E 6RB
TELEPHONE DIRECT LINE 01-212 3301
SWITCHBOARD 01-212 7676

JU273

Secretary of State for Industry

29 November 1982

John Rhodes Esq
Private Secretary to the
Secretary of State for Trade
Department of Trade
1 Victoria Street
London SW1

Dear John

SECOND READING OF THE TELECOMMUNICATIONS BILL

I attach, for your information, a draft copy of the speech that my Secretary of State intends to make in the House this afternoon. I am attachment to Michael Scholar at No 10, Leslie Pallett (Home Office) and Margaret O'Mara (Treasury).

Yours ever
David Saunders

DAVID SAUNDERS
Private Secretary

SECRETARY OF STATE'S SPEECH : SECOND READING OF THE TELECOMMUNICATIONS BILL, MONDAY 28 NOVEMBER

I BEG TO MOVE THAT THE BILL BE NOW READ A SECOND TIME.

MR SPEAKER, THIS BILL WILL EMPOWER THE GOVERNMENT TO CONVERT BRITISH TELECOM FROM A NATIONALISED CORPORATION INTO A COMPANIES ACT COMPANY WITH SHARES LIKE ANY OTHER ~~COMANY.~~ COMPANY

IT WILL ALLOW MEMBERS OF THE GENERAL PUBLIC TO BUY SHARES, STARTING AFTER THE NEXT GENERAL ELECTION.

WHEN ~~51% OF~~ HALF THE SHARES HAVE BEEN SOLD, BT WILL NO LONGER BE A NATIONALISED INDUSTRY AND WILL BECOME A PRIVATE SECTOR COMPANY.

THE BILL MAY WELL BE CONTROVERSIAL IN THIS HOUSE.

BUT IT WILL, I BELIEVE, BE WIDELY WELCOMED BY PEOPLE OUTSIDE.

BECAUSE THEY KNOW THAT COMPETITIVE FREE ENTERPRISE IS A FAR, FAR BETTER SYSTEM THAN STATE MONOPOLY.

~~THIS~~ THE BILL ~~IS IMPORTANT IN ITSELF.~~

~~BUT IT~~ ALSO STANDS AS CLEAR TESTIMONY TO THE DETERMINATION OF THIS SIDE OF THE HOUSE TO ROLL BACK THE FRONTIERS OF THE STATE AND TO GIVE PEOPLE A REAL STAKE IN THE ECONOMY.

THAT IS <u>REAL</u> PUBLIC OWNERSHIP.

THIS BILL FOLLOWS LOGICALLY ON THE MEASURES WE ARE ALREADY TAKING TO BRING COMPETITION INTO TELECOMMUNICATIONS.

BEFORE WE CAME TO POWER, APART FROM THE CITY OF KINGSTON-UPON-HULL, BRITISH TELECOM WAS THE SOLE SUPPLIER OF ~~TELEPHONES,~~ TELEPHONE SERVICES AND MOST TELEPHONE EQUIPMENT.

THE MONOPOLY WAS BAD FOR THE CUSTOMER AND BAD FOR BT ITSELF.

ANY GROWING BUSINESS LIKE BT, TO MEET THE NEEDS OF ITS CUSTOMERS EFFECTIVELY, NEEDS THE DISCIPLINE OF THE MARKET PLACE, THE RIGHT TO RAISE ITS OWN FINANCE, THE FREEDOM TO INVEST, AND THE FREEDOM TO MANAGE THE BUSINESS.

THE BRITISH TELECOMMUNICATIONS ACT 1981 WAS A FIRST STEP TOWARDS GREATER COMPETITION.

I HAVE ALREADY LICENSED MERCURY COMMUNICATIONS LTD TO COMPETE WITH BT - THE FIRST SUCH COMPETITIVE NETWORK IN EUROPE.

AN EVER-WIDENING RANGE OF EQUIPMENT IS BEING OPENED UP TO COMPETITION.

THE MARKET IS INCREASINGLY FREE TO SELL VALUE-ADDED SERVICES OVER THE BT AND MERCURY NETWORKS.

WE HOPE SOON TO HAVE COMPETITIVE NATIONAL RADIO TELEPHONE NETWORKS.

FULL CREDIT IS DUE TO THE CHAIRMAN OF BT, SIR GEORGE JEFFERSON, HIS BOARD AND THE EMPLOYEES OF BT FOR THE WAY THEY HAVE BEGUN TO TRANSFORM WHAT WAS RECENTLY A GOVERNMENT DEPARTMENT INTO A COMMERCIALLY ORIENTED BUSINESS.

I THINK WE NEED TO HEAR FROM THE PARTY OPPOSITE WHETHER THEY ARE IN FAVOUR OF THIS FREEDOM AND WIDENING CONSUMER CHOICE OR WHETHER THEY REALLY PREFER STATE MONOPOLY.

WE PREFER COMPETITION, BUT SO LONG AS BT IS NATIONALISED, SO LONG AS IT IS SUBJECT TO THE WEB OF CONTROLS WHICH STIFLE COMMERCIAL FREEDOM, SO LONG AS ITS CAPITAL FOR INVESTMENT CAN COME ONLY FROM THE CUSTOMER IN HIGHER CHARGES OR FROM THE ~~EXCHEQUER~~ TAXPAYER, BT WILL FACE THE COMPETITION WITH ITS HANDS TIED.

I WANT TO SEE BT BECOMING A MAJOR FORCE IN THE WORLD TELECOMMUNICATIONS MARKET. LIKE AT&T.

FOR THIS TO HAPPEN, BT NEEDS THE FINANCIAL FREEDOM WHICH AS A NATIONALISED INDUSTRY IT DOES NOT HAVE AND CAN NEVER HAVE.

AS A NATIONALISED INDUSTRY, BT DOES NOT HAVE DIRECT ACCESS TO FINANCIAL MARKETS.

ITS BORROWING IS CONTROLLED BY GOVERNMENT AND COUNTS AGAINST THE PSBR.

SO GOVERMENTS HAVE FACED AN AWKWARD CHOICE.

JU264 IF THEY WANT TO HOLD PRICES DOWN, THEN INVESTMENT NEEDS ARE STARVED.

THATS WHAT HAPPENED BETWEEN 1974 AND 1979, WHEN UNDER THE PARTY OPPOSITE, CAPITAL INVESTMENT BY BT DECLINED IN REAL TERMS.

IF, LIKE THE PRESENT GOVERNMENT, WE ATTACH GREATER IMPORTANCE TO INVESTMENT, HIGHER CUSTOMER CHARGES ARE INEVITABLE.

THE ONLY ALTERNATIVE, REJECTED BY BOTH GOVERNMENTS, WOULD HAVE BEEN VASTLY GREATER BORROWING FROM THE NATIONAL LOANS FUND AND CONSEQUENT CHARGE ON THE PSBR.

YES, MR SPEAKER, THE NETWORK IS NOW BEING MODERNISED.

THE NEW DIGITAL SWITCHING IS BEING INSTALLED.

OPTICAL FIBRES ARE NOW BEING USED.

BUT THE CUSTOMER HAS HAD TO DIG DEEPER AND DEEPER INTO HIS POCKET TO PAY FOR ~~IT~~. THIS

THIS DOES NOT HAVE TO BE.

IT IS A SELF-IMPOSED "HOBSON'S CHOICE" DICTATED BY THE BRUTE FACTS OF NATIONALISATION.

WHEN, AFTER THE NEXT ELECTION, A MAJORITY OF THE SHARES IN BT ARE HELD BY THE PUBLIC, BT WILL LOOK TO THE MARKET FOR MOST OF ITS EXTERNAL FINANCING.

THIS WILL GIVE THE MANAGEMENT GREATER FLEXIBILITY.

THIS WILL PUT LESS PRESSURE ON CONSUMERS AND TAXPAYERS.

IT WILL SUBJECT BT TO PROPER MARKET DISCIPLINES; AND IT WILL ALLOW BT TO RESPOND TO THE NEEDS OF CUSTOMERS JUST LIKE THE PRIVATELY-OWNED TELEPHONE COMPANIES IN THE UNITED STATES.

BT HAS ASKED FOR ACCESS TO THE MARKET.

THE UNIONS HAVE ASKED FOR IT.

THE SELECT COMMITTEE HAS ASKED FOR IT.

THE NATIONAL ECONOMIC DEVELOPMENT COUNCIL HAS ASKED FOR IT

THIS BILL OPENS THE WAY.

[STOCKTON] COULD BT GET ACCESS TO PRIVATE CAPITAL MARKETS WITHOUT CHANGING ITS OWNERSHIP?

WE LOOKED AT THE POSSIBILITY OF A "BUZBY BOND" AS THE PRESS CHRISTENED IT - A PERFORMANCE-RELATED BOND WHERE RETURNS TO THE BONDHOLDER WOULD DEPEND ON BT'S RESULTS.

BUT IT WOULD NOT BEGIN TO MEET BT'S NEEDS.

THE MAXIMUM SUM THAT WAS EVER ENVISAGED TO BE RAISED BY THE BUZBY BOND WAS OF THE ORDER OF £150 MILLION, ~~EACH~~ IN THE FIRST YEAR

COMPARED WITH AN INVESTMENT PROGRAMME NOW RUNNING AT NEARLY ONE AND A HALF BILLION A YEAR AND GROWING, THE BOND WOULD ~~HAVE MADE LITTLE REAL DIFFERENCE~~ NEVER HAVE SOLVED THE PROBLEM.

THE ONLY WAY IS TO FREE BT FROM TREASURY CONTROL AND ALLOW IT TO RAISE THE CAPITAL IT NEEDS JUST ~~AS~~ LIKE ANY OTHER MAJOR BUSINESS.

IT IS THEREFORE HARDLY SURPRISING THAT IN THEIR REACTION TO MY STATEMENT ~~ON~~ OF 19 JULY, [CMMD 8610] BT HAD THIS TO SAY :—

> "THE BOARD CAN SAY...THAT, GIVEN THE RIGHT CONDITIONS, IT WOULD WELCOME FREEDOM FROM WHAT THE SECRETARY OF STATE HAS DESCRIBED AS THE WEB OF GOVERNMNENT CONTROL AND INTERFERENCE."

MR SPEAKER, THOSE WHO WANT TO SEE MORE COMPETITION IN TELECOMMUNICATIONS, THOSE WHO WANT TO SEE BT BECOME A MAJOR WORLD FORCE IN INFORMATION TECHNOLOGY, THOSE WHO WANT BT TO COMPETE IN THE RAPIDLY GROWING MARKET FOR TELECOMMUNICATIONS, MUST ACCEPT THAT THIS BILL OFFERS THE ONLY WAY FORWARD.

TO WANT THESE THINGS BUT TO OPPOSE THE BILL WHICH MAKES THEM POSSIBLE IS JUST DOTTY.

YES, LET US DISCUSS THE DETAILS.

BUT LET US DO SO IN THE RECOGNITION THAT, FOR THE CUSTOMER, COMPETITION IS BETTER THAN MONOPOLY, THAT IF BT IS TO BE FREE TO COMPETE IT MUST BE FREE TO RAISE CAPITAL, AND THAT THE ONLY WAY THAT THIS CAN BE DONE IS TO CONVERT BT INTO A PRIVATE SECTOR COMPANY.

246·1 LET ME NOW TURN TO THE BILL.

LET ME SAY AT ONCE THAT, YES, IT IS A LONG BILL BUT IT LOOKS PERHAPS MORE FORMIDABLE THAN IT IS.

THE HOUSE WILL HAVE ALREADY SEEN THAT OF THE 149 PAGES, 25 PAGES CONTAIN SCHEDULE 2, THE RE-ENACTMENT AND UPDATING OF THE TELEGRAPH ACTS, AND NO LESS THAN 50 PAGES CONTAIN SCHEDULE 4 EMBODYING MINOR AND CONSEQUENTIAL AMENDMENTS.

CLAUSES 66 TO 75 AMEND THE WIRELESS TELEGRAPHY ACTS TO STRENGTHEN THE ENFORCEMENT PROVISIONS FOR DEALING WITH RADIO INTERFERENCE AND THE ILLEGAL USE OF RADIO EQUIPMENT.

SO THE HEART OF THE BILL IS TO BE FOUND IN THE FIRST 65 CLAUSES AND IN SCHEDULE 1.

AND IT IS TO THOSE PARTS THAT I NOW TURN.

RATHER THAN TAKE THE HOUSE THROUGH EACH CLAUSE ONE BY ONE, I WILL EXPLAIN THE BILL'S MAIN PROVISIONS.

II and III

PART I, PROVIDES FOR THE APPOINTMENT OF AN INDEPENDENT DIRECTOR-GENERAL OF TELECOMMUNICATIONS AND OF AN OFFICE OF TELECOMMUNICATIONS, AND

~~PARTS II & III~~ ESTABLISH THE NEW REGULATORY FRAMEWORK.

THEY ENTRUST THE LICENSING OF TELECOMMUNICATION OPERATORS TO THE SECRETARY OF STATE.

THEY SET OUT THE FUNCTIONS AND DUTIES OF THE SECRETARY OF STATE, AND ~~OF~~ THE DIRECTOR GENERAL AND THEY PROVIDE FOR THE REGULATION OF TELECOMS OPERATORS. ~~OF LICENSEES UNDER THE NEW SYSTEM.~~

THIS ON ITS OWN REPRESENTS A MAJOR REFORM. ~~WHICH STANDS INDEPENDENTLY OF THE PROPOSAL TO MOVE BT INTO THE PRIVATE SECTOR.~~

IT IS REALLY A RECOGNITION OF WHAT HAS BEEN HAPPENING IN THE MARKET FOR TELECOMMUNICATIONS.

UNTIL NOW, BT HAS HAD WHAT HAS BEEN KNOWN AS ITS "EXCLUSIVE PRIVILEGE".

ONLY BT HAS HAD THE RIGHT TO RUN TELECOMMUNICATION SYSTEMS.

ANYONE ELSE HAD TO BE LICENCED, AND FOR MOST LICENCES, BT ITSELF WAS THE LICENSING AUTHORITY.

BUT WITH COMPETITION, THAT HAS BECOME ENTIRELY INAPPROPRIATE.

BT HAS IN EFFECT BEEN LICENSING ITS OWN COMPETITORS!

THE 1981 ACT MADE A NUMBER OF CHANGES TO PERMIT WIDER COMPETITION, BUT IT IS THIS BILL WHICH FINALLY REMOVES FROM BT BOTH THE "EXCLUSIVE PRIVILEGE" AND THE POWER TO LICENSE OTHERS.

THE POWER TO LICENCE WILL VEST IN THE SECRETARY OF STATE AND BT WILL NEED A LICENCE JUST LIKE ANY OTHER TELECOMMUNICATIONS OPERATOR.

LICENCES WILL CONTAIN CONDITIONS ABOUT HOW SYSTEMS ARE TO BE RUN AND WHAT SERVICES ARE TO BE PROVIDED.

IT WILL BE THE DUTY OF THE DIRECTOR GENERAL TO MONITOR HOW LICENCES IMPLEMENT THESE CONDITIONS.

I SHOULD HAVE THOUGHT THAT WHATEVER VIEW MIGHT BE TAKEN ABOUT THE PROPOSAL FOR PRIVATISATION, THIS NEW LICENSING STRUCTURE SHOULD COMMAND GENERAL SUPPORT.

IT CANNOT BE RIGHT FOR ANY COMMERCIAL ENTERPRISE TO HAVE THE POWER TO STRANGLE ITS COMPETITORS.

CLAUSE 3 IS VERY IMPORTANT.

IT SETS OUT THE GUIDELINES. ~~BOTH FOR THE SECRETARY OF STATE AND FOR THE DIRECTOR.~~

THESE GUIDELINES REQUIRE BOTH THE SECRETARY OF STATE AND THE DIRECTOR TO HAVE REGARD TO:

> "THE NEED TO SECURE THE PROVISION THROUGHOUT THE COUNTRY OF SUCH TELECOMMUNICATION SERVICES AS SATISFY ALL REASONABLE DEMANDS INCLUDING IN PARTICULAR PUBLIC CALL BOX SERVICES, EMERGENCY SERVICES AND SERVICES IN RURAL AREAS."

I CAN TELL THE HOUSE THAT WHEN I ISSUE A LICENSE TO BT UNDER THE BILL, THAT LICENSE WILL ~~IMPOSE A DUTY ON~~ AN OBLIGATION BT TO PROVIDE THESE SERVICES, REQUIRE AS AT PRESENT, WHERE IT IS PRACTICABLE TO DO SO.

LAST JULY, WHEN I ANNOUNCED OUR PROPOSALS I GAVE THE HOUSE A FIRM ASSURANCE THAT ANYONE WHO CAN OBTAIN A TELEPHONE UNDER THE PRESENT ARRANGEMENTS WILL BE ABLE TO OBTAIN A TELEPHONE UNDER THE NEW ARRANGEMENTS.

I REAFFIRM THAT ASSURANCE.

BT'S LICENCE WILL CONTAIN AN OBLIGATION TO PROVIDE SERVICES THROUGHOUT THE UK WHERE IT IS PRACTICABLE TO DO SO.

THE HOUSE WILL HAVE SEEN THAT BT ITSELF, IN THEIR PRESS NOTICE OF 19 NOVEMBER, HAVE (AND I QUOTE)

> " ACCEPTED A CONTINUING RESPONSIBILITY FOR SERVICES TO THE COMMUNITY INCLUDING THOSE IN RURAL AND OUTLYING AREAS."

I AM SURE THE WHOLE HOUSE WILL WELCOME THAT STATEMENT.

IT IS IN FACT A LOGICAL ASSURANCE IN COMMERCIAL TERMS.

THE VALUE OF A NETWORK IS COMMENSURATE WITH THE NUMBER OF PEOPLE CONNECTED TO IT.

IF BT WERE TO NEGLECT AREAS ALREADY PROVIDED FOR OR OPPORTUNITIES THAT MAY BECOME AVAILABLE IN THE FUTURE, THAT WOULD DEVALUE ITS OWN NETWORK.

264.2 I GAIN THE IMPRESSION THAT THIS ARGUMENT IS NOW ACCEPTED AND THE CONTROVERSY HAS TURNED TO PRICES.

LET ME REMIND THE HOUSE THAT, ON CONNECTION CHARGES FOR NEW SUBSCRIBERS, THERE ARE ALREADY SOME DIFFERENCES BETWEEN ONE CUSTOMER AND ANOTHER.

FOR INSTANCE, IF CONNECTION TAKES MORE THAN 100 HOURS OF WORK, THE STANDARD CHARGE IS INCREASED.

~~THESE~~ SUCH DIFFERENCES ARE REASONABLE AND I WOULD EXPECT ~~SIMILAR~~ SOMETHING OF THE SORT ~~ARRANGEMENTS~~ TO CONTINUE.

THE DIRECTOR WILL ENSURE THAT THE LICENCE CONDITIONS ABOUT AVOIDING UNDUE DISCRIMINATION IN THE PRICING OF CONNECTION CHARGES ARE OBSERVED.

TURNING TO THE COST OF CALLS, BT DOES NOT ACCOUNT SEPARATELY FOR SERVICES TO RURAL AREAS; BUT I CAN TELL THE HOUSE THIS: ONCE THE INITIAL INSTALLATION HAS BEEN CARRIED OUT THERE IS NO EVIDENCE THAT THE COST OF TELEPHONE SERVICES IS HIGHER IN RURAL AREAS THAN IN TOWNS AND CITIES.

INDEED, SOME OPERATIONS ARE SIGNIFICANTLY CHEAPER AWAY FROM DENSELY POPULATED AREAS.

IT IS CHEAPER TO INSTAL WIRES OVERHEAD RATHER THAN UNDERGROUND.

EXCHANGE EQUIPMENT IS NORMALLY SIMPLER; LAND AND BUILDINGS ARE USUALLY CHEAPER; LABOUR COSTS ARE OFTEN LOWER.

THESE FACTORS GO A LONG WAY TO BALANCE THE LESS INTENSIVE USE OF THE RURAL NETWORK AND SHOULD OF THEMSELVES PROVIDE A SUBSTANTIAL REASSURANCE FOR THOSE IN RURAL AREAS WHO HAVE EXPRESSED ANXIETIES ABOUT THE FUTURE COST OF THESE SERVICES.

THEN THERE IS THE QUESTION OF EMERGENCY SERVICES.

