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QUEEN ANNE'S GATE LONDON SW1H 9AT

10 April 1989

Dear David,

LOCAL SERVICES

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PR We undertook in the White Paper to announce our firm proposals for legislation on local services by the end of April. MISC 129 has reviewed the original White Paper proposals in the light of the comments made on them, and in its report to the Ministerial Group (MISC 128(89)1) it has recommended a number of modifications. I am writing now to seek the agreement of colleagues to those modified proposals, and to the terms of the ... attached draft announcement.

The modified proposals retain the main principle put forward in the White Paper - that there should be a flexible new technology-neutral framework for local services - but meet the main concerns expressed by the cable industry by allowing local operators to retail as well as deliver services, and by withdrawing the suggestion that they would be liable to levy. The industry will no doubt be disappointed that we have not been persuaded by their arguments against the allocation of franchises by competitive tender. I continue to believe, however, that some form of competitive tender will be the most objective method of allocating franchises, and will also reflect the fact that local franchises will in future carry with them valuable MVDS frequencies. But, as the draft announcement indicates, it would be sensible not to be too specific about the details of the competitive tender mechanism until we have had a chance to consider the comments made on our proposals for the allocation of Channel 3 and 5 licences.

There may also be some resistance from the cable industry to our proposal for the liberalisation of SMATV systems. I consider, however, that a substantial degree of liberalisation would be fully justified. The restrictive policy which the Cable Authority has hitherto adopted towards SMATV systems has been consistent with its statutory duty to promote broadband

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The Rt Hon Lord Young of Graffham
Secretary of State
Department of Trade and Industry

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cable. But, as the Authority has recognised, the advent of services from Astra has made this policy unsustainable, and I am glad that they are now consulting the industry with a view to loosening it up. The recommendations from MISC 129 would take this liberalisation one step further, in recognition of the fact that the ITC will not have a duty to promote cable. The revisions which the Authority is contemplating to its present policy should go some way towards meeting the concern expressed by SKY and others; and the recommendations from MISC 129 will give them ready access to the blocks of flats, which has been their main concern. I believe that the MISC 129 recommendations strike the right balance between the clear case for allowing SMATV the freedom to bring new satellite services to viewers as quickly as possible and the need not to fragment the market so much that LDO franchises would not be viable. We can keep the details of these proposals under review in the light of experience with the Cable Authority's proposed looser policy. In particular, I think that we will need to keep open minds about the exact rules on dish-sharing. MISC 129 has proposed that systems covering a single building or pairs of dwellings sharing a party wall should be covered by a class licence. While this recommendation draws the line in a logical place we may need to reconsider it if the Cable Authority decides on a more generous limit.

There are two points on which the draft announcement is silent at the moment: the frequencies which we propose to make available for MVDS; and the position on non-EC control of cable and local delivery franchises. I understand that you will be circulating proposals on the former within the next few days; our decision will clearly be an essential part of the announcement. As regards non-EC control, I proposed in my letter of 14 March that we should remove the present prohibition on non-EC control of cable franchises and not impose any similar prohibition on local delivery franchises. In your reply of 20 March you indicated your agreement. Ideally, I would like to include this in the local services announcement. However, as I said in my letter of 14 March, I would not wish to announce this in advance of a comprehensive announcement on ownership generally. I will be circulating a paper on this for discussion at MISC 128 on 20 April, and I hope that we can reach agreement then. If in the event we do not, I would propose to indicate in the announcement that we will be making the position on non-EC control clear as soon as possible in the context of a separate announcement on ownership.

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Although the proposals on local services raise intricate questions of policy, they are politically less important and difficult than many of the other issues which we shall need to review in MISC 128. I therefore very much hope that, particularly given the amount of preparatory work done by officials, colleagues will feel able to agree in correspondence to these proposals and to the terms of the draft announcement. If there are any points which colleagues feel need discussion, they can be taken at MISC 128 on 20 April. But I think that there would be strong advantages in settling these questions in advance of the meeting, thereby leaving it free for discussion of Channel 4 and ownership.

