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10 DOWNING STREET
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From the Private Secretary

20 July 1987

Dear William,

MISC 128: INDEPENDENT TELEVISION PRODUCERS

At this morning's meeting of MISC 128, the Prime Minister promised to send the Home Secretary information which she had received privately about the position reached in negotiations between the independent producers on the one hand and the BBC and ITV companies on the other.

In terms of hours, by 1989 twenty-five per cent of the new output of ITV would be 2,430 hours, made up of 1,024 hours for network programming plus 1,406 hours of regional or local interest programming. Against this ITV had, earlier this month, offered just 500 hours to be achieved over the first two years. For the BBC, twenty-five per cent of new output is forecast at 2,569 hours, 1,512 hours network and 1,057 hours regional. The BBC have offered 500 hours per year of independent production to be achieved by the production year 1991/92. A similar figure of 500 hours would be achieved by ITV by the end of 1989.

The BBC has earmarked for independent production £20 million against £113 million that the BBC itself would spend. The BBC have alternatively offered to allow the independents use of BBC facilities.

The broadcasters are insisting that in return for entering into a contract to supply a programme the independent would be expected to give up all rights to distribute or exploit the complete programme elsewhere in the world. In addition, the independent must relinquish all ancillary rights related to the programme, the material or idea upon which it is based, or those included within it.

The ITV companies are insisting on the right to hold between twenty per cent and twenty-five per cent of the shares of an independent producer whose productions would count towards the achievement of the targets set for independent production in ITV schedules.

The information is not always clear, but this gives the flavour.

David Norgrove

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MINISTERIAL GROUP ON BROADCASTING SERVICES

20 JULY 1987

ITEM 3: INDEPENDENT PRODUCERS

CONCLUSION

The Manifesto for the last Election said that

"We will ensure that at least 25 per cent of programmes broadcast on both ITV and BBC will be supplied by independent producers as soon as possible."

2. You will wish the Group to reach decisions on how the Government should respond to the proposals the IBA and the BBC have brought forward for moving towards this target. The options the Home Secretary identifies are

(i) broadly to welcome the proposals and to ask the broadcasters to work out the details; or

(ii) to take the view that the proposals are inadequate and to prepare legislation to place a duty on the broadcasters to take 25 per cent of their programmes from independent producers.

A compromise would be

(iii) to put the ball back in the broadcasters' court by telling them that unless they - or at least the BBC - improve their proposals legislation will be introduced to place a duty on them to take 25 per cent of their programmes from independent producers.

This option was earlier favoured by the Chancellor.

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BACKGROUND AND MAIN ISSUES

3. At its meeting on 30 October (MISC 128(86)2nd Meeting), the Group agreed that steps should be taken to encourage the greater use of independent producers. This was expected to have the effect of reducing costs, not least by weakening the ability of broadcasting unions to sustain restricted practices; encouraging greater diversity and innovation; promoting exports (on which the independent production sector has a better record than either the BBC or ITV companies); and reducing the dominance Channel 4 currently exercises over the independent production sector. The Home Secretary proposed that a precise figure should not be set; but the Group decided that a quantified target was needed to ensure that progress was satisfactory. It invited the Home Secretary to open discussions with the industry on the basis of the target of 25 per cent use of independent producers to be achieved over 4 years.

IBA Proposals

4. The IBA have drawn up an intermediate target of an annual production from the independent sector of 200-400 hours of locally shown material and 175-225 hours of network material (ie 8-10 per cent of network output) by the end of 1989, when the current ITV contracts come to an end. They then propose to review the position and, provided the independent sector have proved capable of delivering the quantity and quality of programmes required at competitive cost, they believe the 25 per cent target will be achieved within the contract period 1990-92. The IBA are optimistic that the ITV companies will agree to their scheme but they have indicated that they would be willing to write provisions into the contracts for 1990-92 should this prove necessary.