THE 999 SERVICE IS ESSENTIAL - ~~IT IS DIFFICULT TO~~ I CAN'T IMAGINE THE SERVICE NOT BEING PROVIDED - AND THE BT LICENCE WILL SAFEGUARD THIS SERVICE TOO.

THEN THERE ARE THE KIOSKS, OF WHICH THERE ARE SOME ~~SEVENTY-SEVEN THOUSAND~~ 77,000 IN THE PRESENT NETWORK.

THEY ARE IMPORTANT BECAUSE THEY GIVE ACCESS FOR TWENTY FOUR HOURS A DAY TO THE PUBLIC - PARTICULARLY FOR THOSE WHO CANNOT AFFORD A PHONE OF THEIR OWN, OR WHO ARE AWAY.

EVEN MORE IMPORTANT, THEY PROVIDE IMMEDIATE ACCESS TO THE EMERGENCY SERVICES AND IT IS A FACT THAT THE MAJORITY OF CALLS TO THE 999 SERVICE ARE MADE FROM ~~PUBLIC CALL OFFICES.~~ COIN-BOX PHONES.

THE KIOSK AND EMERGENCY SERVICES THOUGH ACCOUNTING FOR ONLY 3% OF BT's ~~TURNOVER~~ COSTS, ARE AN IMPORTANT FEATURE OF OUR TELECOMMUNICATIONS NETWORK.

IN ACCORDANCE WITH CLAUSE 3, THE LICENCE WILL ~~CONTAIN CLEAR OBLIGATIONS~~ REQUIRE BT TO PROVIDE THEM.

WE INTEND THAT THE EXISTING ARRANGEMENTS WHEREBY BT AND POUNC AGREE GUIDELINES ABOUT THE PROVISION OF KIOSKS WILL CONTINUE, WITH POUNC'S FUNCTION TRANSFERRED TO THE DIRECTOR OF OFTEL.

THE CLAUSE 3 GUIDELINES ALSO RECOGNISE THE NEED FOR OPERATORS TO EARN A PROPER RETURN ON CAPITAL SUFFICIENT TO FINANCE THE SUPPLY OF RURAL AND OTHER SERVICES AND THE DEVELOPMENT AND USE OF NEW TECHNIQUES. THIS WILL SAFEGUARD BT'S REMARKABLE R&D EFFORT.

CLAUSE 3 ALSO PROVIDES FOR THE PROMOTION OF COMPETITION AND CONSUMER INTERESTS.

UNDER EXISTING LAW, SERVICES ARE PROVIDED TO CUSTOMERS THROUGH WHAT IS CALLED "A SCHEME".

IN ALMOST ALL CASES, THERE IS, STRANGELY, NO CONTRACTUAL RELATIONSHIP; MOST CUSTOMERS ARE QUITE UNABLE TO SUE BT FOR BREACH OF CONTRACT OR EVEN FOR SOME TORTS.

WE WANT TO CHANGE THIS.

THE BILL THEREFORE ~~LAYS DOWN~~ REPEALS (IN CLAUSE 2) BT'S PRIVILEGES SO THAT SERVICES WILL BE PROVIDED TO USERS UNDER ENFORCEABLE CONTRACTS WHICH WILL GIVE THEM NEW CONTRACTUAL RIGHTS THAT THEY HAVE NOT HAD BEFORE.

MOREOVER, THE CONSUMER REPRESENTATION ROLE OF POUNC WILL BE TRANSFERRED TO THE DIRECTOR GENERAL AND THIS WILL HAVE ONE OVERWHELMING ADVANTAGE.

POUNC HAS DONE EXCELLENT WORK BUT THERE HAVE OFTEN BEEN BEEN COMPLAINTS THAT ~~POUNC~~ IT HAS NO TEETH.

IT CAN MAKE RECOMMENDATIONS, BUT IT HAS HAD NO POWER TO ENFORCE THEM.

THE DIRECTOR GENERAL, UNDER THE BILL, WILL HAVE POWERS - POWERS TO SEE THAT LICENCE CONDITIONS ARE PROPERLY OBSERVED, TO INTERVENE WHEN THEY ARE NOT, TO AMEND LICENCES, TO ENCOURAGE CODES OF CONDUCT, TO PUBLISH ADVICE AND SO ON.

I ALSO INTEND THE DIRECTOR TO TAKE OVER FROM POUNC THE TASK OF AGREEING CONSUMER PERFORMANCE TARGETS WITH OPERATORS.

SO CUSTOMERS, AS WELL AS HAVING THE ADVANTAGE OF MORE COMPETITION, WILL HAVE SUBSTANTIALLY INCREASED RIGHTS AND PROTECTION.

I COME NOW TO THE OFFICE OF TELECOMMUNICATIONS OR "OFTEL", FOR SHORT.

2643 THE NEW REGULATORY SYSTEM ESTABLISHED BY THE BILL IS NECESSARY BECAUSE, FOR OBVIOUS PRACTICAL REASONS, TELECOMMUNICATIONS CANNOT BE A FREE FOR ALL.

THERE HAS TO BE A FRAMEWORK.

UNTIL NOW THIS HAS BEEN PROVIDED BY BT'S "EXCLUSIVE PRIVILEGE" AND ITS MONOPOLY ROLE; IN FUTURE, IT WILL BE PROVIDED BY THE REGULATORY SYSTEM UNDER THE BILL.

PERHAPS AT THIS POINT I CAN DRAW THE ATTENTION OF THE HOUSE TO THE PAPER, IN OUR "RINGING THE CHANGES" SERIES, ENTITLED "REGULATORY ARRANGEMENTS FOR TELECOMMUNICATIONS" WHICH WAS PUBLISHED WITH THE BILL ON 19 NOVEMBER.

IN THAT PAPER I HAVE SET OUT, IN BROAD OUTLINE, HOW WE INTEND THAT THE NEW REGULATORY SYSTEM SHOULD OPERATE.

OBVIOUSLY, ONE OF THE MOST IMPORTANT FACTORS WHICH HAS COLOURED OUR APPROACH IS THE INEVITABLE MARKET DOMINANCE OF BT FOR MANY YEARS AHEAD.

BT HAS SEEN THE REGULATORY SYSTEM AS AIMED PRIMARILY AT THEM.

LET ME MAKE ONE POINT ABUNDANTLY CLEAR: OFTEL WILL MONITOR AND REGULATE ALL TELECOMMUNICATIONS ~~SUPPLIERS~~ OPERATORS, ALL OF WHOM WILL HAVE TO HAVE LICENSES.

THUS, MERCURY, ~~AND~~ THE HULL NETWORK, THE RADIO PHONE NETWORKS, ~~RUN BY THE CITY OF KINGSTON-UPON-HULL~~, WILL BE REGULATED IN THE SAME WAY AS BT.

OFTEL WILL ALSO MONITOR LICENCES GRANTED TO PRIVATE SYSTEMS AND TO PROVIDERS OF VALUE ADDED NETWORK SERVICES.

ALTHOUGH IT IS THE SECRETARY OF STATE WHO GRANTS THE LICENCES, UNDER THE BILL IT IS THE THE DIRECTOR WHO CAN AMEND THEM.

HE WILL DO THIS EITHER BY AGREEMENT WITH THE LICENSEE UNDER CLAUSE 10 OR, IF THE CHANGE IS NOT AGREED, HE CAN MAKE A REFERENCE TO THE MONOPOLIES AND MERGERS COMMISSION UNDER CLAUSE 11.

THE DIRECTOR WILL THEN BE OBLIGED TO PUT INTO EFFECT THE DECISION OF THE MMC WHICH WILL OF COURSE TAKE ACCOUNT OF THE PUBLIC INTEREST AND THE CRITERIA IN CLAUSE 3.

IN THEIR BRIEF TO HON MEMBERS, BT HAVE EXPRESSED ANXIETIES ABOUT THE COMPREHENSIVE NATURE OF THE POWERS IN THE REGULATORY SYSTEM.

I HAVE OF COURSE DISCUSSED THEIR ANXIETIES WITH THEM AT LENGTH AND I BELIEVE THAT I WENT QUITE A LONG WAY TO REASSURE THE BOARD OF OUR INTENTIONS.

WE INTEND THAT THEY SHALL HAVE THE MAXIMUM COMMERCIAL FREEDOM TO OPERATE IN THE MARKET.

WE INTEND THAT THE LICENSING AND REGULATORY SYSTEM SHALL CONSTITUTE, AS IT WERE, A LIGHT REIN, AND THAT THERE SHOULD BE THE MIMIMUM OF INTERFERENCE WITH LEGITIMATE COMMERCIAL DECISIONS.

BT CONTRAST THIS INTENTION WITH THE BATTERY OF POWERS SET OUT IN THE BILL, AND THAT WE HAVE INDICATED WILL BE IN THE LICENSES.

I UNDERSTAND THEIR CONCERN BUT I HAVE TO SAY THIS.

IN THE LAST RESORT, THE GOVERNMENT HAS TO ENSURE THAT THE CRITERIA SET OUT IN CLAUSE 3 ARE MET, AND ~~WE HAVE TO MAKE SURE THAT~~ THE LEGISLATION WILL CONTAIN~~S~~ SUFFICIENT POWERS TO ENSURE THAT THIS CAN BE DONE.

THERE IS OF COURSE NO PRESUMPTION OF GUILT.

LET ME GIVE A PARALLEL.

FOR THE ORDINARY CITIZEN, STATUTE AND COMMON LAW MAY WELL REPRESENT AN IMPENETRABLE MESH OF LEGAL DUTIES AND PROHIBITIONS.

HAPPILY, FOR MOST OF US WE CAN LIVE OUR LIVES LARGELY UNTOUCHED BY ANY OVERT ENFORCEMENT OF THOSE PROVISIONS.

SO IT WILL BE WITH THIS REGULATORY SYSTEM.

THE SYSTEM PROVIDES THE FRAMEWORK, ~~IT SETS THE PARAMETERS~~, IT WILL STATE THE DUTIES AND CONSTRAINTS AND IT PROVIDES THE POWERS TO SEE THAT THESE ARE OBSERVED.

IN PRACTICE, THE BT BOARD WILL BE FREE TO CONDUCT THEIR AFFAIRS WITH THE MINIMUM OF INTERFERENCE AND CONTROL.

AND THE MORE COMPETITION THERE IS, THE LESS WILL BE THE NEED FOR REGULATION.

AS A DOMINANT ENTERPRISE, HOWEVER, BT MUST BE SUBJECT TO SOME CONSTRAINT ON THE PROFITS IT CAN EARN.

WE ENVISAGE THAT THE LICENSE WILL ESTABLISH A REGIME BASED ON THE CONCEPT OF A MAXIMUM REAL RATE OF RETURN ON ASSETS, WITH A SLIDING SCALE TO ENSURE INCENTIVES TO GREATER EFFICIENCY AND ENTERPRISE.

IF IN ANY YEAR THE MAXIMUM RETURN AS SO DEFINED IS EXCEEDED, THEN THERE WILL BE AN OBLIGATION ON BT TO REFUND TO CONSUMERS, THROUGH THEIR NEXT BILLS, ~~THE MAJOR PART OF~~ THE MAJOR PART OF ANY EXCESS PROFITS WHICH THEY MAY HAVE EARNED.

THERE ARE OF COURSE OTHER METHODS OF ENSURING THAT A DOMINANT ROLE IS NOT EXPLOITED, AND THE GOVERNMENT HAVE COMMISSIONED PROFESSOR STEVEN LITTLECHILD OF THE UNIVERSITY OF BIRMINGHAM TO REPORT ON AN ALTERNATIVE ARRANGEMENT.

PART IV OF THE BILL PROVIDES FOR THE FUTURE PRIVATISATION OF BT plc.

WHILE I ANTICIPATE THAT THE REGULATORY SYSTEM INCLUDING THE DIRECTOR GENERAL AND OFTEL WILL BE ESTABLISHED SOON AFTER THE BILL BECOMES LAW, NEITHER THE TRANSFER OF THE ASSETS AND OBLIGATIONS TO THE NEW COMPANY, NOR THE ISSUE OF SHARES TO THE PUBLIC WILL TAKE PLACE BEFORE THE NEXT GENERAL ELECTION.

WE ARE CONTENT THAT THE PUBLIC SHOULD DECIDE WHETHER OR NOT THIS IMPORTANT STEP SHOULD BE TAKEN.

THE FLOTATION IS THEREFORE, I SUSPECT, AT LEAST 18 MONTHS AHEAD. BUT I HAVE ALREADY ASKED BT TO START THE NECESSARY PREPARATIONS AND I HAVE APPOINTED MERCHANT BANKERS TO ADVISE ME.

BEFORE THE ISSUE WE SHALL OF COURSE WANT BT plc TO HAVE A PROPER CAPITAL STRUCTURE AND CLAUSES 54 TO 56 PROVIDE THE NECESSARY POWERS.

CLAUSE 58 IS IMPORTANT.

IT IS THAT CLAUSE WHICH WILL ESTABLISH, BY STATUTORY INSTRUMENT, THE MAXIMUM PROPORTION OF SHARES WHICH MAY BE OWNED BY THE SECRETARY OF STATE OR HIS NOMINEES.

TO ALLOW THE ISSUE OF MORE SHARES TO THE PUBLIC, THAT LIMIT MAY BE REDUCED BY A FURTHER ORDER; BUT ONCE REDUCED IT MAY NOT BE INCREASED.

IN OTHER WORDS, IF AFTER PRIVATISATION, A FUTURE GOVERNMENT SHOULD EVER DECIDE TO REVERSE THIS PROCESS, THEY WOULD HAVE TO COME BACK TO THE HOUSE FOR THE NECESSARY LEGISLATIVE POWERS.

SOMEHOW, MR SPEAKER I DON'T THINK THAT THAT IS GOING TO HAPPEN.

WE ALL REMEMBER HOW THE LABOUR PARTY VOWED IN 1954 THAT THEY WOULD RESTORE THE BBC's MONOPOLY OVER BROADCASTING.

BY THE TIME THEY GOT THE CHANCE TO DO THIS, EVEN THEY REALISED IT WAS ABSURD.

SO IT WILL BE WITH BRITISH TELECOMS.

BEFORE I SIT DOWN I WANT TO DEAL WITH TWO SCARES WHICH HAVE BEEN WORRYING SOME STAFF OF BT - PENSIONS AND JOBS.

I AM IN NO DOUBT THAT THERE IS A GREAT DEAL MORE SUPPORT AMONG STAFF FOR FREEING BT FROM TREASURY CONTROL AND GIVING THEM COMMERCIAL FREEDOM THAN WAS EVIDENT ON THE SO-CALLED DAY OF ACTION BY THE POEU.

INDEED, THE EXTENT OF THE MISREPRESENTATION BY THE POEU IN THEIR JOURNAL AND IN THEIR LEAFLETS IS A MEASURE OF THE WEAKNESS OF THE CASE THEY MAKE.

BUT AS SCARES ABOUT PENSIONS AND JOBS HAVE BEEN PUT ABOUT, THE TRUTH MUST BE RESTATED.

TAKE PENSIONS FIRST.

I HAVE ALREADY GIVEN A CLEAR ASSURANCE THAT EXISTING PENSION OBLIGATIONS WILL BE FULLY HONOURED.

THE BILL CLEARLY PROVIDES, IN CLAUSE 53(1) AND IN PARAGRAPH 12(b) OF SCHEDULE 5, FOR BT's PENSION OBLIGATIONS TO BE HANDED ON TO THE SUCCESSOR COMPANY.

MOREOVER, THE TRUSTEES OF THE PENSION FUND ~~FOR POST OFFICE AND BRITISH TELECOM~~ HAVE THE DUTY OF PROVIDING PENSIONS AND HOLDING PENSION CONTRIBUTIONS IN TRUST.

THE BENEFITS PAID TO PENSIONERS ARE GOVERNED BY THE PENSION FUND TRUST DEED.

UNDER RULES ESTABLISHED BY THIS TRUST DEED BT's PENSIONERS ARE ENTITLED TO PERIODIC INCREASES IN THEIR PENSIONS IN LINE WITH THOSE ENJOYED BY MOST CIVIL SERVANTS.

THE TRUST DEED PROHIBITS CHANGES WHICH WOULD REDUCE THE BENEFITS OF ANY PERSON ALREADY ENTITLED TO THE RECEIPT OF A PENSION.

IT WOULD NOT THEREFORE BE OPEN TO THE SUCCESSOR COMPANY, EVEN IF IT WISHED, TO REDUCE THIS ENTITLEMENT.

EXISTING EMPLOYEES ARE GENERALLY MEMBERS OF THE PENSION SCHEME BY VIRTUE OF THEIR CONTRACTS OF EMPLOYMENT.

AS THEY RETIRE, THEY BENEFIT FROM THE SCHEME'S RULES RELATING TO ITS PENSIONERS.

ANY CHANGE IN THOSE RULES IN RELATION TO EMPLOYEES RETIRING IN FUTURE WOULD REQUIRE THE AGREEMENT OF ALL THE TRUSTEES INCLUDING THOSE NOMINATED BY THE TRADE UNIONS.

AND ALL TRUSTEES ARE REQUIRED BY LAW TO ACT IN THE BEST INTERESTS OF THE TRUST BENEFICIARIES.

SO, WHILE NO-ONE CAN EVER GIVE UNCONDITIONAL GUARANTEES ABOUT THE FUTURE ANY MORE THAN IF BT WERE TO REMAIN A NATIONALISED INDUSTRY, THERE IS SUBSTANTIAL PROTECTION BOTH FOR BT's PENSIONERS AND FOR BT's EMPLOYEES UNDER THE TRUST ARRANGEMENTS.

THERE IS NOTHING IN THIS BILL TO CHANGE THAT PROTECTION WHEN BT IS TURNED INTO A PUBLIC LIMITED COMPANY.

I HOPE THAT THE BT UNIONS WILL THINK IT RIGHT TO GIVE AS MUCH PUBLICITY TO THOSE STATEMENTS AS THEY HAVE GIVEN TO THEIR SCARE STORIES.

THEN THERE IS THE QUESTION OF JOBS.

CERTAINLY, THERE IS AMPLE SCOPE FOR INCREASED EFFICIENCY IN BT, AS BT's MANAGEMENT RECOGNISED WHEN THEY CALLED LAST YEAR FOR A 25 PER CENT INCREASE IN PRODUCTIVITY.

I HAVE NO DOUBT THAT, IF BT STAYED NATIONALISED WITH ALL THE CONSTRAINTS ON FINANCE AND COMMERCIAL FREEDOM, HIGHER PRODUCTIVITY AND NEW TECHNOLOGY WOULD STEADILY REDUCE THE NUMBER OF STAFF AS FEWER PEOPLE WOULD BE REQUIRED TO MAN THE NEW EQUIPMENT.

BUT WITH THE NEW COMMERCIAL FREEDOM WHICH THIS BILL PROVIDES, AND WITH THE NEW OPPORTUNITIES WHICH FINANCIAL FREEDOM CONFERS, THERE IS ABSOLUTELY NO REASON AT ALL WHY EMPLOYMENT OPPORTUNITIES IN TELECOMMUNICATIONS SHOULD NOT EXPAND IN BRITAIN JUST AS THEY HAVE BEEN EXPANDING, FOR INSTANCE, IN THE UNITED STATES.

IF IT IS REALLY JOBS WHICH WORRY THE UNIONS, THEN LET THEM EMBRACE THIS BILL FOR IT IS THE BEST GUARANTEE OF EXPANDING JOB OPPORTUNITIES THAT THEY HAVE.

MR SPEAKER, THE CASE FOR THIS BILL IS AN OVERWHELMING ONE.

THE NEW TECHNOLOGY WHICH IS NOW AVAILABLE MEANS THAT STATE MONOPOLY IS NOT ONLY UNNECESSARY; IT HAS BECOME A SIGNIFICANT BRAKE ON PROGRESS.

AT A TIME WHEN MOST OF THE WORLD IS IN RECESSION, AND WHEN NEW JOB OPPORTUNITIES ARE HARD TO IDENTIFY, IT CANNOT BE RIGHT TO KEEP THIS GROWING INDUSTRY IN THE ~~STRAIT~~ STRAIGHT-JACKET OF NATIONALISATION.

THE PUBLIC ISSUES OF CABLE AND WIRELESS AND OF ~~STANDARD TELEPHONES AND CABLES~~ STC SHOWED THAT THE MARKET IS VERY READY TO FINANCE THE FAST EXPANDING WORLD OF TELECOMMUNICATIONS.