I am copying this letter to the Prime Minister, the Lord President (in view of the proposed Parliamentary announcement) other members of MISC 128 and to Sir Robin Butler.

Yours,

Douglas.

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DRAFT ARRANGED PQ ON LOCAL SERVICES

To ask the Secretary of State for the Home Department if he will make a statement about the proposals in the broadcasting White Paper on local services.

DRAFT REPLY

I am grateful to all those who responded to the invitation to comment on these radical proposals.

As the White Paper undertook, we have considered carefully all the views which have been expressed, and in the light of them we have decided to make some adjustments to our original proposals. I am placing in the library of the House a note which outlines the modified proposals which we intend to recommend to Parliament.

We continue to believe that there should be a new, flexible technology-neutral framework for local services, leaving operators free to decide upon the best mix of technologies. As the White Paper noted, this will in practice mean at present cable or MVDS, or a mixture of the two. The fact that we are proposing that local operators should in future have the choice to use technologies other than cable does not imply, as some commentators have suggested, that the Government does not foresee a prominent role for cable under the proposed new framework. The advantages of cable over other delivery technologies are well known; and we have been pleased to see that many recent applicants for cable franchises have plans to exploit these advantages in order to provide telecommunications as well as television services over their networks. The point of the freedom which we are proposing should be offered to

operators is to enable them to choose which delivery technology or combination of technologies to use, based on their commercial judgement of the nature of the services for which there will be a demand. The new framework will be designed to allow operators themselves to choose the level of service they wish to offer their customers. It is, however, important for all local delivery systems to meet certain standards relating not only to safety and interference, but also to performance and compatibility. The Government, after consulting all interested parties, will decide how best this may be achieved.

In line with the White Paper, we propose that the new framework should be based on fifteen year local franchises awarded by the new Independent Television Commission (ITC). Although we have considered carefully the contrary opinions which have been expressed, we hold to the view that some form of competitive tender mechanism will be the best method for allocating franchises. It will provide an objective method for choosing between applicants, and also takes account of the fact that successful applicants will be acquiring the exclusive right to use scarce MVDS frequencies. We will be giving further thought to the precise form of the competitive tender mechanism, taking account of the comments which we have received on the proposals on the allocation of licences for Channels 3 and 5.

We envisage that, initially at least, only one franchise is likely to be awarded for any given area. It will be open to the ITC to award a second franchise if it chooses to do so; but we are no longer proposing that it should be required, as the White Paper envisaged, to consider advertising a further franchise or franchises for an area a short time after awarding the initial franchise there.

The aspect of the White Paper proposals which has attracted most comment is the suggestion that local delivery operators should

not, except at the discretion of the ITC, be permitted to retail programme services. The objective of this proposal was to provide additional scope for competition in the retailing of programme services. While we still attach importance to this objective, we accept the argument put by many commentators that the White Paper proposal could inhibit investment in local delivery networks. We now therefore propose that local operators should be able to retail programme services without restriction, and without the need for permission from the ITC.

The Government does, however, see a case for injecting competition into the local delivery and retailing of services by loosening considerably the present restrictions on the development of Satellite Master Antenna Television (SMATV) systems. The Cable Authority's policy towards the licensing of SMATV systems, [which it is presently considering relaxing in certain respects] [a relaxation in which it has recently announced], has flowed from its statutory duty to exercise its licensing powers in such a way as to promote broadband cable systems. As the White Paper indicated, the ITC will not have such a duty. We therefore believe that the restrictions placed on SMATV hitherto could not be sustained under the new framework, and we are proposing a substantial, though not total, liberalisation of SMATV systems. Under these proposals systems covering single buildings or adjacent pairs of homes sharing a party wall will be automatically licensed by means of a class licence under the Telecommunications Act 1984. Systems larger than this but not covering more than 1,000 homes would be licensed under that Act provided that, in the case of an application for a system within a franchise area, the local delivery operator (or cable operator) had been given the right of first refusal. SMATV operators would not be granted telecommunications code powers, which would in practice make it difficult for them to build systems covering more than 1,000 homes. This size limit would in any case be applied flexibly.