5. Both the Chancellor of the Exchequer and the Trade and Industry Secretary are likely to suggest that, while the timescale is rather longer than the 4 years originally envisaged, the IBA proposals are

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broadly satisfactory. The Trade and Industry Secretary may ask that the question whether the IBA have the necessary legal powers to impose targets in the 1990-92 contract provisions should be clarified before the Government responds to the broadcasters. However, this does not seem necessary: if, on further investigation, the IBA appear not to have the requisite powers, this can be remedied in the Broadcasting Bill planned for later in this Parliament.

BBC Proposals

6. The BBC plan by mid-1990 to have allocated finance for the commissioning of 500 hours from the independent sector to be added to the 100 hours already provided by independent producers. The 500 hours would be network programmes, representing 8 per cent of the total BBC network programme production budget excluding news and news-based programmes which the BBC believe should continue to be made in-house. This would be supplemented by increased co-productions with the independent sector together with the possible use of programmes made by independent producers as a result of commissions by commercial sponsors (on which the Home Secretary will be consulting colleagues separately in due course). From 1990-92, depending on a review of the independent sector's performance up to that time, the BBC would move to the second phase of increasing independent production in which they would "recognise the Government's desire" to reach the 25 per cent target.

7. As both the Chancellor of the Exchequer and Mr Channon as Trade and Industry Secretary have pointed out in correspondence, these proposals are manifestly inferior in a number of respects to those of the IBA. First, much of the 100 hours already provided by independent producers would not count as independent productions under the Peacock definition since they generally represent the work of free-lancers who make use of BBC crews, studios and other facilities. Second, the BBC target of 500 network hours by mid-1990 is expressed in terms of the allocation of finance; because of the lead times

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involved, this will not translate into programmes actually transmitted until the end of 1992. Third, the BBC have excluded from their calculations news programmes and news-related programmes including "Breakfast Time". Fourth, the BBC's commitment beyond 1990 simply to "recognise" the Government's target is exceedingly vague. Finally, a point applying also to the IBA proposals, the review in 1990 will be in-house and must therefore be of doubtful impartiality.

Next Steps

8. The Home Secretary says that the two sets of proposals represent a major shift in practice and thinking and that the initiative will develop its own momentum. He believes that the Government should now welcome the broadcasters' proposals and ask them to work out the details. The threat of legislation can be kept in the background should they fail to deliver. The Home Secretary believes that this approach would enable an early start to be made whereas a decision to legislate could well result in the withdrawal of co-operation and therefore delay. The Lord President agrees with the Home Secretary that the voluntary approach is the best way of proceeding.

9. The Chancellor of the Exchequer and the Trade and Industry Secretary, on the other hand, will argue that the BBC should be told that, unless they substantially improve their proposals, the Government will have no choice but to introduce legislation to compel them to meet their target. They believe that if the Government were to approve their current proposals, the BBC would not take future threats of legislation seriously. The IBA could be told that the possible need for legislation reflected not on them but on the BBC's failure to co-operate.

10. The choice facing the Group is, therefore, not quite so stark as the Home Secretary portrayed it in his minute of 19 May. If the Group considered the BBC's proposals to be unsatisfactory, it would not be necessary straightaway to take a decision on whether or not to

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introduce legislation; the Group could instead invite the Home Secretary to make clear to the BBC that unless they substantially improve their proposals, it would probably be necessary to introduce legislation to place a duty on them to comply with the Government's target. A final decision on whether to introduce legislation could then be taken in the light of the BBC's further proposals and could take account also of the risk that the introduction of legislation could cause a withdrawal of co-operation and the consequent postponement in the use of the independent sector. The Home Secretary may resist this on the ground that it is unlikely to secure any real improvements in the BBC's proposals. However, it seems likely that the Group will conclude that the BBC's proposals are so far short of the Government's target that, unless they are substantially improved, the Broadcasting Bill which the Home Secretary hopes to bring forward in the 1988-89 Session should include provisions placing a duty on broadcasters to meet that target. If, in the meantime, the BBC withdrew co-operation the proposals are so inadequate that little would be lost.