FOR SO LONG AS BT REMAINS IN THE PUBLIC SECTOR, THAT FINANCE CANNOT BE TAPPED, THAT EXPANSION CANNOT TAKE PLACE AND THOSE JOBS CANNOT BE PROVIDED.

THIS BILL WILL GIVE TO BT THE FREEDOM TO COMPETE, THE FREEDOM TO DIVERSIFY, THE FREEDOM TO EXPAND, WHICH AS A NATIONALISED INDUSTRY IT COULD NEVER HAVE.

I ASK THE HOUSE TO SUPPORT THE BILL IN THE LOBBY TONIGHT.

cc JV

RESTRICTED

DEPARTMENT OF INDUSTRY
ASHDOWN HOUSE
123 VICTORIA STREET
LONDON SW1E 6RB
TELEPHONE DIRECT LINE 01-212 3301
SWITCHBOARD 01-212 7676

JU190
Secretary of State for Industry

18 November 1982

David Heyhoe Esq
Private Secretary
to the Lord President & Leader of the
House of Commons
House of Commons
London SW1

Prime Minister (2)

MCS 18/11

Dear David

TELECOMMUNICATIONS BILL

My letter of 17 November to Michael Scholar enclosed a note describing the role and function of the Office of Telecommunications which will be distributed tomorrow morning to all Members of Parliament.

2 It has been pointed out to us that the Opposition may attempt to exploit the note to delay the Second Reading of the Bill and its submission to Committee. They might, for example, argue that the circulation of the note underlines the complexity of the proposals and that, if the proposals are indeed so complex that they require 13 pages of explanation, the House will require more than two weekends to study the Bill before its Second Reading.

3 The Lord President will wish to refute this suggestion. The note has been prepared at the request of the Trade Associations and others and is designed for circulation to individual firms and members who would not normally read the text of the Bill. Those who have pressed the Department to produce the note include the Post Office Engineering Union. Once the note had been prepared my Secretary of State thought it a courtesy to send a copy to every Member of the House to help them in answering constituents' letters and dealing with enquiries. I am copying this letter to Michael Scholar and to Murdo McLean.

Yours sincerely
David Saunders

DAVID SAUNDERS
Private Secretary

Post & telecoms

future of PO

pt 6

JH 300

Post x-section
✓JV

DEPARTMENT OF INDUSTRY
ASHDOWN HOUSE
123 VICTORIA STREET
LONDON SW1E 6RB
TELEPHONE DIRECT LINE 01-212 3301
SWITCHBOARD 01-212 7676

Secretary of State for Industry

17 November 1982

M Scholar Esq
Private Secretary to the
Prime Minister
10 Downing Street
London SW1

Prime Minister (2)

MCS 17/11

Dear Michael

TELECOMMUNICATIONS BILL: ARRANGEMENTS FOR INTRODUCTION

Following Legislation Committee's decision to agree, subject to conditions, the introduction of the Telecommunications Bill, arrangements have been made for the Bill itself to be published on Friday 19 November. My Secretary of State is holding a press conference that morning.

2 My Secretary of State considers that the length and complexity of the Bill make it necessary to provide Members of Parliament and members of the public with a detailed explanation of the regulatory arrangements in everyday language. He therefore intends to send the enclosed note to all Members of Parliament so that they receive it shortly after the Bill is published on Friday morning. Copies will also be available in the Vote Office and will be given to the press.

3 The note describes the proposals in the Bill as introduced. It does not enter into discussion on any of the points on which policy decisions are still outstanding and my Secretary of State has been careful to stress in the final paragraph that the Government keeps an open mind on many of the details of the policy.

4 Copies of this letter go to the Private Secretaries to members of the Cabinet, the Chief Whip, and to Richard Hatfield (Cabinet Office).

Yours sincerely
David Saunders

DAVID SAUNDERS
Private Secretary

REGULATORY ARRANGEMENTS FOR TELECOMMUNICATIONS

THE ROLE AND FUNCTIONS OF THE OFFICE OF TELECOMMUNICATIONS (OFTEL)

Introduction

The Government plans to convert British Telecommunications (BT) into a public limited company (plc) and to sell 51% of its shares following the next General Election. BT is at present a statutory corporation with duties to provide public services imposed by the BT Act 1981. It is subject to a number of Government controls over such matters as its borrowing plans and investment proposals etc and can be given directions on some matters by Ministers. The Government wishes BT plc to have as much commercial freedom as possible and intends to free BT plc from the existing web of Government controls.

2 Nevertheless, the Government believes that the telecommunications industry cannot be free of all controls:

- First, telecommunications are essential for industry and commerce and for the fast expanding information technology industries. Telecommunications are also vital for personal use especially by those isolated by age, infirmity or geography; and for national defence. The Government wants to make sure that, after privatisation, telecommunication services will in fact be provided to meet the reasonable needs of all the nation;

- Second, BT is the dominant supplier of most telecommunications services and the Government wishes to be able to ensure that after BT is transferred to the private sector those who own, manage and work in BT plc do not use this market dominance to make excessive profits, operate inefficiently or to prevent or restrict the development of competition in telecommunications.

The Government will therefore set up an Office of Telecommunications (OFTEL) under an independent Director General who will have powers to safeguard the interests of domestic and business users of telecommunications in all parts of the country and to protect fair competition.

3 This note explains the Government's proposals for these new regulatory arrangements.

Regulation of the Market

4 The conversion of BT into a plc and the sale of 51% of its shares will help to ensure that BT plc is subject to an increasing measure of influence by market forces and disciplines. BT plc's Board of Directors will, like the Board of any other plc, be responsible to their shareholders for the successful operation of the business. In order to raise capital from the market for expansion BT plc will need to demonstrate that it is an efficient and profitable organisation.

5 Although the present BT Board is responsible for running the business, they are subject to a number of controls - particularly over borrowing - by Ministers, who in turn are responsible to Parliament. On top of this there are the series of statutory duties. As Governments have changed, the Ministerial controls have been exercised in different ways. This lack of consistency would be undesirable for any business but has been especially damaging in the case of telecommunications which are so essential for the nation. Privatisation will free BT plc from most Ministerial controls, give it a more precise set of public service obligations and insulate BT's business from political interference.

6 This new freedom will give those who manage and work in BT the opportunity to pursue consistent technical and commercial strategies. Once BT plc is operating in a commercial environment, it will be possible for technical and commercial energies to be directed to providing the customer - both domestic and business - with the goods and services that he or she wants and is willing to pay for.

7 This commercial control will be most evident in BT plc's investment programme and its borrowing, which will be determined by market considerations and its Articles of Association once 51% of BT plc's shares have been sold. At present the Government has the final say over what BT should be allowed to borrow each year after considering not only the needs of the business but also, necessarily, the general public expenditure climate. This has meant that BT has not always been allowed to borrow all the Board believed to be commercially justified and the consequences of inadequate investment in the past are with us now. Once shares in BT plc have been sold to the public, there will be other criteria affecting BT's borrowing and investment programme, for example, the return on investment will have to be sufficient so that shareholders, City institutions and banks will provide the money needed. This will mean that worthwhile and profitable investment should be financed regardless of public sector borrowing requirement rules and that BT's proposals will be subject to scrutiny by the market.

8 These benefits will complement the growing advantages flowing from the development of competition under the Government's policy of liberalisation of telecommunications. Briefly, the Government is making arrangements for telecommunications users to have a choice

- of network: Mercury and the private sector radiotelephone company will give business and some other users a choice of telephone company when they want to make a telephone call;

- of services: users will have a choice of company when they want a service provided over the telephone; and

- of apparatus: users will have the choice of whether to buy or rent most of their telecommunications apparatus from private companies or from BT.

Where competition exists users will be able to see whether BT's service is as good as the competition's and to choose which one they think is better in terms of quality, speed of delivery and price. The stronger the forces of competition, the less need there will be for regulation. As liberalisation proceeds, it will be the market rather than formal regulatory arrangements which will regulate the way BT plc behaves.

9 Commercial considerations will also affect the way BT provides its services. At present BT does not generally provide services under contract, and customers cannot usually sue BT for negligence etc. The Bill will require BT plc to provide its services under contract and BT plc will not have immunity from civil action (except in respect of international calls which are subject to international agreements). Users will be able to take BT to court to obtain redress, just as they can sue, say, a shop which supplies faulty goods.

The need for regulation

10 The introduction of private capital and increased commercial influences on BT's articles will not be sufficient to ensure that:

a) BT plc continues to provide services such as those to remote and rural areas, emergency services and telephone kiosks;

b) BT plc continues to provide the systems and services necessary for national security; and

c) BT plc cannot exploit any dominant position it may have in any part of the telecommunications market.

Moreover, it cannot be assumed that BT plc's competitors will provide essential social and defence services on the scale the nation requires. The Government therefore intends to establish regulatory arrangements to deal with these problems.

Essential Services

11 BT's duties as a statutory corporation include an obligation "to provide throughout the British Islands (save in so far as they are provided by other persons or the provision thereof is, in its opinion, impracticable or not reasonably practicable) such telephone services as satisfy all reasonable demands for them". BT has fulfilled its obligation by providing services in nearly every part of the country, including rural and remote areas where the provision of telephone services might not be justified on purely commercial grounds. BT has also accepted other obligations like the loss-making 999 service, the network of telephone kiosks which made heavy losses last year but which is of great importance for many communities, particularly in rural areas and special facilities for blind, deaf and disabled people. In addition BT provides certain services which are essential to national security and defence.

Market Dominance

12 The prospect of increasing competition is already having its effect in a number of aspects of BT's business; for example BT has already reduced charges on its 100 most densely used trunk routes and there has been a significant reduction in the price of telex teleprinters following liberalisation. Nevertheless, BT can be expected to dominate some sectors of the telecommunications markets for a considerable period. This applies especially to the supply of telephone services to domestic subscribers and to business subscribers away from major cities. In these sectors it will be necessary to ensure that customers' interests are properly safeguarded, whilst permitting BT plc to earn a proper return on capital.

Licensing

13 When the Telecommunications Bill becomes law, BT will lose what is called its "exclusive privilege" which it now enjoys over the running of telecommunications systems and the provision of telecommunication services. Instead it will operate under a licence just as the City of Kingston upon Hull network and the telephone

network now being installed by Mercury Communications Ltd operate under licences. All licences will be issued by the Secretary of State and detailed provisions are made in the Bill about licences. The Bill also provides for the ending of BT's present power to grant licences.

14 The Secretary of State's power to issue licences and to include conditions in them will apply equally to any person or company which is allowed to run a public telecommunications system. BT plc will not be singled out for special controls but, since BT runs what is by far the largest and most important network and since its activities are so vital to the nation, its licence will need to be negotiated with particular care.

15 The Government intends to consult fully with BT about the proposed terms and consitions of the licence. The licence will initially be issued to BT shortly after the Bill receives the Royal Assent but will be transferred to BT plc when BT's rights and obligations are vested in the new company. The Government intends that the BT licence should have broadly the following shape:-

a) a description or specification of the systems that BT is permitted to run and the services that may be supplied over those systems. This is expected to be in very general terms to reflect BT's existing universal network;

b) a condition requiring BT to provide such telecommunications services as meet all reasonable demands for them in all parts of the United Kingdom (and therefore including not only all rural and remote areas to which it is practicable to provide services but also the special telecommunication facilities required by the City of London);

c) conditions requiring BT to provide 999 and telephone kiosk services;

d) conditions requiring BT to permit connection to its system on appropriate terms and conditions of:-

i) apparatus that meets approved standards which has been supplied by companies other than BT;

ii) other licensed systems (eg Hull, Mercury and the radiotelephone company, but also privately owned PABX (Private Automatic Branch Exchange) and other systems);

thus ensuring the development of competition in the supply of telecommunication apparatus and in the supply of telecommunications services in accordance with the Government's policies on the liberalisation of telecommunications;

e) conditions relating to acts or omissions which might prevent, distort or restrict competition;

f) conditions with regard to the rate of return on capital BT is able to earn on its regulated activities (broadly those in which it has a dominant position and where it faces little effective competition), whilst maintaining incentives not only to improve efficiency and quality but also to expand its services;

g) a condition requiring BT to pay a licence fee;

h) conditions requiring BT to provide the Director General of Telecommunications (see below) with information to enable him to ensure that licence conditions are being observed and to follow up consumer complaints;

i) conditions relating to the preparation and presentation of accounting information for the Director General.

The Director General of Telecommunications

16 The task of checking whether licensees observe their obligations to provide services and of monitoring whether there is fair competition (ie fair to BT as well to its competitors) in all parts of the telecommunications market will require a detailed and expert knowledge not only of telecommunications technology but also

of the commercial aspects of telecommunications. Monitoring will need to be carried out in a consistent and informed manner over the years to reflect the long lead times of telecommunications investment. Monitoring must also be insulated from day to day political pressures so that those planning and investing in major developments will have an assurance of stability. The Government has therefore decided to establish a new Office of Telecommunications to build up expert knowledge and to carry out monitoring functions.

17 The Director General himself will be an independent Officer of the Crown appointed for a fixed but renewable period of five years on terms which will provide him with the same degree of independence as the Director General of Fair Trading. The Director General will be able to recruit people from outside the Government service with expert knowledge but, as in the case of the Office of Fair Trading, members of the staff of the Office of Telecommunications (OFTEL) will be Civil Servants and will be subject both to the Official Secrets Act and to additional legal duties to oblige them to protect the commercial secrets they learn in the course of their work.

18 The Director General and OFTEL will have the following functions:-

a) monitoring observance by licensees of the obligations and conditions set out in their licences;

b) monitoring abuses of monopoly situations by those carrying on commercial activities relating to telecommunications and anti-competitive practices which have effects on the supply of telecommunications services and apparatus;

c) receiving and considering represenations by consumers and other users of telecommunication services;

d) providing the Secretary of State and the Government with advice on telecommunications matters;

e) carrying out on the Secretary of State's behalf such of his functions under the Bill as he may delegate to the Director General;

f) monitoring and if necessary prosecuting those who run unlicensed systems or who breach consumer protection legislation on the marking and advertising of telecoms apparatus.

Monitoring of Telecommunications Licence Conditions

19 The Director General will be required to keep under review the way licensees observe their licence conditions. If, for example as a result of public complaints, it appeared to the Director General that BT plc might not be providing adequate telephone services in rural areas he would have power to intervene. He would first ask BT plc for their comments on the complaints. If the complaints were shown to be well founded, the Director General would have power to order BT plc to comply with the terms of its licence (eg to make telephone lines available to customers in the area in question on payment of reasonable charges). Orders would only be issued after notice and a formal opportunity for the licensee to object but, if the licensee did not implement an order once issued, the Director General could seek a civil remedy in the Courts.

20 In the light of experience the Director General might conclude that the conditions included in a licence were not adequate. For example a new condition might in his view be needed to deal with a practice which had not been anticipated when the licence was issued Alternatively, he might conclude that an existing licence condition was unduly onerous and might need to be relaxed or deleted. He will therefore have powers to propose licence variations. If the licensee concerned agrees with the proposed variation (and if the Director General, who would be required to publicise his proposal, does not change his mind because of representations from other interested parties), the Director General will be able to vary the licence condition in question. If, however, a licensee objects to a proposed licence amendment which the Director General thinks necessary, the Director General will be able to refer the question to the Monopolies and Mergers Commission and, if they conclude that a variation is desirable in the public interest, he will be able to make the variation despite the objections of the licensee.

Monopoly Abuses and Anti-Competitive Practices Relating to Telecommunications

21 Licensing arrangements will ensure that the Director General has powers to regulate any monopoly abuse or anti-competitive practice on the part of a licensee in activities directly related to the running of his system. But many telecommunication activities, for example the manufacture and retailing of telecommuncation apparatus, in which both BT plc and others participate, will not be subject to direct licensing controls under the Bill. But they are an area where monopoly abuses and anti-competitive practices are possible, for example a supplier, who might be BT plc or another company, might refuse to sell to customers one item of appartus (eg a PABX) unless they also bought from him all the extension apparatus connected to the PABX. Anti-competitive practices such as this can at present be remedied by orders made following investigations made under the Fair Trading Act 1973 and Competition Act 1980. These activities are the responsibility of the Director General of Fair Trading.

22 The Government considers that it would be inappropriate for the new Director General of Telecommunications to be responsible for dealing with some monopoly abuses or anti-competitive practices by licence conditions but for a different officer, the Director General of Fair Trading, to deal with similar abuses and practices if they are carried out by non licensees. Such a division of responsibilities would create confusion and it might result in one company being subjected to investigations by both Director Generals in respect of the same abuse or practice. Consequently the Government intends the new Director General of Telecommunications to exercise responsibilities for keeping under review all commercial activities relating to telecommunications and for making investigations and references to the Monopolies and Mergers Commission in respect of monopoly situations and anti-competitive practices in that area. The Director General of Fair Trading will, however, continue to have exclusive responsibility for all mergers and restrictive trade agreements affecting telecommunications; the new Director Geneal will have no powers in these two areas but will be required to give the Director General of Fair Trading any information he may have affecting a merger or restrictive trade agreement affecting telecommunications.

Consumer Protection

23 Under the Government's proposals consumers will have greater protection than at present, in particular:-

a) they will have greater choice and therefore an increased opportunity to obtain the telecommunications services or appparatus that suit their particular requirements;and

b) BT will provide services under legally enforceable contract.

24 However, most domestic subscribers will have no effective choice of network for the foreseeable future and the conversion of BT into a plc will mean that the Post Office Users' National Council (POUNC) and its Country Councils will no longer deal with telecommunications. The Bill therefore puts the Director General under a duty to consider complaints and representations about telecommunication apparatus and services, so that, in effect, he will take over POUNC's existing functions in relation to consumer complaints. He will also be required to appoint advisory committees in Scotland, Wales and Northern Ireland similar to POUNC's Country Councils and there will be provision for direct Government finance for local Postal and Telecommunication Advisory Councils who assist the Director on telecoms matters.

25 In the past POUNC has been criticised for "lacking teeth", that is, for not having effective powers to back up any criticism it made of BT's performance. The Government believes that combining under one Office POUNC's previous role of considering complaints and the new powers to monitor observance of licences, to issue orders to ensure compliance with licence conditions and to initiate licence amendments will ensure for the first time that there are effective powers to provide remedies when investigation of user complaints discloses unsatisfactory performance by licensees.

26 The Government expects the Director General to take over POUNC's non-statutory functions for example in the agreement of guidelines governing uneconomic telephone kiosks. The Government intends that the Director should

carry on POUNC's role of agreeing, on a non-statutory basis, performance objectives with licensees on such matters as the time taken to install exchange lines, the time taken before repairs are made and so on.

Advisory Functions

27 The Government believes that there will be considerable advantage if it has available the advice and experience of an independent body like OFTEL which is expected to build up expert knowledge of all aspects of telecommunications. Previously BT has been the Government's main source of such advice but the advent of competition, which has made BT one competitor among many in the market place, means that a new independent source of advice is needed. The Bill provides for the Director General to be asked to give advice and or him to offer advice if he thinks it appropriate to do so.

Functions carried out on Behalf of the Government

28 It is intended that the Government should remain responsible for licensing telecommunications systems, particular public telecommunication systems. But many telecommunication systems (eg taxi radio systems), which require licences under the existing legislation will continue to require licences in future. Hitherto BT has licensed these. This role will under the Bill fall to the Government which will have powers to delegate such routine licensing functions to OFTEL. It is not intended to give OFTEL any power to issue licences under the Wireless Telegraphy Act; that reponsibility will remain with the Home Office.

29 The Government intends to make provision to continue the existing arrangements under which apparatus must conform to approved standards and be tested and approved before it is connected to telecom systems but to clarify and extend the arrangements. Standards are being written under the auspices of the British Standards Institution and subsequently approved by the Secretary of State. Apparatus is being tested and approved by the British Approvals Board for Telecommunications. These arrangements will continue. Then again, the Government proposes to take powers to allow it to delegate the function of approving standards if in due course that seems desirable. Similarly the Bill will

contain powers to delegate the task of approving apparatus but the Government does no intend to use these powers for the time being.

Policing Marking and Advertising Orders

30 The British Telecommunications Act 1981 made provision for Orders requiring apparatus to be marked when offered for sale to show whether or not it is approved for connection to BT's networks and for Orders requiring advertisments, catalogues and other sales material to indicate whether or not the advertised goods are approved for connection. While the main provisions of these orders came fully into force on 1 November 1982, others have been in force for several months. It is becoming apparent that the Orders are not being effectively enforced and the Bill will confer on the Director General a power to enforce the Orders, undertaking prosecutions if necessary. In the case of traders who commit repeated breaches of the Orders it is intended that the Director General of Telecommunications should be able, with the consent of the Director General of Fair Trading, to use the powers under Part III of the Fair Trading Act 1973 to seek undertakings from, and if necessary to take action in the courts against, such traders.