These proposals will be subject to review in the light of experience with [any changes in its existing policy which the Cable Authority decides to make] [the modified policy which the Cable Authority has recently announced]. [Licensed SMATV operators would be able to carry any channels licensed by the ITC or originating from states signatory to either or both of the proposed Council of Europe Convention on Transfrontier Television or the EC Directive on Broadcasting (assuming they come into effect). A system carrying channels falling outside either of these categories would need to be licensed separately by the ITC.]

The White Paper proposed that local operators should be liable to levy while they retained a local monopoly. We have, however, been persuaded on balance that it would be sensible not to introduce a new levy on local services. Whereas the White Paper proposed that broadcasting levies should mainly be based on advertising revenue, revenue from locally sold advertising appears at present unlikely to become a major source of finance for local services. Furthermore, we acknowledge the risk perceived by some commentators that the liability to levy might deter investment in a young industry, and we believe that this outweighs the benefits to the public purse of the modest amount of revenue which a levy might have yielded.

[Frequencies to be made available for MVDS]

[Non-EC ownership - if wider announcement on ownership restrictions ready by end of April]

As foreshadowed in the White Paper, we propose that all cable operators awarded franchises before the date of its publication (7 November 1988) should have the right to opt to become technology-neutral delivery operators under the proposed new framework. We have decided to propose that this right should

also be extended to eventually successful applicants for franchises applications for which had to be submitted by that date. In both cases the right will apply only to franchise holders who have been awarded a licence by the Cable Authority before it ceases to exist. Under our proposals operators in this category will, if they so choose, be licensed as local delivery operators as of right by the ITC when it is set up. As such they will be entitled to use MVDS to deliver services to the home, subject to the availability of spectrum. It will be for the ITC to decide what frequencies can be made available to any operators who take this option. It may not always be possible for it to make available sufficient frequencies to cover an operator's entire franchise area. Cable operators who obtain their franchises after this cut-off date and who are awarded a licence by the Cable Authority will, under our proposals, retain their status as operators licensed under the Cable and Broadcasting Act 1984 for the remainder of the terms of their licences. The ITC will discharge in relation to such licences the duties now undertaken by the Cable Authority.

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GOVERNMENT PROPOSALS ON LOCAL SERVICES

Franchising procedure

1. It is envisaged that the Independent Television Commission (ITC) would award technology-neutral local delivery franchises by competitive tender. The Government will be giving further thought to the precise nature of the competitive tender mechanism. Before their bids could be considered applicants would first have to pass certain pre-qualification tests. These tests, the details of which would be determined by the ITC, would be designed to weed out applicants who did not appear to have the financial or managerial resources to make good use of their franchise, or whose plans were technically unsound.

2. A franchise would give a local delivery operator the right to use a specified block of frequencies for 15 years. The LDO would be free to use any delivery technology he wished (in practice, cable or MVDS, or a mixture of the two). He would have the right to retail services as well as deliver them (subject to the qualification about telecommunication services noted in paragraph 8 below).

3. An LDO who was using MVDS would need a licence under the Wireless Telegraphy Act 1949. One who was laying a cable network in all or part of his franchise area would need a licence under the Telecommunications Act 1984. The award of a franchise would carry with it an understanding that any licences awarded under the 1984 Act would if necessary give the licensee telecommunications code powers. Circumstances warranting the grant of such powers would be:

- a. where the LDO was planning to lay a system capable of carrying interactive services; and

- b. any other cases where there was a proven need for such powers (eg where a part of the franchise area could not be reached off-air, and where it would be impracticable to lay cable without code powers).