HANDLING

11. You will wish the HOME SECRETARY to introduce this item. You may then wish to invite the LORD PRESIDENT, the CHANCELLOR OF THE EXCHEQUER and the TRADE AND INDUSTRY SECRETARY to comment.

MINISTERIAL GROUP ON BROADCASTING SERVICES: 20 JULY 1987

ITEM 4: THE SALE OF UNUSED TELEVISION NIGHT HOURS
(PEACOCK RECOMMENDATION 9): MISC 128(87)3

OBJECTIVES AND CONCLUSIONS OF THE MEETING

This paper deals with the only Peacock recommendation which the Group have yet to address. The Home Secretary invites the Group to note his provisional conclusions which are

- i. Peacock's concept of unregulated night hours' franchises should be rejected.
- ii. Any improvements to the ITV contract system should apply also to contracts for night hours.
- iii. The Home Secretary should explore with the IBA the case for developing separate and competitive contracts for night hours on the ITV frequencies.
- iv. Channel 4 should be left free to develop its night hours, at least if the Home Secretary's proposal for the contingent separation of Channel 4 is accepted (this will have been discussed under Item 2).
- v. No decision should be taken at this time on the BBC's night hours pending further consideration of subscription.

2. These proposals are contingent in large part on the conclusions reached on the ITV system and on Channel 4 (which will have been discussed in Item 2) and on the decisions taken in due course on subscription (on which the consultation period on the CSPI report ends on 30 September). No decisions need to be taken at this meeting,

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though the Group may wish to give the Home Secretary a steer on at least some of his proposals. An appropriate conclusion might be that all these matters be considered further by the Official Group (MISC 129) in the context of the working up of the proposals on the ITV system and of the further consideration of subscription. The Home Secretary could bring his proposals back for decision once this work has been undertaken.

BACKGROUND AND MAIN ISSUES

3. Peacock recommendation 9 was that the hours between 1.00 am and 6.00 am should be removed from the IBA and BBC and sold through the aegis of the Department of Trade and Industry to the highest bidder, the proceeds to be retained by the Treasury. The IBA companies and the BBC would not be permitted to bid for this slot for three years to prevent them from inhibiting potential new entrants. The assumption was that the air time would be used as a subscription service down-loading programmes for video recording.

4. The Home Secretary rejects Peacock's recommendation that night hours broadcasting should be left unregulated save for the criminal law, and this is clearly right. However, while there is no reason why controls on sex and violence should be made any less effective than those which will operate on broadcasting generally, there may be scope for a lighter touch (similar to that exercised by the Cable Authority) on matters such as scheduling.

5. The Home Secretary also rejects Peacock's recommendation that there should be a simple auction to the highest bidder. He proposes instead the same arrangements as he puts forward for the ITV system: a modified form of competitive tender subject to a quality threshold. Provided the Group agree the proposed tender arrangements for the ITV system (which will have been discussed under Item 2) there should be no difficulty in agreeing that the same arrangements should apply for night hours. However, the Trade and Industry Secretary may wish to

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make the point that the quality threshold should not be set so high that few, if any, bidders come forward.

6. The Home Secretary suggests, consistent with Peacock, that there is a good case, for ensuring that after the 1989 or 1992 contract round ITV night hours are used other than by existing ITV contractors. This will probably be welcomed by the Group: night hours stations will not require much capital to set up and the exclusion of day-time contractors will encourage new entrants. The Chancellor of the Exchequer and the Trade and Industry Secretary may press for these arrangements to be established in time for the 1989 contract round: this would help to prepare the ground for the major contract round in 1992 when it is hoped that several new companies will seek entry into the market.

7. The Home Secretary suggests that it would be consistent with his proposals to provide for the separation of Channel 4 for it to be allocated 24 hour use of its channel. However, the Group may think it premature to take a view on this until further work has been undertaken on the future of the ITV system and on subscription.