Representations

31 The Telecommunications Bill provides the statutory powers and duties necessary to implement the arrangements described above. A number of obligations will be embodied in the licences to be issued to BT and other licence holders. Either House of Parliament can amend the Bill during its passage through Parliament in accordance with normal procedures. At the same time, the Government are very ready to consider in parallel proposals and representations from members of the public about any aspect of the proposed changes. Any such comments, proposals or representations should be sent in writing to Miss G M A Lambert, Telecommunications Division, Department of Industry, 123 Victoria Street, London SW1.

CONFIDENTIAL

DEPARTMENT OF TRADE 1 VICTORIA STREET LONDON SW1H 0ET Telephone 01-215 7877

From the Secretary of State

Prime Minister (2)

Lord Cockfield clearly thinks that the BT Bill is moving too fast, and needs more thought.

MCS 12/11

The Rt Hon Patrick Jenkin MP
Secretary of State for Industry
Department of Industry
Ashdown House
123 Victoria Street
London
SW1E 6RB

11 November 1982

Dear Secretary of State

TELECOMMUNICATIONS BILL

Thank you for your letter of 1 November setting out some of your ideas on the future regime for telecommunications. I have also seen your minute to the Prime Minister of 8 November.

Your letter did not deal with all aspects of the Bill; and there are some areas which I shall want to look at more fully when work on them is more advanced. In particular, I shall be interested to see your report to E(TP) on a single or two-tier rates of return, or a profits tax, in the light of Professor Littlechild's study. Meanwhile, a range of important issues on the Bill remain to be settled, and I have specific comments on aspects where my Department is particularly concerned.

My first concern is with British Telecom's efficiency, given the efficiency audit concept which we introduced in Section 11 of the Competition Act 1980. Our common assumption has always been that the powers to investigate BT's efficiency via the MMC would be used automatically, at regular intervals related to setting BT's rate of return. I understand that in the event the Bill does not re-enact Section 11 of the Competition Act so as to bring it to bear on a privatised British Telecom. Instead, the Director General of Telecommunications (DGT) will be able to make monopoly references to the MMC under the Fair Trading Act 1973, as well as having a new power to refer licence variations to the MMC. As a

From the Secretary of State

result, the Bill does not itself contain any explicit concept that there will be a periodic investigation of the efficiency of BT's monopoly, leading to a published report. We need to have a clear public stance on this. It could be established either in the Bill or in the licence conditions (which are obviously becoming an important part of the whole regulatory system). Parliament and the public will need to know our position, and to be assured that the system for controlling the monopoly, striking a balance between preventing abuse and promoting efficiency, is no less effective than the review system in our 1980 Act. Could you let me know what your current proposals are on this?

Next, I am concerned about the powers proposed for the Director General of Telecommunications. As regards licensed telecommunications systems, he should exercise some of the functions currently exercised by the Director General of Fair Trading under the Fair Trading Act 1973 and the Competition Act 1980. But why should his powers in the competition field go significantly wider than the licensed area? The creation of the Director General of Telecommunications, with functions under the Fair Trading Act or the Competition Act, should not be seen as betokening any drift towards weakening our policy towards competition. It would be damaging if the legislation were seen as whittling away the scope of the Director General of Fair Trading's activities, leading to inconsistencies of policy through a division of responsibilities. Your officials and mine have been discussing the best means of avoiding an exessively wide definition of telecommunications in the Bill. My own view is that this is an important problem which we must resolve in the Bill, not postpone to subordinate legislation. The two Directors will need to work together; and flexible machinery must be provided in the Bill so that problems do not later arise with adverse effects for Government resources on the one hand and the business community on the other.

CONFIDENTIAL

From the Secretary of State

I also have some points on your points on your proposals on consumer protection. As a general matter, I agree with you that the rights of BT's customers must be secured, and BT's privileges removed; and I hope our officials will soon complete their work on this. As for the consumer protection machinery in the Bill, while we had some hesitations about the proposal to oblige the DGT to set performance objectives for BT to try to meet, we are content with this as it stands in the latest print of the Bill. But I understand that you are now thinking of dropping it. That would leave quite a hole in the Bill as regards the consumer interest in both quality of service and the efficient use of resources. If it is dropped, it will be important to make clear during the passage of the Bill that the DGT will play much the same role in relation to "customer performance targets" and so on as the Post Office Users National Council (POUNC) has played to date. Indeed, that the licensing mechanism will mean that he can turn such targets into more effective disciplines than they are at present. As a separate matter, our officials have been in touch about the need to provide for continued financial support on the modest scale (under £30,000 a year) required to enable the Post Office Advisory Committees (POACs) to liaise with BT management at local level, and about the Bill's provisions on individual customers' complaints, which OFTEL will need to be able to handle on broadly the same basis as POUNC and the POACs do at present.

Finally, further thought needs to be given to the role of the Monoplies and Mergers Commission, and its relationship with the DGT. The Bill makes an innovation in providing for licence variation references to the MMC; and in these cases it is proposed that the MMC report to the DGT, not to Ministers. But this means that it will be open to the MMC to reach public interest findings on a wide range of issues (eg the provision of uneconomic services as a licence condition) and that it will be left to an official, rather than to Ministers, to act on the MMC's report, without Ministers having the opportunity (as in the

CONFIDENTIAL

From the Secretary of State

case of all MMC reports at present) to interpose their view in deciding on measures to be taken in the public interest. This is quite wrong. It ought to be the responsibility of Ministers to act on MMC reports, and it is quite indefensible to suggest that the job can be fittingly left to an official. I anticipate questions on this point, and should like to be clear of your own views on it.

In your letter you have pointed to the need for speed, and you have said that no further major amendments can be made to the text of the Bill before the Legislation Committee print. Neither I nor, I suspect, some of my colleagues will be prepared to accept that difficult issues should be brushed aside in this way.

I am copying this letter to the Prime Minister, the Home Secretary, the Chancellor of the Exchequer, the Secretaries of State for Scotland, Northern Ireland and Wales, the Minister for Agriculture, Fisheries and Food, the Secretary of State for the Environment, the Chancellor of the Duchy of Lancaster, the Lord Privy Seal, the Chief Secretary and the Chief Whip, and to John Sparrow and Sir Robert Armstrong.

Yours sincerely

RP LORD COCKFIELD

[Approved by the Secretary of State and signed in his absence.]

Post & Telecomms

Future of Post office

CONFIDENTIAL

File
bc JV
Post + Tels.

SUBJECT.

10 DOWNING STREET

cc. Master ack.

From the Private Secretary

9 November 1982

BRITISH TELECOMMUNICATIONS: REGIONALISATION

The Prime Minister held a discussion this morning on the issues raised in the note attached to your letter to me of 13 October. The Home Secretary, the Chancellor of the Exchequer, the Minister of State, Industry (Mr. Baker), Sir Robert Armstrong, Mr. Sparrow and Mr. Walters were also present.

The Prime Minister said she was attracted to the idea of having a number of local telephone companies instead of one national monopoly. It would enhance competition in telecommunications, and would provide a means of comparing the performance of one company with another. A local monopoly would be subject much more to local control, and local companies would have both incentives and opportunites to innovate and try new techniques. Your Secretary of State said he had considered this matter carefully and he saw the advantages of breaking up BT into local companies. But BT had no management or accounting system which would enable such a break-up to be brought about. Sir George Jefferson had found not one qualified accountant in any one of BT's 61 areas when he took over as Chairman. Devolved accounting and management arrangements were now in process of being introduced. But it would take many years to set in place a structure of successor companies to BT, and to identify the assets and liabilities to be allocated to each company. These measures would postpone flotation of BT for many years. There would be, furthermore, very considerable opposition within BT to privatisation on a devolved basis. The network was an integrated one (unlike the position in America). Finally, breaking up BT would damage consumer interests, particularly in rural and remote areas.

The Prime Minister said that she did not agree with a number of these arguments. But it had to be accepted that to embark now upon breaking up BT into local companies would set back privatisation to an unacceptable extent. She regretted that these issues had not been thoroughly displayed at a much earlier stage.

I am sending copies of this letter to the Private Secretaries to those present at this morning's meeting.

M. C. SCHOLAR

Jonathan Spencer, Esq.,
Department of Industry.

MR. SCHOLAR

PRIVATISATION OF BRITISH TELECOM: SECRETARY OF STATE'S MEMORANDUM OF 8 NOVEMBER 1982

One reform in the Secretary of State's memorandum is that now they have eliminated the 100% marginal rate of tax. This at least helps a bit. But, as you can see in paragraph 3, there is still the requirement to have efficiency audits by the bureaucracy and almost certainly tariff control - but the Secretary of State does not talk about that. I would expect Kleinwort's to advise that such a system would be accepted by the market. After all, it is broadly the same system that is used in America, with the most enormous bureaucratic regulation system behind it in many industries. It is also more or less the same as the system we use to control the nationalised industries - such as railways and electricity. It has resulted in railways and the electricity industry raising their tariffs during the slump in order to cover their costs and achieve a cash target. In electricity, for example, tariffs have been raised much above costs because of the low loading of expensive electricity equipment. This is the opposite of what we want to see.

In paragraph 4, he mis-states my suggestion. The amount would not decrease the more BT increased its output. The whole point is that the percentage scale of profits tax would decrease the more BT increased its output. It is not an output-related tax as such, it's an output-related percentage tax.

It is true I have not had the opportunity to develop my ideas in detail. It requires both an analytical treatment and probably also a computer modelling of the implications. And I agreed that Littlechild of Birmingham was one, of a list of three, who would be suitable for doing this job.

Littlechild came to see me this afternoon. He has not yet got his terms of reference from the Department of Industry. He had, however, seen Kleinworts and had a standard list of problems. They were easily dealt with.

I would like to emphasise that I do not know whether my idea is the best that could be thought up. What I do know, however, is that the drift of the DoI suggestions, is both familiar and bad. This we

/know

know from experience. It seems to be a case of pursuing the known failure rather than the unknown, but possible success. One can easily see if we pursue the known failure route then nobody can be criticised.

It is perfectly true that my suggested solution is a radical one. It is designed not to nullify the profit motive, but to magnify it. Since we have been busily muting or stifling the profit motive for so long, it is understandable that any suggestion that would magnify it comes as a shock. But there it is. Somehow we must break out of this lethargy and the path of familiar failure.

8 November 1982 (Dictated but not seen by AAW) ALAN WALTERS

JF1937

CONFIDENTIAL

ADW

(2)

Prime Minister

To note (please also see Alan Walters' note on this, attached).

MCS 8/11

PRIME MINISTER

PRIVATISATION OF BRITISH TELECOMMUNICATIONS

When E(TP) agreed my proposals for the regulation of British Telecommunications plc at their meeting on 30 June (E(TP)(82)2nd Meeting), we decided to investigate further the question of how to prevent BT exploiting the dominant position it will continue to hold in important parts of the telecommunications market by overcharging subscribers or tolerating inefficiencies. I was invited to arrange for officials to consider the respective merits of imposing in BT's licence a single maximum rate of return, a two-tier maximum rate of return and a profits tax.

2 These issues have been considered by a working group of officials drawn from the Department of Industry, the Treasury, the Department of Trade and the CPRS in order to fulfil the remit from E(TP). Kleinwort Benson, my merchant bank advisers, also participated. I had hoped that Alan Walters (or his nominee from the Policy Unit) could also join the study, but I understand that this did not prove possible. I therefore had a long meeting with Alan myself last month. Paragraph 4 below reports the outcome.

3 Officials and Kleinworts agreed that a two-tier maximum rate of return procedure would be appropriate. Under this BT would be allowed to earn up to a previously specified rate of return,

say 6% per annum on a CCA basis, and would pay back a major part of any excess over the limit as a rebate to subscribers, the rebate being fixed on a sliding scale so as to avoid 100% marginal rates of tax. In addition the Director General of Telecommunications would be able to agree with BT some relaxation in the limit (so that BT for example might retain all its earnings up to a maximum of 6.6%) in return for meeting a series of previously agreed performance targets. This would give BT an incentive to increase its efficiency and its quality of service whilst ensuring that the consumer did not pay excessive prices. I am satisfied that arrangements on these lines would provide a practical and acceptable solution to the problem which concerned us. Kleinworts advise that such a system would be accepted by the market.

4 Alan Walters, however, told me that he still considers that we would be much better advised to go for an output-related tax, the amount of which would decrease the more BT increased its output above a previously agreed level. At our meeting, he explained that owing to pressure of other work he had not had time to develop his ideas in full detail. I am, however, attracted by many aspects of his proposal and, after a lengthy discussion, I suggested that, whilst I should go ahead with introduction of the Telecommunications Bill on the basis of the proposed two-tier control on BT's maximum rate of return, I should commission an independent economist to develop Alan's ideas and compare their strengths and weaknesses with the

proposals put forward by officials. With Alan's agreement, I have asked Professor Littlechild of the University of Birmingham to carry out this study which will be completed in time for me to amend the Bill during its passage through Parliament if we decide that this would be desirable. I should perhaps add that Kleinworts feel that the novelty of such an output-related tax could confuse the market and so make privatisation more difficult. However, I will report further to E(TP) Committee when I have received Professor Littlechild's study.

5 E(TP) also asked me to reach agreement with the Treasury on the relationship between BT plc and the Government in any interim period after the first sale of shares during which BT plc might remain in the public sector. The Chancellor and I have now agreed that it would be best to deal with this problem by including a suitable provision in the Articles of Association of BT plc, underpinned by a short clause in the Bill.

6 This I think deals with both the points which we left outstanding after our discussion in E(TP).

7 Copies of this minute go to members of E(TP) Committee, John Sparrow and Sir Robert Armstrong.

PJ

P J

8 November 1982

Department of Industry

CONFIDENTIAL

Miss Stephens

Post + Tel.

10 DOWNING STREET

From the Private Secretary

Caroline please

MS

all set up. CS. 1/11

SIR ROBERT ARMSTRONG

Cable Systems: Hunt Report

The Prime Minister has agreed to the arrangements for the handling of the Government's reponse to the Hunt Report, as set out in your minute of 28 October. Her agreement is, of course, subject to the timetable you lay out being practicable insofar as the Prime Minister's diary is concerned. I have asked Miss Stephens to be in touch with your office about this.

M. C. SCHOLAR

1 November 1982

CONFIDENTIAL

Prime Minister ①

Agree these arrangements, if they are practicable in diary terms?

Yes

MCS 29/10

Ref. AO9907

PRIME MINISTER

Cable Systems: Hunt Report

It is necessary to decide how to handle the Government's response to the Report of the Inquiry into Cable Expansion and Broadcasting Policy (the Hunt Report) and the report on cable systems by the Information Technology Advisory Panel, published earlier this year. The Government will be expected to make a fairly early statement to Parliament of its views. You yourself are due to give a speech on Wednesday 8th December at the Barbican Information Technology Conference; and although there is no commitment to announcing decisions on that occasion, there is a widespread expectation that you will do so.

2. I think that the issues raised by these documents are too complex to be conveniently handled by a body as large as the Ministerial Committee on Economic Strategy (E). It seems preferable to use the Ministerial Sub-Committee on Telecommunications Policy (E(TP)). This has broadly the right membership (yourself, the Home Secretary, the Secretary of State for Industry, the Lord President of the Council, the Chief Secretary, Treasury, the Secretary of State for Trade, and the Minister of State for Industry (Mr Baker)), though it will also be necessary to invite, for some items, the Secretary of State for the Environment, because the question of local authority responsibilities will arise, and perhaps the Lord Privy Seal, because of her interest in the form of any regulatory machinery. ?

3. On the timetable, I would envisage broadly the following.

(a) I shall be holding a meeting on 3rd November to discuss security aspects, and hope thereafter to be able to report to you and the other Ministers concerned by Friday 5th

November. This would prepare the ground for a meeting of Ministers under your chairmanship on the security issues, currently planned for 8th November. The outcome of this will have important implications for the relationship of cable systems and telecommunications.

(b) The report of the Official Group on Cable Systems (MISC 73) should be available by about 12th November.

(c) This would allow a first meeting of E(TP) on the Hunt Report and the other cable issues in the second half of the week beginning 15th November. I suggest that this meeting should start with a presentation of the issues by the Chairman of the Official Committee, with appropriate visual aids, followed by a 'second reading' debate.

(d) E(TP) could then take detailed decisions at a further meeting (or possibly two meetings) later in the same week, or early in the week beginning 22nd November.

This programme will allow sufficient time for a draft of your speech, and of an appropriate statement to Parliament, to be prepared once E(TP) has taken the decisions of policy.

4. This is not to suggest that it will be either necessary or possible to decide all the issues by the end of November. A good deal of further work will need to be done by Departments, probably leading up to a full statement of Government policy in the Spring of 1983. But it should be possible for E(TP) to decide enough to give a broad indication of the Government's thinking by early December.

5. I should be glad to know whether these suggestions are acceptable to you. We can then put the necessary arrangements in hand.

RCA

ROBERT ARMSTRONG

28th October 1982

REPORT

OF THE

INQUIRY INTO CABLE EXPANSION

AND BROADCASTING POLICY

F.R.

CONFIDENTIAL

CONTENTS

CONFIDENTIAL

Chapter 1

THE INQUIRY'S TASK

1. The Home Secretary announced on 22 March 1982 that this Inquiry was to be established with the following terms of reference:-

> "To take as its frame of reference the Government's wish to secure the benefits for the United Kingdom which cable technology can offer and its willingness to consider an expansion of cable systems which would permit cable to carry a wider range of entertainment and other services (including when available services of direct broadcasting by satellite), but in a way consistent with the wider public interest, in particular the safeguarding of public service broadcasting; to consider the questions affecting broadcasting policy which would arise from such an expansion, including in particular the supervisory framework; and to make recommendations by 30 September 1982".

2. Our timetable was accordingly tight and some representations were received that more time should have been allowed. It is right therefore to record our view that the time we were given was sufficient to allow us properly to consider the issues raised by our terms of reference. It was long enough, following the issue of our consultation document on 7 April (Appendix A), to allow no fewer

than 189 organisations and individuals to submit written evidence to us, all of which we carefully considered; and for us in many cases to take oral evidence from them as well. The Inquiry held 32 meetings. In addition, visits were made to the United States and Canada, where we had useful discussions with many people involved in one way or another with cable and broadcasting, and to two of the subscription television pilot schemes in this country. The full list of those who made written submissions or with whom discussions were held is at Appendix B and our thanks are due to all of them.

3. We also wish to record our thanks to our own Secretariat. Mr Jon Davey, the Secretary to the Inquiry, has been unfailingly helpful and resourceful. The fact that we had only six months in which to undertake the Inquiry, combined with the very large amount of evidence submitted to us, imposed a heavy burden of work on him, on our Assistant Secretary Mr Peter Storr and on Miss Juanita Rodney. They never flagged and we are very grateful to them.

Chapter 2

THE BROAD PERSPECTIVE

4. The decisions which must be taken in relation to cable expansion are of great significance. There are no modern cable systems in this country. We have some ageing narrowband systems, which do no more than relay public service broadcasts except in the case of a handful of pilot schemes of subscription television which add a single channel consisting almost entirely of films. The new wideband cable systems can provide not only a very large number of channels but also channels with two-way communication capability ("interactive") allowing information to pass in both directions. For example, cable operators can put questions to viewers through the television set and get their response; viewers can have fire or burglar alarms which can alert the emergency services; and, more fundamentally, interactive channels can provide rapid communications between businesses and between them and their customers. At its best therefore cable can help both business and the individual by providing new methods of working, buying and selling direct from the home; increased facilities for education and training in the home; services like electronic mail and tele-banking; and a greatly increased and enriched choice of home entertainment. At its worst, however, it could lead to a waste of resources, risks to privacy and a lowering of the quality of broadcasting. It is therefore crucially important that the right decisions are taken.

5. This Inquiry was not concerned with the technology to be used for cabling the country, for example, whether coaxial or fibre optic cable should be used. Nor were we concerned with the provision of the interactive services for business and the consumer. These matters are under separate study by Government departments. There is however one general point which needs emphasising. It seems to be generally agreed that investment in cable television for entertainment purposes will be the necessary base to which the interactive services of economic benefit to business and the individual will be added. It is therefore very important that decisions about cable television should be taken with this fact in mind and that for example the award of franchises should positively encourage the development of the interactive services.

