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C. Adygnid
J. A. Watters (4)
Prime Minister 27/10/45

CHANCELLOR OF THE EXCHEQUER

To note. We are penciling
in a meeting (see penultimate para) for 27/10.
MUS 13/10

TELEVISION LICENCE FEE

In my minute of 29th June to the Prime Minister I outlined a strategy for our handling of the next television licence fee increase: that we should go for an increase which would have to last the B.B.C. for three years and which would be subject to certain conditions designed primarily to ensure that it did so. At our meeting with the Prime Minister this strategy was agreed.

Since then, we have received the B.B.C. application for a licence fee increase, which amounts to a request for fees of £52 for colour and £15 for monochrome, to last until the end of 1984 (or £53 and £15 to last until March 1985). Your officials and mine have examined this application and a good deal of additional information has been sought from the Corporation in order to clarify certain aspects of it. I have also been considering in more detail what conditions should be attached to a three-year increase, and how they could be made to stick. And I have had a preliminary talk about the application with George Howard and some of his senior people.

The further thought that I have given to the problem, and my talk with the B.B.C., has confirmed my provisional view that the right course is to go for a three-year increase, provided the new licence can be set at a level that enables the B.B.C. to maintain a service at a satisfactory level and does not provoke too much resentment from the licence-purchasing public. The case for a three-year increase is essentially the one set out in my earlier minute, but four points are worth recalling:

- (a) even if we went for a one-year licence, we would not avoid a substantial increase - it could not be set lower than £42 (and £15 for monochrome); and we should face further increases in the two succeeding years. The increase to a figure that

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the public could be assured would last for three years would not be all that much greater.

- (b) a three year increase would have the advantages of giving the public a sense of stability, and of taking the issue out of the public eye until beyond the next Election; and it should help to sap the campaign for concessions in deserving cases which - however much we may sympathize - would be costly, and hard to draw up on a defensible basis.
- (c) the licence fee system is important to the independence of the B.B.C. from Government and enables public service broadcasting to be financed otherwise than from public expenditure. A series of one-year increases would go a long way to undermining it.
- (d) a three-year increase enables the B.B.C. to plan ahead in a realistic and disciplined way.

But all depends on getting right the level, and the conditions.

First as regards the conditions, the Chairman of the B.B.C. has agreed to commission a wide-ranging efficiency audit, and has engaged Peat, Marwick and Company (who have experience on the I.T.V. side) to conduct it. He is keen to make an early announcement. The resulting report could be expected in something like nine months time. The Chairman is happy to make it available in confidence to the Home Office and the Treasury. In the light of its findings, and the B.B.C.'s reaction thereto, you and I will need to consider what further information to ask the B.B.C. to supply before the next increase in licence fee. The efficiency audit would be on top of the value-for-money audits which the B.B.C., of its own initiative, has asked its own auditors to undertake in particular areas of the organisation. And of course the Corporation has its own management service people and in general gives me the impression that it cares a good deal about the pursuit of efficiency.

Next, the question of expenditure limits. The B.B.C. need, for their own purposes, to draw up an annual expenditure plan, in particular so as to ensure that too much of the three-year income is not spent in the first year. They will bring this plan (and any change in it) to me, so that we shall have an opportunity of commenting on it and, if necessary, warning them of the necessity of making the licence fee last at least three years. But in the last analysis decisions about apportioning expenditure over the three years must be theirs. What is crucial, if a three-year increase is to last, is that the B.B.C. should understand - and proceed on the assumption - that the net revenue which the licence fees will produce in the three years is all it is going to get; so that it plans to build up a surplus of revenue in the first year to finance a shortfall in the third in order to reach the end of the three years with a nil deficit. That is the real discipline of a three-year increase. To achieve this end I believe that the right approach would be to make it clear to the Corporation that:-

- (a) the next increase will last for at least three years - i.e. the fees will not be increased before November 1984.
- (b) furthermore it must plan on the basis that there will be no fee increase until the end of March 1985 - i.e. for the rest of this year and the next three full financial years;
- (c) it must have a nil deficit in November 1984 and should aim to have a nil deficit in March 1985;
- (d) if it appeared from these plans that the Corporation would be going into deficit between November 1984 and March 1985 it should not assume that I will necessarily be prepared when I come to fix the next increase after November 1984 to take the deficit into account: the effect of my not taking the deficit into account would be to reduce the B.B.C.'s borrowing powers.

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Of course, the strategy of a three-year increase has risks, which we have to take into account in fixing the level of licence. If the increase decided on turns out to be insufficient, either because of inflation or because the B.B.C. fails to control its expenditure, or because licence revenue from the fees we fix fails to match our estimates, I could be faced with a serious B.B.C. financial crisis, quite possibly in the run up to the Election. In this event our strategy - indeed the licence fee system itself - would have to be reviewed.

As I said above, the B.B.C.'s request is for an increase to £52/53 (monochrome £15). To judge from the B.B.C. inspired talk of a "£50 licence", even the Corporation does not expect to get £52. And we could not contemplate so high a figure.