8. The Home Secretary suggests that, given the decision to index the licence fee and to require 25% independent productions, the BBC is well on course to become more commercial and more cost conscious and that there may be a case, therefore, for its retaining its night hours. Other members of the Group may not share his optimism about the BBC but the Home Secretary's conclusion that no decisions be taken until further work has been undertaken on subscription seems clearly right.

HANDLING

9. You will wish to invite the HOME SECRETARY to introduce this item. You may then wish to invite the CHANCELLOR OF THE EXCHEQUER and the TRADE AND INDUSTRY SECRETARY to comment.

MINISTERIAL GROUP ON BROADCASTING SERVICES:

20 JULY 1987

ITEM 2: THE INDEPENDENT TELEVISION SYSTEM MISC128(87)2

DECISIONS TO BE REACHED

The purpose of this item is to consider the Government's stance on the future development of the independent television system, including Channel 4.

2. You will wish the Group to reach clear views on the matters on which the Home Secretary seeks decisions. These are that the Official Group should develop proposals for:

(i) the allocation of ITV contracts by competitive tendering with contracts incorporating annual payments based on advertising revenue (paras 5-10 of Memorandum);

after passing IBA quality tests

(ii) legislation providing for the separation - to be triggered by secondary legislation - of Channel 4 from the IBA with a requirement to finance itself through its own advertising but to preserve its present distinct programme service (paras 14-16 of Memorandum).

Once the Official Committee have reported back and the Ministerial Group have reached conclusions on these matters, the results would be included in the White Paper proposed under item 1.

3. The Home Secretary invites the Group also to take note:

(iii) that he proposes to invite the IBA to devise an improved system for the supply of programmes to the ITV network (paras 12-13 of Memorandum);

(iv) that he and the Trade and Industry Secretary will keep under review the position on advertisers' complaints about ITV

sales practices in the light of the inquiry (which has now been established) by the Office of Fair Trading (para 11 and Annex to Memorandum).

MAIN ISSUES

(i) Allocation of ITV Contracts and Levy Arrangements

4. Under the present arrangements for the award of contracts to ITV companies, the IBA selects the prospective contractor which seems likely to provide the best mix of programmes. The likely return to the Exchequer through levy and tax is not relevant (though the financial plans are taken into account in assessing whether the programming promises will be fulfilled). The contract period is eight years.

5. These arrangements are open to accusations of arbitrariness in that it is difficult to assess objectively which company will produce the best programming. The present arrangements also provide an in-built advantage to existing contractors because the IBA is inclined to have more confidence in companies with an existing track record. A majority of the Peacock Committee therefore proposed a system of auctioning the franchise contracts.

6. The IBA answer to all this is to propose the extension of the contract period from 8 to 12 years with full-scale review of a company's performance in the fifth and ninth years and the option to renew contracts without readvertisement if this seemed desirable in the light of the second of these reviews. Such an arrangement would, of course, further entrench existing contractors. It totally fails to meet the objections to the existing arrangements.

7. Like Peacock the Home Secretary proposes instead the introduction of a system of competitive tendering. Under his proposals (which are developed from Peacock's outline) the IBA would set a quality threshold and would then select the company satisfying that

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requirement which put in the highest bid in the form of a lump sum payment, part of which might be phased over the contract period.

8. The Home Secretary proposes that contractors should also pay an annual rental based on revenue. This would replace the existing levy based on profits. The profits levy is currently 45% for UK profits (above a certain threshold) and 22.5% for overseas profits. Together with corporation tax, this makes for a marginal rate of deduction of 64.3%. The majority of the Official Committee considered that this provided insufficient incentive to the elimination of restrictive practices and inflated labour costs. Apart from obvious objections on grounds of efficiency, inflated costs in the independent sector drag up the costs of the BBC which, because its income will be pegged to the RPI, may respond by reducing standards.

9. The replacement of the profits levy by a revenue levy would increase incentives for profit-making and, hence, for rooting out restrictive practices: it could increase Exchequer revenues substantially and would certainly provide the Exchequer with a more certain return. And it would help to curb the growing disparity between ITV and BBC income.