6. While television will be only part of a cable system it will be a very important part. How should it be regarded? And why, to quote our terms of reference, is it necessary to consider "the safeguarding of public service broadcasting"? What indeed distinguishes the latter?

7. The ability to receive BBC and Independent Television throughout the country at no charge after the payment of the licence fee has clearly been one important characteristic of public service broadcasting. Equally important however are the quality and wide range of the programming. Reith's aim was "the best of everything for everyone": and both BBC and ITV are publicly accountable not only to maintain high programme standards with a large amount of original material but also to put out a balanced selection of information, entertainment and education, with something of interest to all sections of society and to all ages. They have a formal obligation to do this and it has a significant effect on their programming schedules. Furthermore, while the BBC and ITV naturally

want to reach large audiences, they are shielded from direct commercial pressures on their programming. It would be a serious loss if programming of such quality and diversity were eroded either through a general lowering of standards ("the bad driving out the good") or if quality programmes tended to become available only to people who could pay extra for them and who lived in those parts of the country which had been cabled. If the recommendations in our report are accepted, we do not think this is likely to happen. Furthermore we believe that recent developments both in multi-channel cable technology and indeed in public service broadcasting itself justify a reassessment of the arguments against subscription television which the Pilkington (1) and Annan (2) reports found convincing. We are however satisfied that some limited safeguards against damage to public service broadcasting will be necessary in the interest of the large sections of the community who, through choice or necessity, will remain dependent on it.

8. We believe that multi-channel cable television should be seen as supplementary, and not as an alternative or rival to public service broadcasting. In Chapter 6 we make it clear that all new cable systems must carry all free BBC and Independent Television services as part of their basic programme package both so that no-one should be deprived of them by a decision to connect to a cable system and also to preserve the habit of national viewing alongside the new channels which will cater more for special interests and also be more locally orientated. Apart from carrying these basic services, cable television should be different and should greatly widen the viewer's choice by providing many additional channels for those people ready to pay more than their basic television licence fee. Because financing and other constraints will limit the geographical area of any one cable system it should be responsive to local demand. There will therefore be no such thing as a "typical" cable television package. Assuming however a

---

1. Report of the Committee on Broadcasting, Cmnd 1753.

2. Report of the Committee on the Future of Broadcasting, Cmnd 6753.

system with more than 30 channels most packages would normally comprise three distinct sections: first, the "must-carry" broadcast services referred to above; second, some interactive services of benefit to business and the consumer; and third, a larger range of channels providing such programmes as sport, films, arts, continuous news, education (including the Open University at convenient times), children's features, hobbies, health, games and locally derived programmes whether they be community affairs, ethnic, local arts or channels providing access for local people to make their own programmes.

9. Cable television is therefore all about widening the viewer's choice. It should be innovative, experimental and sensitive to local feeling. It cannot be run as though it was another branch of public service broadcasting providing a balanced service for the country as a whole. The multiplicity of cable systems all offering many channels would in any case make this sort of control impossible without a large bureaucracy which would stultify the initiative and diversity that will be both inherent and desirable in a cable system. The whole approach needs to be different, with the maximum incentive and encouragement for responsible initiative.

10. There is no reason why we should not have a high standard of privately financed cable television, just as we enjoy a high standard of public service broadcasting. Nor should we look too much to the experience of other countries where cable televison developed for quite different reasons: for example,the inadequacy of "off-air" reception and the lower standards of public service broadcasting in the United States, or the desire to bring in programmes from neighbouring countries in parts of Europe. A high standard will not however necessarily be maintained of its own accord, particularly given the understandable

wish to see an early return on the considerable investment that will be needed. In the early stages there will also be an inevitable shortage of good material made in this country; and while no doubt there are many creative writers and producers who will seek outlets for their ideas in the world of cable television it must be remembered that the making of original programmes for television is much more expensive than, for example, panel games, the showing of old films, etc.

11. We have carefully considered the thesis that a cable television system, as a result of its diversity, can be seen as just another branch of publishing, subject only to the laws on such matters as defamation, sedition and obscenity. We believe this approach might become acceptable when the whole country is cabled, if there is then genuinely the same sort of choice as is found in a bookshop, and if there is a general consensus about what has, and what has not, got a place on cable television. In the early days the capacity of some systems will still be limited: there will be a need for diversity and innovation to be matched by some consistency over access and standards: and the weight of evidence submitted to us strongly suggests that most people still see the carrying of programmes into the home as different in kind from the act of going out to buy a book or a magazine. A book is read alone, whereas much television is watched by the family as a whole. Furthermore we agree with the Williams Committee (1) that film with all its associated techniques of close-up and special effects, is a uniquely powerful instrument, and we regard video material as within the same category. We deal later with whether a more permissive attitude would be appropriate if electronic "locks" are fitted, which allow the subscriber to restrict the reception of some programmes.

---

1. Report of the Committee on Obscenity and Film Censorship, Cmnd 7772.

12. Cable television must therefore operate within certain, albeit liberal, ground rules. Some of these can be settled at the outset and we make recommendations accordingly. We are however satisfied that there will be a need for some continuing oversight. We do not think that "self-regulation" by the cable industry would be generally acceptable at a time when cable is establishing itself and when, for example, there are clearly differing views within the industry itself about the showing of programmes which could be offensive to many people. However, we emphasise the word "oversight" rather than regulation. The latter implies imposing detailed programming rules across the country whereas the whole idea of cable is that it should supplement public service broadcasting and be responsive to local demand. The concept should be one of cable operators accountable to observe a few general guidelines and provide the service offered when given their franchises rather than one of a central body regulating in detail how they go about their business.

13. There is a further reason why some degree of oversight seems inevitable. While we have confidence in the recommendations we make for the introduction of modern cable television systems we are far from confident that we can accurately foresee future developments. Cable television is in many ways a leap into the dark precisely because it should be experimental, diverse and attuned to local needs. At this stage it is impossible to know what sort of channels people will most want. General oversight, as opposed to detailed regulation, will provide the opportunity to respond flexibly as the industry develops in ways which are impossible to forecast now.

14. This chapter has set out our basic approach to cable television. The following chapters describe in greater detail the issues which will arise and contain our recommendations on the decisions to be taken at the outset and on the arrangements for subsequent oversight. We begin with the way in which cable systems are likely to be established.

Chapter 3

FUNCTIONS IN CABLE AND THE CASE FOR A FRANCHISE SYSTEM

15. We found it helpful to identify four functions which, although interrelated, can be seen as distinct and requiring different kinds of expertise. They are as follows:-

(a) The cable provider - the installer and owner of the physical infrastructure.

(b) The cable operator - the manager of a local cable system who puts together a package of cable services to sell to subscribers in his area, from whom he collects revenue. For this purpose he will draw on various sources in order to assemble the most attractive service with which to attract the greatest number of subscribers.

(c) The programme or service provider - the assembler of programmes into channels or segments of channels for sale to cable operators, consisting for example of cinema films, news, sport, education, children's programmes, etc; or the provider to the cable operator of other services (local information, home security, teleshopping, etc).

(d) The programme maker - the ultimate source of the programme material which is assembled into channels by the programme providers.

16. Our conclusion is that the key figure of these four will be the cable operator. The evidence we have received strongly suggests that the main commercial motivation lies in selling services to the public. It is therefore probably the cable operator who will take the initiative in putting together proposals for new cable systems. An alternative view that the cable provider will take the initiative seems less likely because he is more remote from the eventual sale of services. It is significant that the minority of witnesses who saw the cable provider as the key figure were not themselves proposing to install cable systems. Those who wish to participate in the cabling of the United Kingdom are primarily cable operators - and we class those companies who also intend to install their own systems as first and foremost cable operators, because their wish to install cable is secondary to their main purpose of operating systems once they are in existence.

17. Our perception of the cable operator as the key figure is in any case not dependent entirely on our view that he will normally be the initiator of cable expansion. Even if a cable provider were to take the initiative, the key figure for our purposes, which chiefly concern the supervisory framework for entertainment and other services to the public, would still be the cable operator, since it will be he who will be answerable to the viewer for the service he provides. This fact is central to our approach to a number of the questions we have to consider.

18. In our view, therefore, cable systems will be installed because cable operators take steps to get them installed; but what are those steps to be? The Cable Television Association advocated continuation of the procedure presently applied to the existing narrowband cable systems which provide a very limited range of services largely of a relay nature. Under this a cable operator obtains from the Home Office a licence under the Wireless Telegraphy Act 1949 (which permits him to receive wireless signals for the purpose of distributing them by cable) and another under the Post Office Act 1969 (which permits him to operate a programme distribution service) and then negotiates wayleaves (which permit him to lay cables in the street etc) with the relevant local authorities. We felt unable to recommend this procedure for multi-channel cable systems. We are clear that there are strong grounds for a formal system in which a franchise is granted for the operation of a cable system in a particular area. The principal reasons for taking this view are:

(i) The cable operator will have an effective local monopoly as a result of the high cost of installing and operating a cable system and of the need to achieve high customer penetration for financial viability. It is desirable that this monopoly should be conferred explicitly in a way which secures for the customer the best possible service rather than that it should happen de facto by licensing on a first come first served basis.

(ii) Franchising would provide the best way of facilitating the submission of competitive applications and the fairest mechanism for selecting the most desirable operator having regard to the channel capacity of the proposed system, the quality and variety of programming and the provision of other services, the degree of local access and the geographical area to be cabled.

(iii) Having negotiated the provision of the best system with the cable operator, a franchising authority would be the most appropriate body to oversee his performance in relation to the proposals put forward when the franchise was granted.

(iv) Without a formal franchising system, there is a risk that the grant of wayleaves by local authorities would be turned into an informal system of franchising with the criteria and conditions varying from authority to authority, some of which might seek to take powers which are unnecessary or inappropriate.

The form and nature of a franchise system, together with related aspects of cable oversight, is discussed in Chapter 7.

19. We do not believe it is necessary for the programme provider or the programme maker to be licensed; and given the large number of local channels likely to exist it would be very difficult to do this anyway. Moreover, licensing of programme providers would seem inappropriate if cable operators are allowed to relay services from overseas - and given the almost inevitable inclusion of foreign programmes in the services assembled by British programme providers it

would be even more inappropriate to license programme makers. It will be the cable operator who determines what services are carried on his system and except for those channels for which a United Kingdom broadcasting authority takes responsibility it seems simplest to hold the cable operator responsible for the programmes and services he distributes. Programme providers will then only succeed if they produce material which the operator is able to use.

20. The question remains whether the cable provider should be licensed, for example in order to ensure that he complies with any necessary technical standards which might emerge from the studies on these matters now being undertaken by Government departments. This is not primarily a matter for us. Separate licensing could perhaps be avoided if the onus were placed on a cable operator granted a franchise to ensure that any system he operated met certain specifications.

21. In the evidence submitted to us and in our own deliberations a good deal of attention was directed towards whether, to avoid undue monopoly, there should be any enforced separation of ownership between the four roles we have identified or whether two or more could be undertaken by the same organisation. We now consider this point in the light of the key role which we see for the cable operator.

22. First, the relationship between the operator and the cable provider. If the cable system throughout the country were to be laid by a single body (whether British Telecom or a new authority) acting as a national common carrier which would then rent its lines to cable operators, there would of course be no need to consider separation between the provider and the operator since it would already exist. Although not within our terms of reference, the national common carrier model appears unlikely as it is inconsistent with the Government's policy on competition and its expressed view that cabling should not make significant demands on public expenditure. If on the other hand the cable infrastructure is

to be financed privately (with the cabling of different systems being done by more than one body not excluding British Telecom) there will be a need for close co-operation between those raising the money for it and those who are to market the subsequent services, and in some cases we would expect the same company to wish to undertake both functions. Subject to one proviso, we see no reason to insist that these functions must be carried out by separate companies. This proviso is that in cases where the cable operator was also the cable provider a condition of the franchise given to him as operator would be that, to ensure continuity of service to his customers, he should sell or lease his infrastructure on a predetermined basis to another operator if he was deprived of his franchise.

23. We now turn to the relationship between the cable operator and the programme provider. Again we see no reason why the operator should not also provide programmes if he wishes to do so especially as these would clearly be only a small part of his programme package. It has been suggested that ownership links between cable operators and programme providers in the United States have in some cases restricted the choice for subscribers because cable operators who are associated with particular programme providers are less likely to carry programmes offered by others. We do not think there will be real risks from such vertical integration in this country in the foreseeable future. Indeed the problem is more likely to be one of a shortage of good material rather than good material not finding an outlet. However, in awarding a franchise attention should be paid to the programme package proposed to ensure that diversity of programme sources is encouraged and any undesirable monopoly avoided, and there should be an expectation that some channels should be available for leased use by persons having no connection with the cable operator.

OWNERSHIP OF CABLE OPERATORS

24. A cable operator will be concerned with providing information and education, as well as entertainment, to his customers and he will also have an effective monopoly in his area. We are therefore satisfied that it is right that there should be some restrictions on ownership of companies which operate cable systems.

25. We believe that the ownership of cable operating companies providing monopoly services into the home should be free from any kind of political or ideological bias. We would exclude both central and local government, and also any political party or organisation, from direct participation in the ownership of companies operating cable systems. We think the same rule should apply to religious bodies.

26. The next question is whether there should be restrictions on foreign ownership, or ownership by the press or radio or television companies. In these cases we distinguish between a majority and a minority interest. We see no need to prohibit companies in these categories from participation in the ownership of cable operating companies. There is a great deal of experience of operating modern cable systems in other countries which is not available here. So far as the press is concerned, we see a significant role for cable systems in facilitating communication in local communities and we welcomed the evidence given to us that the press would like to contribute to these new developments. The experience of

the television and local radio programme companies would also be valuable. But while these are all useful sources of expertise which could have a stake in a cable operation, we do not think any individual company of this kind should have a controlling interest. It would seem unacceptable for cable systems to be under foreign control, and control by another media interest could lead to undesirable monopoly power.

27. Apart from this, we see no need to suggest any other restrictions on the ownership of companies operating cable systems. It is likely that the resources needed to install and run future cable systems will bring together a variety of interests in consortia which will apply for local cable franchises. It is desirable that, because cable systems will be essentially local, there should usually be some local participation in the equity. However, we see no need to rule out the possibility of a single company, such as one which already owns and operates cable systems in this country, being allowed to proceed alone if it has the resources to do so.

28. We have already proposed that there should be some kind of franchising procedure, and it seems to us that it is within these arrangements that any other considerations relating to possible monopoly interests in cable operating companies can be taken into account. In the light of local circumstances, the franchising authority could decide if a particular level of cable ownership or involvement seemed undesirable.

29. We see little danger of a monopoly arising from excessive ownership of cable franchises throughout the country, as distinct from the ownership of individual systems. Although much of the evidence we received stressed that it would be undesirable for one company to own a substantial number of the cable operations in this country, it was widely thought that this was unlikely to happen. The cost of cabling the country will be such that no one company is likely to be able to undertake more than a relatively small share of the task. We do not recommend specific restrictions on the scale of operation of particular companies, but the franchising process could again monitor the possible danger of national monopoly. We deal in Chapter 7 with the kind of franchising arrangements required, but any question of maintaining oversight of the pattern of ownership throughout the country points to the idea of franchising being undertaken on a national rather than a local basis.

30. We see no reason to impose any restrictions whatever on the ownership of programme makers, cable providers or programme providers, apart from that in the last sentence of paragraph 76.

Chapter 5

CABLE'S SOURCES OF INCOME

Rental

31. The ageing narrowband cable systems in the United Kingdom at present charge those who use them a small monthly rental - usually not much more than one pound or so. This is now often insufficient to pay the cable system's overheads but all the customer is getting is the relay of off-air broadcast services, for which the cable operator pays nothing. A small incentive to subscribe to cable at present is that the cable operator, by using a superior aerial to that which most householders would consider installing, is often able to relay one or two out-of-area ITV services in addition to the local service, and this will at times give the subscriber a wider choice of viewing.

32. The basic rental charge for a cable system of the future containing 30 or more channels is bound to be more than a cable subscriber pays at present, since the operator will incur much greater costs, some of which will have to be recovered in this way. The customer will however get more for it. In addition to the existing public broadcasting services there may well be a wider range of out-of-area ITV services and foreign broadcasting services which cannot readily be received by an individual aerial; there will be services of direct broadcasting by satellite (DBS) which could well be cheaper to obtain by connecting to a cable system than by installing an individual receiving dish (though one BBC channel will be by subscription); there could be local information services and

community programmes produced at modest cost; and there will probably be some interactive channels which will provide information services or facilities for home shopping, etc. However, if the basic charge is kept at a level likely to encourage the rapid expansion of cable, the cable operator's revenue is unlikely to cover very much more in the way of additional programme material unless the latter is financed by subscription or by advertising.

Subscription

33. Many people would be prepared to pay an additional charge to receive extra programme services of their choice. The present pilot schemes of subscription television involve cable subscribers paying an extra subscription for a channel which provides a programme of recent feature films; the indications are that the idea of paying to see in the home newer films than are being shown on BBC or ITV is attractive. Subscription for particular additional channels is a natural and, by the evidence we received, a generally acceptable way of financing additional programme services on cable. It is a new source of revenue and would not divert revenue from the BBC, which (until it starts its DBS subscription service) draws its income from television licence fees, or from ITV which is financed solely by advertising. We are however satisfied that the number of additional channels for which most people are prepared to pay extra is limited.

34. Admittedly, subscription rather than advertising has been the main source of financing for cable in the United States hitherto, though this is changing. But we think this is a respect in which American experience may be a misleading guide to developments in the United Kingdom. One of the reasons for the success of subscription television in the United States is the attraction of getting away from the intrusiveness of broadcast television advertising. There is twice as much advertising per hour on the broadcast networks in America as in the United Kingdom and the commercial breaks are more frequent. In this country, the lower level of ITV advertising is much more acceptable to the viewer who already has a choice of watching television with or without advertising. For most people the presence of advertising does not affect the decision whether or not to watch a particular programme. Thus the motivation to pay for subscription television may be weaker here than in the United States, and as a consequence subscriptions may be a less buoyant source of finance and insufficient on their own to finance cable expansion. Equally so, there may not be the same antipathy to advertising in cable services provided it does not become too intrusive. It is also relevant that the programmes for which Americans are paying through subscription cable services are largely cinema films. Much of the wider range of American cable services is contained in the many channels which are provided nationally and offered as part of the basic cable package supported by advertising rather than by special subscription. These include the Alpha arts channel, the 24 hour news channels (like Cable News Network), and the sports channel (ESPN).

35. Accordingly we recommend that subscription for particular additional channels should be allowed: but we think it unlikely that significant cable expansion in the United Kingdom will be able to take place solely on the basis of rental and subscription.

Advertising

36. Advertising on cable raises issues at the heart of our terms of reference, since we were asked to concern ourselves with the safeguarding of public service broadcasting. The independent half of public service broadcasting is entirely dependent on advertising revenue and might be damaged if part of its income was drained away through the establishment of services which were in direct competition for the same source of revenue. It is also arguable that a deterioration in ITV programmes would have a knock-on effect on the BBC.

37. The questions we have considered are whether and to what extent the total amount of advertising is likely to increase if new opportunities to advertise on cable are offered; what kind of advertising is likely to be attracted to cable; whether and to what extent advertising will be taken away from existing media; which forms of media are most likely to suffer if this happens; and what the effects are likely to be.

38. Total advertising expenditure in this country in 1980 represented 1.32 per cent of gross national product. This is higher than in most countries in Europe but lower than in the United States, where the equivalent proportion is 1.6 per cent. It is also lower than has occurred in the past in the United Kingdom - in 1960 it was 1.43 per cent - but it has been growing steadily over the last six years. If advertising's proportion of GNP returned to its previous highest level in this country it would represent additional advertising expenditure at 1980 prices of about £200 million. If advertising expenditure in the United

Kingdom were to rise in relation to GNP to the level in the United States the increase in expenditure at 1980 prices would be more like £500 million. Moreover, advertising expenditure would be expected to increase with the growth in GNP, and this could result in an additional several hundred million pounds (depending on the rate of growth of GNP) being spent on advertising by 1990. Although it has been argued that the amount of money available for advertising is determined by commercial judgement irrespective of the number of media available, we find it difficult to believe that advertising revenue is fixed at its present level in real terms and that advertising on cable would necessarily mean the same size cake being sliced more thinly.

