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Secretary of State for Trade and Industry

14 May 1985

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

Dear Nigel,

CABLE INDUSTRY : CONSORTIUM RELIEF

I am becoming increasingly concerned about the ability of the 'independent' cable operators to raise the finance necessary to fund their cable franchise proposals. If the 'independents' fall by the wayside we will be left with the development of the industry only in the hands of the large operators, such as BT, Rediffusion and Thorn EMI, with what that implies for reduced competition and customer service. It is an outcome that we should avoid if at all possible.

2 Our policy has always been that the cable industry should be privately financed, without special public financial support. That must remain our position. The attractiveness of investment in cable was undoubtedly substantially reduced by the phasing out of accelerated capital allowances announced in last year's Budget: but the main problem now facing the 'independent' operators is that they are at a substantial disadvantage compared with the large integrated groups. The latter can at least offset the lower revised taxable losses of their cable subsidiaries in the early years by way of group relief against the profits of the rest of their business; so yielding a still reasonable, if not spectacular, commercial rate of return. To achieve a comparable rate of return to the large operators and so offer serious competition, the independents, who do not have profits against which to set early losses, have to find a way of passing on the tax losses in the early years to their equity investors.

3 In response to representations my officials have been encouraging the independents and their financial advisers to consider the use of consortia. You agreed in last year's Budget to relax the conditions of consortium relief with the cable industry

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principally in mind. The increase in the minimum number of consortium numbers and the inclusion of overseas members have proved very useful to the cable industry. But it has become clear that for the cable 'independents' some serious drawbacks to consortium relief remain.


4 The problems arise because shares in a consortium company must not be held as a trading asset of the claimant company. Financial institutions, which in these cases would be the predominant consortium members, are taxed as share dealers and would therefore have to invest in the consortia via investment companies. While there would be no difficulty in setting up specific investment company subsidiaries for the purpose there are significant tax disadvantages compared with group relief from which the large operators can benefit.

5 To remove this bias I believe that two amendments will be required to the consortium relief rules:

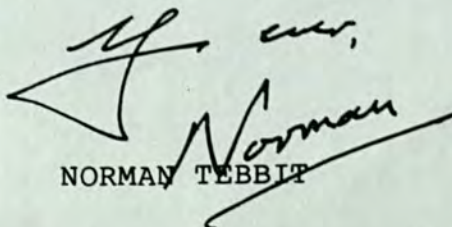
- amendment to S.258(2) ICTA 1970 to allow a consortium member's share of consortium relief to be surrendered to other members of a consortium member's group;
- amendment to S.263(5) ICTA 1970 to allow losses of a consortium member to be offset partly against its share of the consortium profits and partly against the profits of other companies within the group.

6 We have advocated these changes over the last few years within the Revenue's review of group relief. The issue is now particularly pressing and I hope that you will be able to agree to these amendments, to redress the balance against the 'independent' cable operators.

7 I appreciate that these amendments will require complex and lengthy legislation if the possibility of tax avoidance is to be prevented. If it is not possible at this late stage to draft the legislation in time for this year's Finance Act, a public commitment this year to legislate in the 1986 Finance Act would be a less desirable but still satisfactory way round the problem.

8 In view of our strong support for cable and the recent report by the Prime Minister's Information Technology Advisory panel  which urged the Government to find ways of encouraging the development of cable. I do hope that you feel able to help.

9. I am copying this letter to the Prime Minister.

  
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