10. There is a risk that this package could lead to a reduction in standards with companies which had based their tenders on over-optimistic forecasts being forced to go down-market in an attempt to maximize their returns. As in the case of TV-AM, the IBA is unlikely to veto even a very radical modification of the original undertakings on programming if to do so would put the company out of business. There is some risk also that ITV companies would react adversely to the proposals by refusing in the period before the introduction of competitive tendering in 1993 to co-operate in securing greater use of independent producers. However, both these risks are inherent in any scheme which threatens the relatively entrenched position existing contractors presently enjoy. If the ITV companies proved to be intransigent about independent producers they could be brought into line by legislation (see item 3).

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11. I understand that the Chancellor of the Exchequer and the Trade and Industry Secretary are likely to support the Home Secretary's proposals. The Trade and Industry Secretary may also suggest that the Official Group's remit be extended to take in consideration of the contracting out of the transmission of ITV programmes (para 18 of the Report by the Official Group), on which the Chairman of the Official Group suggested that further work could be undertaken if Ministers so wished.

Channel 4

12. The Home Secretary proposes that power be taken for secondary legislation to require that Channel 4 be converted from a subsidiary of the IBA to a separate non-profit making broadcasting authority. He fears that, unless this is done, the IBA's role in the television market could become overdominant should its three DBS channels become established in the early 1990s.

13. He also proposes that if Channel 4 is thus separated then it should be required to finance itself by selling its own advertising. (He rejects the Peacock recommendation of simply giving Channel 4 the option on this point.) The advertising industry would welcome this as providing greater choice even though, as they are aware, it might well lead to increases in the cost of advertising on Channel 4.

14. There is a risk that requiring Channel 4 to finance itself through advertising could squeeze its revenue, forcing it to abandon its remit to provide a distinctive and innovative service. It is difficult to predict how likely this would be: much would depend on the state of the advertising industry at the time, Channel 4's performance, and the vigilance of the IBA in seeking to maintain standards. The Channel 4 Board (including the new chairman) are themselves opposed to any change in the status quo and this is the background to the Home Secretary's proposal that the Bill should provide a power to float off Channel 4, exercisable by secondary legislation. A decision on whether or not to implement it can take

account of the attitude of the Channel 4 Board at the time, the state of the market etc.

15. The Chancellor of the Exchequer and the Trade and Industry Secretary are both likely to welcome the Home Secretary's proposals. The latter may suggest that consideration would need to be given to the creation of a joint advertising authority to ensure that advertisers need concern themselves with only one regulatory body for television advertisements. If this idea commends itself to the group it could be remitted to the Official Group for consideration.

Networking

16. Production of programmes for screening throughout the ITV network is at present concentrated in the five largest companies. The Home Secretary proposes to invite the IBA to devise a better system with stated objectives, including that programmes for networking should first pass some competitive process of selection, that non-network ITV companies should be given access on equal terms and that independent producers should be given access in accordance with the already announced initiative. Members of the Group may wish to probe whether it is satisfactory to leave this to the IBA themselves or whether some form of independent inquiry would be more effective.

Advertising Practices

17. There is a long history of complaints by the advertising industry about unfair practices by the ITV companies. The Office of Fair Trading are now making inquiries into the market for advertising in the United Kingdom. The Home Secretary invited the Group to note that he and the Trade and Industry Secretary will keep the matter under review. Some members of the Group may wish to probe whether it is possible to respond more vigorously to the advertisers' complaints; but it might be difficult for the Government to take any initiative of its own, since this would risk appearing to undermine the position of the Office of Fair Trading.

HANDLING

18. You will wish to invite the HOME SECRETARY to introduce his paper. The discussion might then be divided as follows.

(i) Allocation of ITV Contracts and Levy Arrangements

Do the Group agree that the Official Group should be remitted to work up proposals for the allocation of ITV contracts by competitive tendering with annual payments based on advertising revenue? The CHANCELLOR OF THE EXCHEQUER and THE TRADE AND INDUSTRY SECRETARY will have comments.