39. It is noteworthy that the fastest growth in total advertising expenditure in the United Kingdom took place in the late 1950s. This was the period during which television advertising became available for the first time and although by the end of the five years up to 1960 television had secured 22 per cent of total advertising expenditure, with the share taken by the press falling as a result from 87.7 per cent to 70.9 per cent of the market, the growth in total advertising over that period was such that expenditure on press advertising actually increased in real terms. Fears about the loss of advertising revenue to the press following the introduction of television advertising turned out to be unfounded.

40. There will already be a significant increase in the availability of television advertising time, and hence in the competition for revenue, when Channel 4 starts broadcasting in November this year. One suggestion put to us was that even assuming there is some elasticity in advertising expenditure, this will be pre-empted by Channel 4, which hopes to raise over £100 million a year through advertising revenue.

41. This was not a universal view. The Institute of Practitioners in Advertising thought that cable advertising would not erode the advertisement base of Independent Television but could by 1995 contribute £120 million a year (at 1980 prices) towards the costs of cable services. They also forecast that, after allowing for this, spending on Independent Television advertising could rise from £692 million in 1980 to £800 million in 1995, and that total annual advertising expenditure would increase over the same period from £2562 million to £2900 million. They emphasised that fears which had been expressed in the past about the effect of new media advertising on the viability of established media had in all cases proved to be exaggerated.

42. The effect on existing media will partly depend on the type of advertising which is attracted to cable. The Cable Television Association suggested to us that the local nature of cable systems would make them unsuitable for the kind of advertising which is carried by Independent Television. This was a premise that we do not wholly accept. We think it unlikely that cable systems could become sufficiently attractive to the public solely on the basis of local programming. It is likely that, as in the United States, national services will develop, fed to local cable systems by means of trunk cable networks or microwave links or satellites, and these could be financed by a combination of national and local advertising. Some cable advertising may therefore be of a national character. Even on countrywide services, however, some advertising could be placed locally by national advertisers who wished to support the test-marketing of new products in certain areas, for which purpose the present ITV regions are sometimes too large. It might also be that some national services would be specialist in nature and therefore attractive to advertisers interested in reaching a target audience and for whom television advertising would normally be too expensive. The trend in advertising is very much towards identifying the right audience instead of simply looking for the largest audience and it was suggested to us that specialised channels would be fertile ground for more specialised advertising. Advertising of this nature would be unlikely to detract from the revenue of Independent Television and could well represent entirely new spending.

43. We agree, however, that one of the strengths of cable will be its local nature and its ability to attract local advertising. For the first time, television will become a medium which will be available to local shops and services, and advertising by them will increase the overall amount of television advertising and represent new spending. Some of it, however, could be drawn away from the local press and this could happen particularly if cable were able to offer a service of classified advertisements, of jobs or of property for example, as happens in the United States. Cable channels would be particularly well-suited to offer new forms of classified advertising. The viewer could select at his set only the advertisements he wished to view from a very much larger number which were available. The reaction of the Newspaper Society, representing the provincial and local press, towards these possibilities was a positive one. They did not oppose advertising on cable, provided they were allowed to participate in cable systems. As we said in paragraph 26, we see no reason why the press should not have a stake in cable operation provided it did not amount to control.

44. To some extent the possibility of advertising on cable television could also threaten the income of Independent Local Radio. This was a matter about which the radio contractors expressed concern to us; in particular, it was the local element in cable advertising which they thought might detract from that part of ILR revenue (about half) which came from local advertising, and they proposed that cable services should be financed solely by subscription. It is difficult to assess the validity of these fears but we noted that the forecast of the Institute of Practitioners in Advertising was that ILR advertising revenue would grow in real terms notwithstanding the competition from cable, and we do not think that the risk is sufficient ground for banning advertising on cable.

45. Finally, in considering the effects on other media, we must record that fears were expressed to us by the cinema exhibitors, whose comparatively small advertising revenue is nevertheless frequently crucial to their viability. The kind of advertising shown in local cinemas could well be what cable systems would expect to carry in the future and we recognise the fear of the cinemas that some of this might be lost to them. However, their main concern was not with advertising but with the showing of films on cable, which we discuss in paragraphs 78-81.

46. Our terms of reference required us to take the effect of cable on broadcasting (rather than on the press or cinemas) as our main concern. Misgivings were expressed to us that if ITV or ILR suffered a large loss of revenue, they would be less able to meet their present obligations and would feel the need to compete for audiences through programming of a more popular character to the detriment of the public service concept. We should make it clear however that these misgivings did not lead the Independent Television Companies Association or their individual members to suggest to us that advertising on cable should be prohibited, and they were by and large content to face a certain amount of competition from this source (especially as they are expecting some compensation in the form of additional markets in which to be able to sell programmes).

47. All forecasts of additional advertising revenue and the proportion which will be taken by cable are hedged around with uncertainties: and these uncertainties are greater at a time of recession. We have however not been convinced that the likely level of advertising on cable would damage ITV or ILR to any significant extent in the short or the medium term; and both the advertiser and the consumer should benefit from the increased competition and the flexibility that cable can offer as an advertising medium. Furthermore, as we have already said (paragraph 35) we consider it very unlikely that the full potentiality of cable expansion could successfully be achieved without advertising revenue. We also believe that advertising on cable will have some positive benefits. Accordingly we recommend that it should be allowed.

48. Having reached that view, we considered the case for any restrictions on cable advertising, whether from the point of view of amount or as to nature. The amount of advertising on broadcast television is restricted, to an average of six minutes an hour and a maximum of seven minutes in any one hour, but it does not follow that advertising on cable should be subject to the same restrictions. The limitation on broadcast television is primarily to protect the viewer from excessive advertising, as part of the concept of broadcasting as a public service. Cable, however, would not be a public service in that sense and it would have to provide a service that was sufficiently attractive for the public to buy. Advertising that was so intrusive that it put the public off would be counter-productive. On the other hand, cable could play a useful role in providing a service of specialised advertising. The emergence of longer and perhaps more informative advertising could assist consumers to make product choices; and we have already referred to the possibility of a channel or channels devoted to classified advertising. Recruitment advertising in particular, it was suggested to us, could be very successful on cable. Another example would be a channel devoted to home shopping where, in effect, a television channel would become the equivalent of a mail-order catalogue. We see no reason why cable should not be allowed to devote the whole or any part of a channel to advertising in this way. If the intention is that some channels might consist of nothing but advertising, it becomes rather more difficult to restrict the amount of advertising which might be allowed on other channels. On balance, we believe that there are insufficient reasons for seeking to lay down defined limits at the outset. However, we have earlier in our report stressed the need to adopt a flexible approach to the future of cable and this is an area where, after some years of experience, it could become necessary to impose restrictions.

49. As to the nature of advertising, there is a clear need for observance of a code of practice, and we do not think that advertising on cable should adopt different standards from those which now apply to ITV in relation to products whose advertising is prohibited or the methods by which goods or services are advertised. We do, however, consider that there is scope for sponsorship of programmes on cable provided that certain clearly defined rules, including the separation of advertisements from editorial matter, are observed. We think that the likely range of advertising on cable, including local and classified advertisements on a multitude of local cable systems, will preclude the external pre-vetting of advertisements and we consider that a mechanism for dealing retrospectively with complaints of breaches of the code of practice will be sufficient. We deal with this in Chapter 7.

Pay-per-view

50. There is one other possible method of financing cable services to be considered. This is the question of premium payment for particular programmes (as distinct from channels) or, as it is usually called in North America, "pay-per-view". The technology of future cable systems, with the capability of all connected sets being individually addressable, will make it easy to direct the desired programme only to those who have paid for it or ordered it. But charging comparatively large amounts for individual programmes would have considerable social implications, particularly at a time when the majority of the country would not be cabled. For example, the BBC represented very strongly that one of their main concerns about cable competition lay in the possible siphoning of sporting events from free television to those who could afford to pay a premium for them and who happened to be in the area of a cable system. They were concerned generally that popular events might be bought up for subscription television, to the detriment of viewers who did not live in a cabled area or were either unwilling or unable to pay extra to watch what they had been accustomed to get as part of an ordinary broadcast service: but they

identified as the critical part of this threat any introduction of pay-per-view on cable or DBS. The special danger of pay-per-view is that if there was a particularly popular event which enough people were prepared to pay a sizeable fee to watch - let us suppose that a total of one million people in a number of cable systems were prepared to pay £5 each - the revenue thus generated would be sufficient to guarantee that no ordinary broadcasting service, with an obligation to spend its available funds on continuous programming, could hope to compete for the television rights. In this way the ordinary viewer would be deprived of a major popular event in favour of a minority of the television audience. We found that this particular problem was already exercising many people we visited in the United States and in Canada and we have concluded that it would be safer for the time being to preclude pay-per-view programmes being offered on cable systems here.

51. Excluding pay-per-view will not necessarily prevent the siphoning of some events from broadcast television to subscription services, but it does at least avoid the problem in its most acute form. We do not think that pay-per-view is something on which cable expansion would rely heavily, and its exclusion will provide a measure of reassurance for public service broadcasting. The more general issue of cable programming and its potential effect on broadcasting, including the question of siphoning, is dealt with in the next chapter.

Chapter 6

CABLE PROGRAMME SERVICES

Number of channels

52. The role of cable systems in the United Kingdom so far has been clearly defined and very limited. They have been the means by which the three British broadcast television channels have been received by a small part of the population (currently just over 13% of those holding television licences). Many television relay systems were built on the foundations of even earlier radio relay systems, some of which were established in the 1920s, and their common purpose was to bring television to people who could not at the time receive a satisfactory signal off-air or who, for local environmental reasons, were not allowed individual external aerials.

53. That limited role has not been through lack of aspiration to do more. Cable operators have had to work within a strict regulatory framework and with a licence from the Home Office which requires that they must carry all locally available public broadcasting services and may not - subject to very limited exceptions mentioned in the next paragraph - do anything else. Previous inquiries into broadcasting (like the Pilkington report in 1960 and the Annan report in 1977) have recommended that Governments should not allow cable operators to offer their own services to paying subscribers. Cable operators have therefore been forced to stick to their relay role and have consequently had no reason to install cable systems with capacity for many channels. Half the commercial cable systems in the United Kingdom can carry no more than 4 television channels, with 2 or 4 radio channels. Moreover, as constant improvements have been made in the broadcasting organisations' transmitter networks, cable's television relay role has become increasingly redundant.

54. The limited extensions of the local relay role have been of four kinds. First, the cable operator has normally been allowed, if he can receive off-air the signals from a neighbouring ITV region, to relay that channel as well as the local ITV service. Subscribers to some cable systems can therefore receive two or even three ITV channels as well as two BBC channels, and although ITV programmes may much of the time be identical, this does at other times increase the viewer's choice of programmes. Second, a limited pay-television experiment in London and Sheffield, based on a coin-in-a-slot meter, was authorised in the 1960s and ran between January 1966 and November 1968. Third, some community programming was authorised for cable television in 1972 and for cable radio in 1976. Only six community television stations and seven community radio stations have taken advantage of this authorisation and success has been difficult to achieve. One television station, at Greenwich, distributing three hours of community programmes a week, and five radio stations, at Basildon, Greenwich, Milton Keynes, Telford and Thamesmead, are all that remain operating. Fourth, thirteen pilot schemes of subscription television, the first starting in September 1981, enable a single channel to be used to provide an additional programme service, consisting almost entirely of cinema films.

55. So much for the past. We now have to consider the situation if cable operators are allowed to use modern technology to provide a large number of channels and programmes. The first point to make about the services on future cable systems is that we see no reason to restrict in any way the number of programme channels that can be supplied, subject only to the adequate provision of interactive channels of communication (see paragraph 5). Indeed, the object should be to provide the maximum variety and choice for the viewer. The questions we have considered relate more to the kind of programme services that cable will carry.

56. At this point we should perhaps say that we see no incompatibility between the expansion of cable services and the developing use of satellites for the distribution of television programme services. These developments are complementary to each other, particularly in the sense that cable systems could increase the number of viewers to whom DBS services are available and could enable them to be received more cheaply. Furthermore, under the 1977 Geneva Plan of the World Administrative Radio Conference, the United Kingdom has been allocated frequencies for only five national television channels by means of DBS and it could therefore give the viewer only a small part of the choice which wideband cable could offer. Moreover, DBS could not offer the interactive capabilities of modern cable systems.

57. A second kind of satellite, providing low-power telecommunications links rather than transmissions which can be received by the general public, is now widely used in the United States for feeding programme services to cable systems across the country. These telecommunications satellites are therefore an alternative not to local cable systems but to the trunk or microwave network which might otherwise provide the means of feeding the same programme services - particularly live programmes which could not be distributed in the form of videotapes - to a number of cable systems. The need to use satellites for this purpose is less in a country the size of the United Kingdom; moreover, we understand that there could well be problems within the United Kingdom in finding the necessary frequencies for an extensive satellite distribution network which would not interfere with existing and planned terrestrial services.

The "must-carry" rule for public service broadcasting

58. It is appropriate to start with the continuation of the relay role described above, which is usually referred to as the "must-carry" rule. All the evidence put to us assumed that a basic feature of a multi-channel cable system would be the carrying of public broadcasting services. There was no argument about whether or not this should be done, because cable operators, present and potential, considered that it would be in their interests to provide their subscribers with BBC and ITV programmes as part of their basic package covered by the fixed rental fee. The only question is whether there should be a formal obligation on them to do what they are likely to want to do anyway. We noted that this formal obligation exists in both Canada and the United States, despite the considerable freedom given to cable operators in other respects in the latter country. We think there are strong arguments for making it clear to the person who rents cable that in all circumstances he will continue to be able to receive the public broadcast services he has received in the past. We do not for example think that it should be open to an operator to remove a public service broadcast channel provided as part of his basic package - say BBC 2 or Channel 4 - in order to substitute a subscription service. Such action would be contrary to our basic philosophy that cable services are supplementary and not an alternative to to public service broadasting. We therefore recommend that cable operators should be required to carry all free broadcast television services serving their particular locality, whether present or future. Thus in addition to BBC1, BBC2, ITV and Channel 4 or the Welsh Fourth Channel, there should be a requirement to carry DBS services available to all viewers, but not those requiring payment of a subscription.

59. There is a temporary problem about the application of the must-carry rule to those existing systems which can carry only a few channels and which are no longer profitable on a relay basis only. Unless the operators of those systems can provide new revenue-generating services they may be forced to close down. On the other hand, if the operators can use channels for commercial purposes they can probably survive until modern cable systems can be installed. The Cable Television Association emphasised that it would not be in their members' commercial interests to seek to deprive their customers of BBC and ITV programmes. In many cases it would be possible to provide subscribers with the means of receiving broadcast signals off-air with television sets adapted for both off-air and cable reception, prior to utilising cable channels for other purposes. In the case of these out-of-date relay systems, we think it would be reasonable to give a temporary waiver of the must-carry rule provided the cable operator was willing and able first to provide the viewer at no extra cost to him with the means of receiving the public service channels satisfactorily off-air. The operator would require the consent of the franchising authority to the provision of new progamme or other services on an existing system, and those services would then be brought within the oversight which we propose for new cable services. However, we think it important that this conditional waiver of the must-carry rule should not be used to perpetuate out-of-date cable systems and thus not achieve the other benefits of recabling with wideband systems. Accordingly, we recommend that this waiver should be for a period of no longer than five years. Nor could the existing relay company necessarily assume the automatic right to a franchise to install a modern multi-channel system in the area. It would obviously be very well-placed to get this but if there were other applicants they would have to be considered on a competitive basis.

60. We considered separately the application of the must-carry rule to radio services. Such a rule now exists, its form varying according to the capacity of the system. For example, in those systems which can carry only two radio channels in addition to television, the two services relayed must be chosen from the BBC's national radio services; if three can be carried, the operator may choose either another of the BBC's national services or a BBC or IBA local radio station serving that area; and if channel capacity is no problem, it is only after distributing all the BBC's national services and both local radio services, if there are two serving that area, that a cable operator can choose to relay any other authorised broadcasting station, such as Radio Luxembourg. It was suggested to us that radio relay by cable is nowadays of little practical significance because so much radio listening is from car radios and portable transistor sets. Nevertheless, we were told that both the Independent Local Radio contractors and the BBC attach importance to the carriage of radio by cable; and, if we are moving towards a society in which many more activities in the home will use cable connections, it may well be that radio by cable will have a greater role than hitherto. We were not entirely persuaded by this argument but since the bandwidth for many radio channels is less than for one television channel and since on our visit to the Manhattan cable system it was noted that it carried under a must-carry rule 24 FM radio channels in addition to its 28 television channels, we suggest that the must-carry rule should continue to apply to new cable systems for radio.

Carrying of other UK broadcasting services

61. We turn from the broadcasting services which cable must carry to those which it may perhaps carry. We have already explained that some cable systems now carry out-of-area ITV services. This could develop considerably with interlinked multi-channel systems. However, the multiple relay of ITV services on a wide scale would raise sensitive issues for the ITV system, because the IBA

awards contracts on the basis that the programme companies have the virtual monopoly (particularly of advertising) in their own area. This system could be distorted if, with the expansion of cable systems, a significant part of the population were able to choose whether to watch the local ITV service or that from another area. Nevertheless, we would support making it possible for the Welshman living in London to watch the Welsh Fourth Channel or the expatriate Scot to watch local services from Scottish Television, as part of the increased choice which cable will offer. We found a measure of support for this idea among some ITV companies but we recognise that there could also be some problems. Moreover, given the fact that cable television is all about widening the viewer's choice we think it would be an anomalous arrangement if cable were able to offer its own programme services alongside the local ITV service but were not allowed to carry other UK broadcasting services. We think therefore that the relay of out-of-area ITV programmes is a matter which should be left for the cable operator to negotiate if he wishes to do so in the light of local circumstances and demand.

Carrying of foreign broadcasting services

62. There are also arguments for freedom to distribute foreign broadcasting services. Radio Telefis Eireann suggested to us that cable systems in the United Kingdom should be permitted to carry RTE's radio and television programming to increase the choice available for viewers and listeners, particularly those of Irish descent; and we noted that the proposals put forward by Merseyside Cablevision envisaged that RTE programmes would be included if they were allowed to install and operate a cable system in Merseyside. We see no objection to cable operators choosing to carry foreign services. It could be a help to international understanding and an aid to language education if some other European services were distributed here by cable, particularly when the development of DBS will make them more readily receivable in this country. We doubt however whether many cable operators will think the demand is likely to justify this, and again we think it should be left to them to decide.

63. In one significant respect, foreign broadcasting services are different from out-of-area ITV services. Since they originate outside this country, they are not susceptible to any British control. A case in point is advertising, discussed in the previous chapter which concluded that advertising on cable should be subject to the same code of practice as is applied to Independent Television. We are aware that work is in progress towards European agreement on the standards to be applied to satellite broadcasting, as regards both advertising and programme material, and this may result in a measure of harmonisation. Nevertheless, and in the meantime particularly, it seems to us right that if a cable operator wishes to distribute a foreign broadcasting service he should not only ensure that he has the copyright owner's clearance but accept responsibility for its content.

Range and balance of programmes

64. The main potential threat to public service broadcasting from cable expansion is seen by the BBC and Independent Television to lie in what they regard as the commercial approach cable services are likely to take towards securing large audiences by popular programming, particularly by obtaining exclusive rights to programmes - popular sporting events especially - which will encourage people to pay for subscription services. The argument is that broadcasting will be both weakened by losing a large part of its audience and also impoverished by being deprived of certain programmes or by being forced to compete more on a popular level to the detriment of serious or quality programming. We do not ourselves rate this threat very highly but we must consider whether there should be any further safeguards, additional to the must-carry rule and the exclusion of pay-per-view, to minimise it.