The B.B.C. seeks, over the next three years, some £140m (at April 1981 prices) for maintaining and improving the quality of the existing service, and for certain new services (including the increase in Welsh language programmes). A further £80m (at April 1981 prices) is sought for capital expenditure, largely for the replacement of ageing equipment. I do not believe that the licence fee increase should reflect these objectives in full. On the other hand I am convinced that the B.B.C. will have to spend more in real terms, in order to prevent further decline in the quality of the existing service which has undoubtedly gone down over the last couple of years. I believe that the Corporation should also improve its services in the sense of reducing repeats and bought-in material. I believe too that the case for some increase in capital spending (when there has been a history of cutting back) is made out. I recognize, and have put to the B.B.C., the difficulty for the Government in approving a fee increase that allows for growth at a time when cut-backs in services are the order of the day. But what seems to me the crucial point here - and one which the B.B.C. has stressed to me - is that it is one part of an enterprise the rest of which is in the private sector. It is in direct competition with I.T.V., whose advertising revenues

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are holding up well (and, prospectively, with the Fourth Channel). It would not be in the interests of a healthy broadcasting system to allow too wide a gap in standards to develop between the B.B.C. and I.T.V. The B.B.C. say that they also need a further £140m (current prices) over three years to halve the gap that exists between what they and I.T.V. pay to staff and artists. We cannot ignore this point because the quality of a broadcasting service depends so heavily on the quality of the creative people making the programmes.

The remaining, and larger, part of the B.B.C.'s case - £670m (current prices) over three years - reflects their assumption that inflation of their costs will amount to 10% per annum generally (and more as regards some specific costs) over the three-year period. I have made clear to them how difficult it is for H.M.G. to accept from them - and still more to base a licence increase explicitly upon - estimates of future inflation which are at variance with its own intentions. The risk in a three-year settlement which makes inadequate provision for increases in costs is of course that the B.B.C. may simply run out of money (including borrowing capacity) before the period expires - possibly in a pre-Election period.

So much for my general approach. It is not my task to go through the Corporation's detailed plans, accepting some and rejecting others. I do not have any control over how the B.B.C. spends its money in detail. To do so would anyway be artificial, because our primary aim must be to make the three-year strategy work. If we can do that, we shall have achieved an important objective. If we fail because we set the fee level too low, or abandon the attempt because we cannot bring ourselves to set it at a level that enables the B.B.C. to operate throughout this period, we place ourselves in great difficulty, for the reasons that I have indicated.

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As regards the actual amount of the new licence, I see the minimum licence likely to last for three years as £46 (£15 monochrome). That would allow the B.B.C. to increase its rate of spending by 11 per cent a year - i.e. would provide for inflation and some modest growth (unless, that is, the B.B.C.'s more pessimistic inflation assumptions were proved right). But as I said in my minute of 29th June - and subsequent talkswith them has reinforced my earlier view - the B.B.C. would forcefully object to an increase to no more than £45 and I am certain that they would have a good deal of support from a number of our own backbenchers and a section of public and press opinion. To avert that, and to make it more sure that the settlement will last the three year period, I believe there is a good case for an increase to £48 and £15.

The presentation of the increase to Parliament and the public will need careful handling. I should want to announce the increase in the context of a new strategy for making the licence fee system work and for enabling the B.B.C. to plan ahead. I should spell out that the increase would have to last for at least three years; that the B.B.C. will be expected to plan on the basis that the increase will have to last until the end of 1984-85, and on the basis that it should pay off its current deficit and keep out of deficit until March 1985. I should also want to welcome the B.B.C.'s plans for a wide ranging efficiency audit and say that the results will be taken into account when the fees are next reviewed. I would say that the fee increases should enable the B.B.C. to sustain the quality of its existing services but that the extent to which it will be able to do so will depend on its ability to keep down its costs, particularly labour costs. By using a formula of this kind I should hope to avoid (and would hope that the B.B.C. would also avoid) any detailed discussion of what element in the increase represented an allowance for future inflation. I should also want to say as much as I can about the development of methods of paying the fee by instalments.

Tentatively
arranged
for 27/10
MUS

I suggest that we should seek the opportunity of a discussion with the Prime Minister about these proposals soon after she returns from Mexico. It might be helpful if you and I had a preliminary meeting in the meantime and perhaps our offices could be in touch about that. When we have reached decisions on these proposals, I should then need to secure - as I believe I can - the B.B.C.'s agreement to the conditions I have outlined above. I envisage that the increases should be announced on 24th November (the day after the two year anniversary of the last increase). They could hardly be announced in December because of Christmas, and I should prefer not to announce in January, so soon after Christmas. By February the B.B.C. could well be right up against its borrowing limit.

I am sending a copy of this minute to the Prime Minister, and to Sir Robert Armstrong.

Ann T. L.

(Private Secretary -
approved by the Home Secretary
and signed in his absence)

13th October 1981

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