(ii) Channel 4

Do the Group agree that the Official Group should work up proposals for legislation providing for the separation of Channel 4 from the IBA and self-financing through advertising? The TRADE AND INDUSTRY SECRETARY may wish to report the views of the advertising industry. The CHANCELLOR OF THE EXCHEQUER may have views. The LORD PRESIDENT may wish to comment given his responsibility for the legislation which established Channel 4.

(iii) Other Issues

(a) Networking

The TRADE AND INDUSTRY SECRETARY may wish to probe whether it is satisfactory to leave it to the IBA to come forward with proposals for improving the networking arrangements.

(b) Advertising

The TRADE AND INDUSTRY SECRETARY may wish to comment on the inquiry by the Office of Fair Trading. Other members may wish to probe whether the Government could respond more vigorously to the advertisers' complaints.

MINISTERIAL GROUP ON BROADCASTING SERVICES

20 JULY 1987

ITEM 1: PROPOSALS FOR BROADCASTING LEGISLATION: (MISC 128(87)4)

OBJECTIVES AND CONCLUSIONS OF THE MEETING

1. This paper is a broad overview of the main themes in the Government's broadcasting policy, and it runs over the main issues which the Home Secretary proposes to cover in the Broadcasting Bill which he hopes to bring forward in the 1988/89 Session. It will provide the opportunity for a "Second Reading Debate" on his proposed package, and for members of the Group to indicate whether it covers the right ground. However, you will probably wish to avoid detailed discussion of particular points on which members of the Group will not have been fully briefed. In particular, you will wish to prevent discussion under this item on subjects which come up later in the agenda.

2. The proposed shape of the Bill seems to be on the right lines and the Chancellor of the Exchequer and the Trade and Industry Secretary will be briefed to endorse it. You will wish to check whether there are any items which have been excluded; or whether there are any points which members of the Group wish to register at this stage.

3. The only matter on which the Home Secretary seeks a decision is that he should work up proposals for a White Paper for publication not later than the end of November. That timing may be optimistic, but the general idea of a White Paper seems right. You may wish to explore the degree of detail that the Home Secretary has in mind.

MAIN ISSUES

4. The paper begins by stating the general principle of encouraging competitiveness and response to the consumer, and the special considerations that qualify the application of the principle in the field of broadcasting. It then reviews the progress to date in combatting these obstacles by increasing access to the spectrum and extending direct payment by the consumer. It then reviews, in turn, the areas of radio, independent television, programme standards, and the BBC, outlining the contents of the Bill in each area.

5. Subject to the decisions to be taken under items 2 and 3, the only major point of broadcasting policy that will be outstanding after this meeting is the future of subscription payment which was the foundation for much of Peacock's argument. This cannot be taken much further until the consultation period on the Consultants' report runs out at the end of September, and the Home Secretary has assessed the results. It would clearly be the next major issue on which MISC 128 focuses. You may wish to tell the Home Secretary that you trust he will be able to bring forward his proposals on subscription to a meeting of the Group in October.

6. Some of the areas touched on in the paper (especially in paragraphs 3 and 13) interact with the work on the future communications infrastructure which is being overseen separately by the Sub-Committee on Telecommunications Policy (E(TP)) and its supporting Official Group (MISC 131). As announced by Ministers in April, a consultancy study has been commissioned from the PA consulting group, and a consultation paper has been issued by DTI. The consultants' final report is due in December, with an interim report in July. The Trade and Industry Secretary can report on this work. You may wish to probe with him and the Home Secretary how far it may be necessary to bring these matters into the scope of a Broadcasting Bill.

HANDLING

7. You will want to invite the HOME SECRETARY to introduce his paper. You may then like to invite the CHANCELLOR OF THE EXCHEQUER and the TRADE AND INDUSTRY SECRETARY to add their comments. Other members of the Group may also wish to comment.