65. One view put to us was that the value of cable expansion would lie in "narrowcasting", by which we mean its ability to provide television on a truly local scale and in such abundance that all kinds of specialist interests could find themselves catered for in a way that is not possible on broadcast television. It was sometimes implied that cable should confine itself - or be confined - to this role and not get involved in competing for mass audiences. Our assessment is that if left to develop freely, cable will not confine itself solely to a narrowcasting role. For example, there seems to be a clear and large market for the viewing of cinema films in the home. We find it difficult to characterise programming of this kind as of specialist interest or as falling within the description of "narrowcasting". The best of it will plainly appeal to a large audience which may be drawn away from some BBC and ITV programmes, just as we heard in the United States that a popular film on subscription television may draw a larger audience among those with access to it than any of the broadcast networks. However, only a small proportion of films will have this kind of drawing power and, assuming that the BBC and ITV continue to maintain the quality of their programmes, we do not think they need fear the loss of the bulk of their audience, even when cable eventually achieves a high penetration in this country. In any case, we doubt whether it is feasible to guard against this by preventing cable from trying to be popular. To do so would certainly inhibit the development of cable and, although we are aware that the Canadian authorities have decided that subscription television can go ahead only with restrictions on the proportion of box office successes which may be included among the cinema films shown, we came to the conclusion that it would be wrong to follow this precedent or to confine cable either to a narrowcasting role or to a heavily regulated regime. A sports or continuous news channel would similarly not come within the definition of narrowcasting. Cable operators in our view should have freedom to provide programmes which are likely best to appeal to their customers, even though some of these may be provided by national programme providers to a large number of cable operators.

66. The converse to the argument that cable's role should be limited to certain types of programme is that it should be obliged to cover all fields, in the same way that public service broadcasting has an obligation to maintain a wide range and balance in its programming. The argument here is that public service broadcasting would be at an unfair disadvantage in competing with cable if it, but not cable, were to be required to provide a balanced service with, for example, a certain proportion of serious material and of adult education, some current affairs programmes or documentaries in peak viewing time, limitations on the number of films, quiz and game shows, etc. There could be no question of requiring a wide range and balance of programmes on individual cable channels and it seems to us artificial and unnecessary to place an obligation as to diversity on the totality of a cable system's output. It will happen anyway as a result of a multiplicity of channels and of the carrying of the public broadcasting services, and we do not believe that an attempt to spell this out in detail would represent any safeguard for the future of public service broadcasting. Indeed, we think it may be more realistic to think of the variety of services which could be provided by cable as in time reducing the need for some of the existing obligations on public service broadcasting, for example the amount of local programming by the ITV companies.

67. We therefore make no recommendation on the range and balance of programmes. Diversity is an aim that we think the franchising system can encourage. In any case, what is wanted and what can be financed may vary from one place to another, but there should be a presumption that all systems should provide children's programmes, education and a community service. We have already suggested that any cable franchise should be awarded after taking account of the various mixes of services to be offered. In this way, the franchise for that locality would go to the operator able to provide the best service, and we prefer this approach to one that seeks to lay down a lot of obligations on all cable operators from the start.

Exclusive rights

68. There is one particular threat to public service broadcasting, and thus to the viewer without cable, to be considered at this point. We have already referred (paragraphs 50-51) to the possibility that cable would have the money to negotiate exclusive rights for certain important sporting and national events. We were left in no doubt about the importance attached to this threat by the broadcasting organisations and also by a large number of our other witnesses since it would affect many viewers who cannot have or do not want cable. For this reason we have already recommended that pay-per-view should not for the time being be permitted as a source of cable finance. But is this a sufficient safeguard?

69. Section 30 of the Broadcasting Act 1981 enables the Home Secretary to make regulations to prevent the making of exclusive arrangements for the broadcasting of sporting or other events of national interest. No such regulations have ever been made and the provision is regarded as a reserve power against the background of which the broadcasting organisations should agree among themselves about those events which should be protected against exclusive arrangements made by either the BBC or the ITV companies. The events which the BBC and the ITV companies have agreed should be protected in this way are the FA Cup Final, Wimbledon, Test Matches, the Derby, the Grand National, the Oxford and Cambridge Boat Race and the Commonwealth Games when held in the United Kingdom. However, it should be noted that despite the agreement in principle that exclusive arrangements for these events should be avoided, the position in practice is that most of them are covered by only one of the television networks, because the other does not think duplication is worthwhile.

70. Those who gave evidence to us from the cable industry disavowed any intention to seek exclusive arrangements for the kind of national sporting events that are already on the protected list. Nevertheless, we think it likely that cable will want to carry other major sporting events which will attract big audiences and thus encourage viewers to subscribe to cable services; and to draw a protective line around certain events could well have the effect of distorting the operation of the market and creating anomalies. However, the broadcasting organisations are likely to remain for the foreseeable future in a strong position to bid for the television rights to the majority of major events and we hope that one effect of the arrival of cable may be to extend the range of sports which the viewer will have the opportunity of watching and which will benefit from the injection of money from television rights. Admittedly, it could force up the fee for events which are already televised, but we had some sympathy with those who suggested to us that television at present secures sporting coverage on the cheap. Nevertheless, we think it right that the great national events should continue to be protected for the sake of the average viewer who has been used to seeing them on broadcast television. For this reason we take the view that the present list of protected events, modified from time to time if necessary and which may in the future need to be the subject of a formal regulation by the Home Secretary, should apply to new cable services as it applies to broadcasting. Apart from this, however, and subject to our proposed ban on pay-per-view services, we do not think it appropriate to place restrictions on the sporting or other events which cable television may wish to cover.

Local access

71. We have already stressed cable's important local role. We noted, for example, that in Canada an average of 8 per cent of cable revenue is spent on the production of community programmes. We have considered whether to recommend specific obligations on cable systems to provide facilities for local community programming and for access by local groups. This would allow local events and activities to be covered by television, enable local groups of various kinds to participate in the making of television programmes and provide a means of fostering interest in the community and encouraging expression within it. On balance we felt that this was another aspect of cable services that could be left to be taken into account in the franchising process, when the proposals of rival companies or consortia are considered. However, we believe that there should be a presumption that the cable operator should accept responsibility for ensuring and financially assisting some community participation in cable programmes and we hope that cable systems' relationship with and contribution to their local communities might become a source of mutual pride.

Taste and decency

72. We now turn to the question of programme standards and in particular whether the traditional broadcasting requirements relating to taste and decency, and the suitability of programmes for children likely to be watching, should be imposed on cable operators. We think they should. In paragraph 11 of our report we explained why we did not accept the analogy with publishing, which is subject only to the laws on such matters as defamation, sedition and obscenity. The majority of those who gave evidence to us also took the view that the place

of television in the average family home is such that restraints on pornography and violence are required additional to those imposed by the law of the land. We do not think that the mass of public opinion here would find acceptable some of the programmes receivable without restriction on cable channels in the United States. This may sound prudish but what is at issue is more a matter of the general climate of opinion than an argument about whether cable is more like publishing or broadcasting. In fairness to present and potential cable operators it should be said that many (but not all) of them agreed.

73. The question is however whether the industry should be left to operate a code of its own or whether a formal obligation should be placed on it. Frankly we doubt whether self-regulation would be acceptable on such a sensitive issue at a time when a large number of new cable operators, with different views on what is acceptable, will be establishing themselves on a local basis. Here again, it is clear that the majority of those who gave evidence to us shared this view.

74. Accordingly, and subject to the important exception dealt with in the next paragraph, we recommend that cable operators should be under the same formal obligations as the broadcasting authorities, namely to ensure so far as possible that nothing is included in their programmes which offends good taste and decency, is likely to encourage crime or lead to disorder or to be offensive to public feeling, and also to have special regard to programmes broadcast when large numbers of children and young persons are likely to be watching.

75. There is however a case for saying that there could be greater freedom for subscription channels which are optional extras to the basic package covered by the cable rental. The argument is that cable customers are not obliged to receive these channels and that those who wish to do so should be able to pay to receive material some of which might be offensive to others. In particular, relaxation of the times at which 'X' films can be shown would be of especial value to shift workers who would thus be able to watch during the day films that were otherwise available only in the late evening. The trouble about this argument is two-fold. First, subscription channels of films will carry much that would be offensive to no-one and which all potential subscribers might wish to see. Second, we are concerned about the problem of confining so-called "adult" material to adults once a decision is taken to subscribe to a channel which may carry it. However, we were impressed by the sophisticated decoder used by SelecTV in their pilot schemes of subscription television at Milton Keynes, Northampton and Tredegar. This enables each subscriber to lock out from his set films of censorship categories which are not wanted on the subscription channel for the time being, while allowing other categories to be received. Thus a parent going out for the evening can effectively prevent children watching an 'X' film or any film of either 'AA' or 'X' certificate or even, should it be desired, a film with an 'A' certificate. Any such system does of course depend on the parent bothering to activate the electronic lock and taking steps to maintain the secrecy of the personal code number, but otherwise the system is tamper-proof. We therefore take the view that on a subscription channel with sophisticated electronic locking facilities of the kind described, there would

no longer be a need to restrict the time of day for showing the sort of films currently shown late in the evening because they are unsuitable for children. Furthermore, we think it would be acceptable with this safeguard to allow the showing, without any overriding constraints of taste and decency, of any film passed by the British Board of Film Censors for public exhibition with an existing censorship category[1]. We do not think it right to go any further and, for example, allow the showing of the kind of film which has hitherto not been passed for public exhibition and has been confined to cinema clubs or other video material which does not conform to public service broadcasting requirements of taste and decency.

Impartiality

76. Another question relating to programme standards is whether it is necessary on cable to require strict impartiality on matters of controversy. We are satisfied that news, whether it be national or local, should be presented with accuracy and impartiality. Comment, however, is a matter that we think could well be allowed greater latitude on cable, but not to the extent that there is a political bias across a cable system as a whole. Impartiality in community access channels should mean only impartiality in allowing access. Those allowed access would be under no obligation to be impartial. Similarly, individual channels could carry programmes provided by special interest groups, for example political or religious organisations. However, we think it would be wrong if the amount of programming by political parties and religious groups was solely dependent on their ability to raise money and for this reason we recommend that they should not have their own cable channels.

---

1. "Existing censorship category" refers to the categories used so far by the British Board of Film Censors and any future equivalent categories, but not to the new "RESTRICTED (18)" category being introduced to cover some sexually explicit or violent films hitherto shown only in cinema clubs.

Foreign material

77. We have considered whether requirements should be imposed as to the proportion of British material which should be included on entertainment channels on cable. The broadcasting organisations are obliged to ensure that a "proper proportion" of their output is British (or from the European community generally) and they interpret this to mean that no more than 14% should come from outside Europe. The subscription television pilot schemes were required in their cinema film programmes to show the same quota of British films as applies to the cinema. However, we noted that the Government at the beginning of this year had reduced the Films Act quota from 30 per cent to 15 per cent and it has more recently announced that from 1 January 1983 the quota will be suspended altogether. The existence of the quota has not been effective in ensuring that sufficient British material has been produced to fill it, and this experience does not encourage us to propose that a quota should apply to cable programmes. Moreover, we received no evidence to suggest that a rapid expansion of the number of cable channels could in the short term rely very heavily on British material. Cable will inevitably have to buy in many programmes from elsewhere, mainly the United States, and unless it is able to do that, it will be much slower to develop. In the longer term, we have faith in the British film and television industry's ability to expand to satisfy the market provided the cable operators encourage this and do not continue to rely unduly on low cost material from abroad when there is sufficient British material available. The ITV programme companies are eager to have the opportunity to serve new outlets, as is the expanding independent production sector which has already been stimulated by the demands of Channel 4. We believe that the supervisory body might have a role in encouraging the production and use of British material on cable and possibly even have power to impose restrictions in the longer term, if that was thought appropriate, on the amount of foreign material which could be included in cable programme channels.

The cinema

78. We referred in paragraph 45 to the position of the cinema. A powerful plea was put to us by the cinema exhibitors for a measure of protection against the inroads of cable. We have already pointed out that one of the main attractions of cable lies in its provision of feature films, and it is clear that the development of the "cinema-in-the-home" concept may weaken the position of the cinemas, which have in any case been faced for many years with a steadily declining number of customers. What the cinema exhibitors would like in particular is a statutory restriction on the ability of cable operators to show new films, so that cinemas would retain the monopoly of exhibition for the first twelve months at least.

79. The normal practice at present is that cinema films are not shown on television for three years after release. This practice applies only because film producers and distributors have decided that it is in the best interests of the film industry generally that they should not make their films available to television during that time, to allow cinemas to exploit them fully. Exceptions are sometimes made. When the subscription television pilot schemes started, their wish to offer more recent films on payment was recognised but the cinema was still given some protection, through a condition of the cable operator's licence that a film should not be shown on cable within twelve months of its registration. The cinema exhibitors indicated to us that for cable they would be content with the twelve month rule where films were part of a subscription service but that otherwise they wanted the three year rule to apply, and they argued that these restraints should now be imposed by legislation rather than by agreement within the film industry.

80. We have some sympathy with the position of the exhibitors but we believe that market forces should be allowed to dictate the showing of films on cable. Just as the showing of films on television now is determined by the film industry's assessment of its own interests, so we believe it should be left to decide on what terms it will make films available to cable. It may conclude that a film can be sold more profitably and established in the public mind by being premiered in the cinema; but if it ceases to believe in the commercial value of exhibiting films in the cinema before they are shown on cable television or on television generally, we are not convinced there is a case for imposing a statutory constraint on its freedom to sell its product in whichever market it chooses.

81. It was not our job to give detailed consideration to the problems of the cinema. If, however, our general approach is accepted we think that cinema owners have a point in arguing to us that they alone should not be forced to pay the Eady levy to help finance British film production. It is not for us to recommend whether or not the levy should be abolished or widened. But we think the arguments for equal treatment over this between the cinema and television - cable or otherwise - are made stronger by our conclusion that the cinema should not be accorded any statutory preferential position in relation to the availability of new films for exhibition.

Copyright

82. We received a number of submissions suggesting that a necessary precondition of the expansion of cable television should be the reform of the present laws on copyright. The Government is already considering reform of the copyright laws in the wake of the Whitford Report[1] and it was not for us to make proposals in that field. We have no doubt that the Government will give due weight to the extra need for amendment of the copyright law which may flow from a decision to allow greater freedom to programme services delivered by cable.

---

1. Report of the Committee on Copyright and Designs Law, Cmnd 6732.

Chapter 7

OVERSIGHT

The nature of the task

83. In Chapter 2 we set out a broad perspective within which to see the future of cable television. To recapitulate briefly, it should be seen as supplementary and not as a rival or alternative, to public service broadcasting. It should widen and enrich the viewer's choice by providing a large number of channels of special interest for which people are prepared to pay. It should be encouraged to be innovative, experimental and above all responsive to local needs which will vary from place to place. It cannot be run as though it were another branch of public service broadcasting. On the other hand its development will need oversight; and there must be some safeguards to preserve the quality and range of public service broadcasting, both as an end in itself and because many viewers, by choice or necessity, will remain solely dependent upon it.

84. The kind of oversight we envisage will involve both a positive and a reactive role. The positive aspects will be centred on the franchising process and on the choice of an operator to provide cable services in a particular area. Thereafter, the oversight will be reactive, intended to ensure that certain ground rules are observed but without constant supervision of the services that are provided.

The purpose of franchising

85. For the reasons given in paragraph 18, we feel strongly that there should be a formal process for granting franchises. A cable operator will have an effective local monopoly which should be conferred only after an opportunity for judging any competing bids and for securing the provision of the best service for the area concerned.

Depending on decisions taken by the Government about the planning of the cable network, the franchising body might take the initiative in delineating areas and inviting applications for franchises; but given the local nature of cable systems we think there should also be room for cable operators to take the initiative in putting forward applications for franchises in areas of their choice. Any bids of this kind should however lead to the public advertisement of the franchise and the opportunity for other operators to put forward their own proposals to be considered in competition with the original application.

86. The decision on a franchise will involve the franchising body making a positive judgement about a number of elements in the applications before it and could also include some negotiation on them. These would include:

a) the area to be cabled. We are satisfied that there can be no precise answer as to the optimum size of a cable system, since it will depend partly on the nature of the area to be served. The ideal would be a franchise area of a size small enough to retain an identity with the locality and to enable cable to be installed expeditiously but which could at the same time support a wide range of cable services. It would be a pity if, by suggesting an arbitrary limit to the size of a franchise area, the effect was to deny to the suburbs of a city the benefit of connection to the cable system serving the city itself. However, because we attach importance to the local nature of cable systems, we take the view that even in the conurbations a franchise area should not cover more than about half-a-million homes, and should normally be smaller than that. Equally so, if cable is to spread successfully, many relatively small towns should be cabled even though they may not be able to support such a large number of channels. There are two other considerations relating to the area to be cabled. The franchising

body will need to take into account the comprehensiveness of the cabling within the area concerned, so that it is not restricted to streets where a majority of occupiers are likely to pay for cable. It could also speed up the widespread development of cable and avoid what is known as "cherry-picking" by seeking in some cases to combine less attractive localities with those carrying the best commercial prospects or even by asking large consortia which bid for a prosperous area to provide a separate cable system in a less promising area elsewhere;

b) the speed with which the cable system is to be installed and, to learn a lesson from United States experience, the sequence in which different parts of it are to be cabled, in order to avoid the situation in which the cable system is never in practice extended beyond the most profitable parts of the franchise area;

c) the ownership of, and the interests represented in, the prospective cable operating company and any problems of monopoly whether national or local;

d) the channel capacity of the system and the range and diversity of the proposed programme channels, including the proposed financing arrangements;

e) the arrangements proposed for community programmes and local access;

f) the intentions regarding the provision of interactive services.

87. We considered what the term of the franchise should be. Because much of the evidence given to us has argued for the need for a lengthy period of assured use over which the very considerable cost of installing the cable can be recouped, we in turn stress that we do not propose the licensing of the cable provider and that the

franchise we are considering is solely for the operation of the system. If the cable operator's franchise came to an end, this would not render the system itself useless and of no value: it would be available for use by another operator. Indeed, we made clear in paragraph 22 that where the operator also owned the cable he would be required in the event of his losing his franchise to sell or lease his infrastructure on a predetermined basis to another operator in order to ensure continuity of service to the cable customer. In these circumstances we consider that the cable operator should ordinarily be granted a franchise, as are ITV programme contractors, for eight years. However, in the first instance, when the cable system and its services have to be developed from scratch, it should be for ten years from the start of operation.

88. Existing cable operators should be allowed to continue operating until a full franchise is granted for the area covered by their system, whether to them or to another operator; and of course the grant of a franchise would not affect the continuation in the same area of non-commercial master antenna systems providing nothing but broadcast relay (such as those which simply use one aerial to feed BBC and ITV programmes to all the occupants of a block of flats).

Subsequent oversight

89. Once the franchising body had taken its decision on the best cable operator for a particular area, its most positive function would be completed. It should remain in the background unless important developments or specific complaints required it to take an interest. We see no need for it to control the charges to cable customers. Nor would there be arrangements for continuing regulation by way of approval of programme schedules, prevetting of advertisements or constant scrutiny of output. Cable systems should operate under minimum constraints. The approval of the franchising body would however be needed if it was subsequently proposed to modify the basis on which the franchise had been granted, for example if there was a change of

ownership of the cable operating company or if there were significant modifications of programme channels, as we recognise might happen in the light of experience and the availability of new services. We have already made clear the extent to which we think that cable programmes should conform to the traditional requirements as to taste and decency, and also that advertising should conform to the IBA code of advertising standards and practice. There is therefore a need for an authority which would keep in touch with what is going on; serve as a forum of advice to operators; and be generally known as the body to receive and adjudicate on complaints concerning the service being provided if the viewer felt the operator had given an inadequate response. We have also identified the need for an eye to be kept on the amount of United Kingdom programme material being used and on the way in which advertising on cable might develop. Above all, however, it should be responsible for judging whether cable operators were living up to their promises and for responding in a flexible way as the cable industry developed.

Local or central franchising?

90. There is therefore a crucial link between oversight and franchising, and the first question is who is to do the latter. Despite the vigorous case put forward by the Association of District Councils in particular, the bulk of the evidence given to us was against franchising being undertaken by local authorities. We agree with this view. Cable systems may cross local authority boundaries and not be readily susceptible to control by one authority alone; it might be desirable to combine for franchising purposes less attractive areas with those with the best commercial prospects; and our examination of local authority franchising in the United States does not lead us to think it is a good model for this country. In particular, we noted the growing feeling in the United States that local authorities have been using their powers (which are based on no more than the same need to obtain wayleaves to dig up public highways as exists in this country) to excess, slowing down the

franchise process and demanding too much from cable operators. Furthermore, local franchising would not be at all an appropriate way by which to facilitate the speedy development of cable systems throughout the country in a way which allows some overall oversight of what is happening.

