**PRIME MINISTER** 14 April 1989

Agreed MT

**BROADCASTING: LOCAL SERVICES AND CHANNEL 6**

This was the area of the White Paper in which Ministers and officials had little first-hand knowledge. It was also the most complex area, and probably for these reasons, the one least thought out.

The consultation process on cable has been very useful. Cable companies, and especially US companies which have considerable experience of cable in the US, have made excellent submissions. As a result, the official group have proposed major amendments which the Home Secretary has circulated for approval.

**The Policy of the White Paper**

This was to:

(i) permit local operating companies to provide local broadcasting and television services, using either cable or MVDS - the choice being based on commercial considerations and with government therefore being technology neutral;

(ii) restrict companies to either the delivery or the retailing of local services;

(iii) allocate local delivery franchises by competitive tender;

(iv) impose a levy on local services;

(v) compel the ITC to consider issuing second franchises in local areas after a short period of time.

## Revised Proposals

### (i) Separation of Delivery and Retailing

The basis of the separation, as well as the tender system of allocation and the award of the second franchise, was on grounds of competition policy.

Potential investors, however, have made it abundantly clear that there is no way in which they will continue investing in cable if such a restriction is introduced. The financial returns are so reduced by this process that the investment is not worthwhile. An excellent study by Charles Jonscher (who has done very good work for both Home Office and DTI) confirms this view. It suggests rates of return on capital falling from 25% to between 2% and 8% depending on how rigidly separation is enforced.

From the point of view of competition policy, the key distinction is between a mature and an immature industry. At a time when cable and MVDS are just getting going, and they face the extra competition from satellite and Channel 5, monopoly considerations are hardly likely to be major ones. When the whole of the country is cabled, and the industry is mature, it could be a different story.

**Meanwhile, the Home Secretary is right to abandon the rigid separation.**

### (ii) Levy

Once again, a levy over and above general taxation only makes sense to reduce monopoly profits. Because of the infancy of cable and MVDS, potential competition from other sources, as well as the competitive tender for franchises in the first place, the introduction of a levy makes little sense.

**The Home Secretary is right to recommend withdrawing this proposal.**

**(iii) <u>Second Franchises</u>**

Quite apart from the fact that existing franchises may not be very profitable, it is doubtful if sufficient spectrum exists for this purpose.

**The Home Secretary is right not to impose a requirement on the ITC to issue a second franchise in a short period of time, but should the opportunity present itself, the ITC should have the right to do so.**

**(iv) <u>SMATV</u>**

(Satellite Master Antenna Television, ie [typically] a communal dish for a block of flats, or to feed a small area by cable from the dish.

The White Paper said nothing on this, but it has emerged as an important problem for Sky Television.

SMATV systems can only be established with a licence from the Cable Authority. Because the Cable Authority has a duty to promote cable, it has not generally been willing to licence SMATV systems to protect existing cable systems and to avoid prejudicing its future franchising policy.

The case for liberalising is:

a) the ITC is not being set up to promote cable - it is meant to be technology neutral;

b) people living in blocks of flats will not be able to receive satellite TV unless the current system is changed.

The Home Secretary recommends substantial liberalisation which should certainly cover the requirements of Sky. Once again, this deserves to be accepted.

Local Services: Recommendations

Accept the Home Secretary's revised proposals to:

(i) permit operating companies to combine delivery and retailing;

(ii) withdraw the levy;

(iii) allow second franchises but not make them obligatory;

(iv) liberalise SMATV.

The Home Secretary also recommends two minor changes:

(a) phrase the announcement in such a way that it does not rule out introducing pricing to allocate unwanted spectrum;

(b) to ensure that existing cable operators are not disadvantaged by the new proposals involves defining what "existing" means: the new proposal does so by including both operators awarded franchises before the publication date of the White Paper, and those whose will be successful but which were submitted before that same date.

Both of these are sensible.

## Channel 6

The proposal from David Young is not to proceed with further work for Channel 6 because:

- for Channel 6 to extend its coverage to 40% of UK households would require 20,000 viewers in up to 10 areas being unable to receive either BBC1, BBC2, ITV or C4;

- extending Channel 6 would mean abandoning the installation of 200 relay transmitters to bring existing terrestrial services to an extra 350,000 people;

- it would also involve spectrum capacity problems for existing outside broadcasts plus independent producers;

- Channel 6 would require households to install yet another aerial.

## Recommendations

**As deregulation is already providing substantial extra competition, the costs of Channel 6 appear much larger than the benefits the extra channel would provide.**

**Accept David Young's proposal: the suggested [PQ] answer is very clear.**

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