4. It is envisaged that LDOs would not have coverage obligations. The ITC would, however, have the discretion to revoke franchises where the LDO was not making reasonable progress towards carrying out the plans included in his application for the franchise. LDOs would be subject to take over, provided that the new owners did not fall foul of the ownership restrictions (see paragraph 6 below).

5. It would be open to the ITC to advertise a second franchise for an area at any time but it would not have a duty to consider doing so at any specific point.

Ownership rules

6. The ownership rules for LDOs would be as proposed in paragraphs 6.48-6.53 of the White Paper (save for the separation of delivery and retailing).

Television and radio services

7. LDOs would be free to deliver and retail television and radio services. They would not have editorial responsibility for the content of services originating in the UK (which would be licensed by the ITC in their own right) or for services originating from states signatory to either or both of the proposed European instruments (assuming that they come into effect). They would, however, have responsibility for the content of any services falling outside these categories; and it would be a condition of their ITC licence to ensure as far as possible that any services of this sort which they carried complied with the consumer protection requirements. To the extent that LDOs originated any services themselves (eg local

channels) those services would need to be separately licensed in their own right by the ITC (or the Radio Authority in the case of sound-only services), like any other UK-originated service.

Telecommunication services

8. It is proposed that LDOs would also be able to deliver and retail telecommunication services on the basis proposed in the White Paper (paragraph 6.38). In particular, they would be able to retail as well as deliver such services only if they made their system equally available to others.

Non-LDO delivery systems

9. Not all local delivery systems would be subject to the franchising procedure. The procedure would come into play if:

- a. the delivery operator wished to use spectrum; or
- b. even if he was planning to use cable only, his proposed system fell outside the class of systems which would be eligible for a SMATV licence from DTI (see paragraph 10 below).

It would be unlawful to run a local delivery system without having either a DTI SMATV licence or an LDO franchise.

10. It is proposed that SMATV licences would be issued by the DTI under the Telecommunications Act 1984 in the following circumstances:

- a. systems covering single buildings or adjacent semidetached houses or pairs of houses in a terrace would be licensed automatically under the terms of a class licence;

- b. in areas already franchised, or where a franchise was being advertised, the LDO (or the eventually successful applicant) would be given the right of first refusal whenever an application for a SMATV licence was made. If he was unable to provide a service within a reasonable timescale then a SMATV licence would be granted to the original applicant. If a SMATV operator were licensed then it would be open to him subsequently to enter into a commercial arrangement with the LDO (eg to sell his system to the LDO, or to come to a joint venture agreement) if he so chose. Although no rigid rules would be laid down the expectation would be that DTI would not licence systems covering more than 1,000 dwellings;
- c. in areas which were not franchises, and where a franchise was not being or about to be advertised, SMATV licences would be granted. Again there would be a flexible limit of 1,000 homes. If an LDO franchise was later awarded for an area covering the SMATV system it would be open to the SMATV operator to enter into a commercial arrangement with the LDO if he so chose.

DTI would not envisage granting SMATV operators telecommunications code powers.

11. SMATV systems are likely in general to carry only channels licensed by the ITC or originating from a state bound by either or both of the European instruments. A system carrying a channel falling outside either of these categories would need to be licensed separately by the ITC. Operating in these circumstances without a licence would be unlawful. It is envisaged that the ITC licence would simply be a licence designed to ensure that the consumer protection requirements were met; it could not be withheld or withdrawn to regulate access to the market.

12. These would continue to be a licensing regime for restricted services (except to the extent that they were merely relaying channels licensed in their own right by the ITC) in order to apply content controls. Again it is envisaged that the ITC would not have the discretion to withhold or withdraw a licence in order to regulate access to the market.

Transitional arrangements

13. It is proposed that any operators awarded franchises by the publication date of the White Paper (7 November 1988), and any eventually successful applicants for franchises applications for which had to be submitted by that date, will have the right to opt to become LDOs. This option would apply only to franchise holders actually awarded licences by the Cable Authority before it is wound up.

Home Office
April 1989

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