91. We therefore recommend that franchising should be undertaken centrally. Central franchising has the advantage that it greatly facilitates the link we wish to see between franchising and oversight, because our view is that the latter can only be undertaken nationally and not in isolation in each individual area. Indeed, if the local authorities were to be responsible for franchising we think there would also have to be some national oversight body, thus involving some quite unnecessary duplication of functions. Central franchising therefore enables promise and performance to be judged by the same body. It also greatly simplifies the question of dealing with unsatisfactory performance because the ultimate sanction is to take away a cable operator's franchise. We discuss sanctions further in paragraphs 99-101.

92. If franchising is to be a central function, we are clear that the franchising body should nevertheless devise ways to obtain local opinion on rival bids, as is currently the practice in relation to ITV and ILR. Some means may also have to be found to prevent the grant of local authority wayleaves being used as an indirect means of controlling cable systems. We understand that it has been common for local authorities in granting wayleaves to impose conditions requiring the cable operator to pay continuing fees based on a percentage of the system's revenue and to obtain their approval to any increase in subscriber charges, whereas we see no need to control charges. Once cable is allowed greater freedom the scope for further conditions to be imposed would be increased. We therefore take the view that either the central franchising body should have power to grant wayleaves or, if local authorities are to retain the power, the franchising body should have reserve powers to override the local authority if need be.

The cable authority

93. In our view there are only two candidates for a central franchising and oversight body - the IBA with different requirements placed on it in respect of cable television, or a new body.

94. It would be possible for the IBA, which is at one remove from the programme companies and already also looks after ILR as well as ITV, to oversee different regimes for broadcasting and cable. It has great experience in handling franchise applications, administering an advertising code and setting technical standards. It also has a network of regional offices and advisory committees. There is moreover a case for saying that the very fact that it exists would mean that it could take responsibility for cable, under different ground rules from broadcasting, more quickly and smoothly than a new body which would have to start from scratch.

95. Nevertheless, we do not think this would be the best solution. However conscientiously the IBA approached its differing responsibilities, there would be at least an appearance of some conflict of interest which could become real if, contrary to our expectations, cable made serious inroads into ITV or ILR advertising revenue. In any event there would be suspicion that the IBA might have an over-protective attitude to public service broadcasting, and this could deter potential investors in cable. We have expressed the hope that cable will most effectively widen viewers' choice by being innovative and developing in a distinctive way free of the kind of perceptions which presently govern broadcasting and the press; this can best be achieved if its supervision is independent of those who supervise the existing media. We think that the additional work load for the IBA would also be considerable; and it has no expertise in the information technology aspects of cable which should benefit business and the consumer. The evidence we received was overwhelmingly against the IBA being responsible for cable.

96. We therefore recommend the establishment of a new cable authority which should be responsible both for awarding franchises and for monitoring performance.

97. We envisage its governing body having membership based on wide-ranging interests rather than narrow interests relating solely to cable and other media. We see value in ensuring that the interests of the different parts of the United Kingdom are represented so that the desirability of spreading cable throughout the country - and its effects on those areas without it - can be understood from the start. The authority will need a small staff sufficient only to help it with the franchising process and in those aspects of oversight which we identify as essential. Its costs should be modest but will need to be met by appropriate charges.

98. The new authority will need to be established by legislation: and we do not know whether time for this can be found in the next session of Parliament. If legislation in the 1982/83 session is not practicable it would be possible, following discussion and debate of our report, for the Government temporarily to use the powers described in paragraph 18 to issue licences in order to facilitate an early start on the new cable systems. If however this course is adopted, we hope it would be accompanied by the establishment of the new cable authority initially on a non-statutory basis so that it can play its part from the outset and on the understanding that, unless there were exceptional circumstances, Ministers would use their licensing powers in accordance with its advice.

Sanctions

99. We have expressed our conviction that cable should develop with only the minimum of constraints; but we have made it clear that cable operators should be subject to certain obligations. Their programmes will have to comply with the ground rules we proposed in Chapter 6 and their advertisements will have to conform to a code of

practice. They will also be expected to live up to the offers made in bidding for the franchise. The cable authority will have oversight only from a distance, but it will consider complaints and their remedy. How in the last resort should its supervision be enforced?

100. We have referred in paragraph 91 to deprivation of franchise being the ultimate sanction. The existence of this power will in most cases be sufficient. We think it would be rare for the power to have to be exercised, but we have to consider whether this knowledge would weaken the power of the cable authority vis-à-vis an operator who, for example, was committing persistent but relatively minor breaches of the taste and decency requirements or who was making no real attempt to show an adequate amount of British programme material. Do we need the kind of intermediate sanction which exists in other countries to deal with repeated complaints of misbehaviour that could scarcely justify the franchise being revoked? Even if the complaint is not serious enough to justify the franchise being revoked, fear that persistent breaches will reduce the chance of its being renewed is likely to encourage most operators to co-operate. But there may be cases where this is not enough: the franchise may have some years to run and thoughts of renewal may be remote; or the operator may either not wish to continue the franchise or have already given up hope of its being renewed.

101. We have considered the possibility of the cable authority being authorised to impose financial penalties on the operator which could, as in the United States, be taken from a performance bond lodged by him, but we do not think this is a very satisfactory solution: performance bonds in particular are not well suited to failings which are a matter of qualitative judgement, as breaches of taste and decency would be. An arrangement we favour is one in which the operator would forfeit his deregulated position until the cable authority was satisfied that he could be relied upon to meet his obligations without supervision. Thus in the light of

persistent complaints and failure by a cable operator to remedy their cause, the cable authority would be empowered to issue a public warning that recurrence would lead to the operator being brought under closer supervision. For example, he could be required to submit his programme schedules or the details of particular programmes or his advertisements before they were shown. The cable authority would have discretion to apply this across the output of the cable system or restrict it to particular channels; and it would have power to direct that certain programmes should not be shown or even that particular channels should be closed down. The public nature of the advance warning that was given would act as a restraint on unnecessarily interventionist action by the cable authority; but from the cable operator's point of view the imposition of a regulated regime for a period would be a considerable inconvenience and in our view the kind of sanction which, coupled with the threat of revocation of a franchise, will be sufficient.

Chapter 8

SUMMARY OF CONCLUSIONS AND RECOMMENDATIONS

102. Our terms of reference told us to assume the Government's willingness to consider an expansion of cable systems for entertainment and other services, but in a way which would safeguard public service broadcasting; and asked us to make recommendations on the questions affecting broadcasting policy which would arise, including in particular the supervisory framework. We were not therefore concerned with the cable technology to be used or with the provision of services on cable which would have no impact on broadcasting policy. Our task was to consider whether arrangements can now be devised under which cable television and public service broadcasting can co-exist without unnecessary inhibitions on the development of the former and without damage to the essentials of the latter. We believe that they can within the broad perspective we have described. We have considered the potential of cable and the circumstances in which it is most likely to develop. Equally, we have considered the social implications of a situation where some people - either because of their means or because, for a long time at any rate, of where they live - would be able to pay for services which were not available to others. We see no convincing argument against this provided the result is not a deterioration in the range and quality of the broadcasting services freely available to all. We think such a result can be avoided; but to provide both positive encouragement to new multi-channel cable operators and at the same time safeguards for public service broadcasting and those who rely on it involves striking a nice balance. We therefore emphasise the importance of looking at our main conclusions as a whole.

103. Against that background we draw together here our conclusions and the recommendations we have made in the course of our report.

Functions in cable and the case for a franchise system

1. We identify four functions in cable (paragraph 15):

a) the cable provider - the installer and owner of the physical infrastructure;

b) the cable operator - the manager of a local cable system who puts together a package of cable services to sell to customers, from whom he collects revenue;

c) the programme or service provider - the assembler of programmes into channels or segments of channels for sale to cable operators, or the provider of other services;

d) the programme maker.

2. The key figure of these four will be the cable operator. The initiative for the installation of cable systems is most likely to come from him. In any case, he will be answerable to his customers for the service he provides and will be the key figure for the purposes of any supervisory framework (paragraphs 16-17).

3. Because cable systems will have a de facto monopoly, there should be a formal franchising system in which franchises for cable operators should be open to competition (paragraph 18).

4. It is not necessary for the programme provider or programme maker to be licensed; the cable operator should be held responsible for the programmes and services he distributes, other than those for which a United Kingdom broadcasting authority takes responsibility (paragraph 19).

5. A separate licence for the cable provider might not be necessary if the onus is placed on the cable operator to ensure that any system he operates meets the appropriate technical specifications (paragraph 20).

6. There is no need for separation of ownership between cable operator and cable provider; but where the cable operator is also the cable provider he should be required if deprived of his operator's franchise to sell or lease his infrastructure on a predetermined basis to another operator (paragraph 22).

7. The cable operator should be free to provide programmes if he wishes; but care should be taken in awarding franchises to encourage a diversity of programme sources and avoid any undesirable monopoly. There should be an expectation that some channels should be available for leased use (paragraph 23).

Ownership of cable operators

8. Central and local government, political parties and organisations, and religious bodies should be excluded from direct participation in any form in the ownership of companies operating cable systems (paragraph 25).

9. The press, Independent Television and Local Radio contractors and foreign companies should be allowed to participate in the ownership of cable operating companies, but individual companies of this kind should

not be permitted to hold a controlling interest (paragraph 26).

10. It is desirable but not essential that there should be some local participation in the ownership of cable operating companies (paragraph 27).

11. The franchising authority would be able, in the light of local circumstances, to consider whether a particular level of ownership or involvement would have undesirable monopoly implications (paragraph 28).

12. There is no reason why a particular company should not hold more than one franchise. There is little likelihood of a national monopoly arising but the franchising authority could monitor the situation (paragraph 29).

13. There should be no restrictions on the ownership of programme providers but (see paragraph 76) political parties and religious groups should not have their own channels. There should be no restrictions on the ownership of cable providers (paragraph 30).

Cable's sources of income

14. The first source of finance should be the rental charge for a basic package of cable services (paragraph 32).

15. Subscription for particular additional channels should be allowed (paragraph 35).

16. Substantial cable expansion in the United Kingdom is unlikely to be able to take place solely on the basis of rental and subscription (paragraph 35).

17. Because of its ability to provide new opportunities to both local advertisers and national advertisers seeking specialised or local audiences, cable could encourage new spending on advertising and should benefit the consumer (paragraphs 42-43).

18. To enable cable to achieve its full potential, advertising should be permitted (paragraph 47).

19. It is unnecessary in the early years of cable's development to limit the amount of advertising permitted. This would be unlikely to damage ITV or ILR to any significant extent in the short or medium term. There should be flexibility through the franchising process to impose restrictions at a later date if this proves necessary (paragraphs 47-48).

20. Advertising on cable should conform to the same standards and code of practice as apply to ITV; but there is scope for the sponsorship of programmes on cable provided that certain rules including the separation of advertisements from editorial matter are observed. The external pre-vetting of advertisements will be impracticable and a mechanism for dealing retrospectively with complaints will be sufficient (paragraph 49).

21. Pay-per-view should not be permitted for the time being as a method of payment for individual cable programmes (paragraph 50).

Cable programme services

22. Cable operators should be allowed to provide however many new programme channels they choose (paragraph 55).

23. We see no incompatibility between cable expansion and the development of direct broadcasting by satellite (paragraph 56).

24. New multi-channel cable systems should be required to carry all existing and future free BBC and Independent Television and Radio services serving the area concerned (paragraphs 58 and 60).

25. Existing limited-capacity cable systems could be excused this requirement for a period of no more than five years on condition that the operator can and does provide his customers with the means to receive satisfactory signals off-air at no extra cost to them. With the consent of the franchising authority, an existing cable operator could then provide new programme and other services on his system pending the award of a new franchise for the area concerned. He would not however have an automatic right to a new franchise for the areas covered by his cable system (paragraph 59).

26. Cable operators should be free to negotiate the relay of any out-of-area ITV services (paragraph 61).

27. Cable should be free to relay foreign broadcasting services with the agreement of the copyright owners (paragraph 63).

28. Cable programme services should not be confined to a "narrowcasting" role. Conversely they should not be subject to the public service broadcasting requirements regarding range and balance. The diversity of services to be carried should be taken into account in the franchising process (paragraphs 65-67).

29. Cable should not be allowed to obtain exclusive rights for national sporting events of the kind which are protected under section 30 of the Broadcasting Act 1981. These events may need to be the subject of a regulation by the Home Secretary and the list may need to be revised from time to time (paragraph 70).

30. There should be no specific obligations on cable systems to provide facilities for community programming and local access but there should be a presumption that these would be provided and proposals for such facilities should be taken into account in the franchising process (paragraph 71).

31. For the reasons given in paragraph 11, we do not think that at the present time cable television can be regarded as just another branch of publishing, subject only to the law of the land, or that self-regulation would be acceptable. Cable programmes, with the single exception covered in the next recommendation, should be subject to the same obligations as the BBC and IBA not to offend good taste or decency, to be likely to encourage crime or lead to disorder or to be offensive to public feeling, as well as to have special regard to programmes broadcast when large numbers of children and young persons are likely to be watching (paragraphs 72-74).

32. However, on any channel for which a specific subscription is paid and which is capable of being electronically locked by the subscriber there should be no restriction on the time for showing the sort of films currently shown late in the evening because they are unsuitable for children. Additionally, we think it would be acceptable on such channels to show at any time any film passed for public exhibition by the British Board of Film Censors in an existing censorship category (see footnote to paragraph 75).

But we would not go further in allowing the showing of other films or video material which do not conform to traditional taste and decency requirements (paragraph 75).

33. News should always be presented impartially. Otherwise, impartiality on individual channels need not be required but a cable system as a whole should not maintain a position of bias. There should be impartiality of access to local cable channels (paragraph 76).

34. There should for the time being be no minimum quota of British material but the use of British material should be encouraged (paragraph 77).

35. There should be no formal restrictions for the sake of the cinema industry on the films which may be shown on cable, but there is a case for equality of treatment as to the requirement to contribute to the British Film Fund (paragraphs 80-81).

36. The Government should consider the implications for the existing copyright law of a decision to allow greater freedom to programme services on cable (paragraph 82).

Oversight

37. Oversight has both a positive and a reactive role. The positive aspects should be centred on the franchising process. Thereafter, oversight should be reactive, intended to ensure that certain ground rules are observed but without constant supervision of the services provided (paragraph 84).

38. Although the franchising body may take the initiative in delineating franchise areas and inviting applications, it should also be possible for cable operators to take the initiative in applying for franchises in areas of their choice (paragraph 85).

39. The franchise decision should take account of (paragraph 86):

a) the size of the area, for which we have suggested certain criteria but recommend no arbitrary limits; the comprehensiveness with which all streets within the area will be cabled; and in some cases the desirability of encouraging the cabling of less commercially attractive areas along with those with the best prospects;

b) the speed of installation of the system and the sequence in which different parts of it are to be cabled;

c) the ownership of and interests represented in the prospective cable operating companies and any problems of monopoly;

d) the channel capacity and the range and diversity of programme channels, including the financing arrangements;

e) arrangements for community programmes and local access;

f) the intentions regarding the provision of interactive services.

40. The term of the franchise should ordinarily be eight years but should in the first instance be ten years (paragraph 87).

41. Existing cable operators should be able to continue pending the grant of a franchise for their area. Master antenna cable systems providing only broadcast relay would be able to continue notwithstanding the grant of a multi-channel cable franchise for the area concerned (paragraph 88).

42. Once a franchise has been awarded oversight should be on a monitoring and reactive basis only. There is no need to control charges to cable customers. Programme schedules should not require advance approval. Advertisements should not be subject to external pre-vetting. There should be no constant scrutiny of output (paragraph 89).

43. The approval of the franchising body should be required to any subsequent change in ownership of a company operating a cable system or significant modifications in programme channels (paragraph 89).

44. There is a need for a body to keep in touch with what is going on; serve as a forum of advice to operators; be generally known as the body to consider complaints; keep an eye on the use of United Kingdom programme material and developments in advertising; judge whether cable operators are living up to their promises; and respond flexibly as cable develops. This would have to be done by a central body (paragraphs 89 and 91).

45. Franchising should also be undertaken centrally rather than by local authorities. Promise and performance can then be judged by the same body. The central franchising body should however devise ways to obtain local opinion on rival bids. The franchising body should have power to

grant wayleaves or it should have reserve power to override the wayleave powers exercised by local authorities (paragraphs 90-92).

46. A new cable authority should be established and given responsibility for awarding franchises and monitoring performance. Its governing body should have a membership based on wide-ranging interests rather than one relating solely to cable and other media, and the interests of different parts of the United Kingdom should be represented. The cable authority should be a statutory body. If necessary it should be established initially on a non-statutory advisory basis (paragraphs 96-98).

47. The ultimate penalty for any cable operator who was grossly in breach of his obligations would be loss of his franchise (paragraph 100).

Right of appeal? To whom?

48. A less drastic sanction will be needed for use in circumstances not warranting loss of the franchise. Financial penalties are not recommended. A better course would be to give power to the cable authority to impose a regulatory regime on a cable operator for a period by requiring the submission of programme schedules or the advance vetting of programmes or advertisements (paragraph 101).

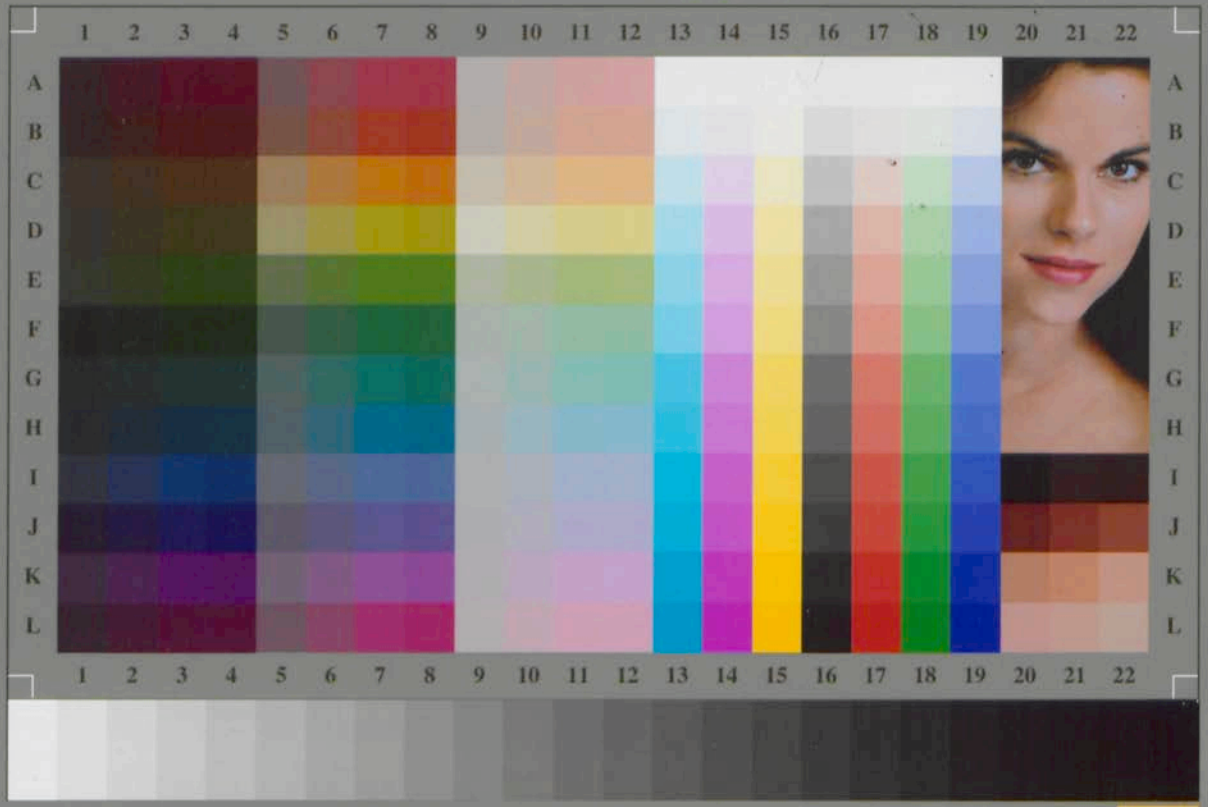
PART 5 ends:-

A. Walters to MCS of 21/10/82.

PART 6 begins:-

RTA to PM (A09907) + att of 28/10/82

KODAK Q–60 Color Input Target



IT8.7/2–1993
2007:03

FTP://FTP.KODAK.COM/GASTDS/Q60DATA

Q-60R2 Target for
KODAK
Professional Papers