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Prime Minister

MISC 128: CHANNELS 3, 4 AND 5

I am grateful to you and colleagues for your comments on the draft announcement I circulated on 9 June.

... I now attach a final version of the announcement which includes all of the drafting changes that we have been able to accept. There are two points of substance in this final version. I have decided to include a reference to our decision that the Home Secretary should be given an exceptional power to veto the highest bid if the funding is from an undesirable political source. Although this may divert attention from some of the other issues, I think on reflection it would be better to announce it now rather than introduce it separately later on. Secondly, I have attempted to shorten the announcement by deleting paragraph 8 of the earlier draft which dealt with the number of Channel 3 licences for which any applicant might apply. This will be swept up in a Written Answer which I hope will also be given tomorrow.

I am copying this minute and the attachment to MISC 128 colleagues and to Sir Robin Butler.

Douglas Hurd.

12 June 1989

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Mr Office

COMPETITIVE TENDER AND CHANNEL 4 : DRAFT ANNOUNCEMENT

With permission, Mr Speaker, I would like to make a statement on the future of commercial television. I apologise for its length.

The White Paper proposed a two-stage procedure for awarding licences for Channels 3 and 5 under which applicants would have first to pass a quality threshold, consisting of positive programme and consumer protection requirements, and would then go on to offer financial tenders. The Independent Television Commission would be required to select the highest bidder.

Many of those who commented on the White Paper expressed concern that these proposals might lead to a loss of quality in programming. We recognise that concern and believe that a case has been made out for strengthening the quality threshold. We do not consider it would be right to do so by adding more detailed requirements in the legislation to supply specific types of programme. We therefore propose to strengthen the quality threshold by broadening the third positive requirement in paragraph 6.11 of the White Paper to read:

"to provide a reasonable proportion of programmes (in addition to news and current affairs) of high quality, and to provide a diverse programme service calculated to appeal to a wide variety of tastes and interests."

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It will be for applicants to interpret this combined quality and diversity test in drawing up their programme proposals. Those who fail to satisfy the ITC that they can meet this requirement will not have their financial bids considered.

A number of suggestions have been made to us about the form that the financial bid should take. The Chairman of the IBA proposed that it should comprise a sum fixed by the ITC and a bid by the applicant of a percentage of advertising revenue. I support this combination of elements but, in order to improve the transparency of the bidding process, propose that they should be reversed. Accordingly, the ITC will fix a percentage of net advertising or subscription revenue for each licence to form the minimum sale price. Applicants will then be required to bid a lump sum which they would pay if successful in addition. For successful applicants, both sums will be paid annually over the period of the licence to avoid the imposition of debt burdens on licensees.

Applicants will also be required to post a bond with their tender application. Successful bidders will be required to add to this an amount which, together with the first, will add up to a substantial performance bond. This requirement will

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strengthen the enforcement powers of the ITC. Those who fail to meet their programme promises given at the quality threshold stage will stand to lose a proportion of the bond.

We have considered carefully the arguments about the criteria on which the tenders should be decided. I do not believe that at the tender stage, before it is clear to whom the licences will be awarded and before the nature of any network arrangement is known, it will be possible for the ITC to make fine distinctions between the quality of programme service offered by different applicants, all of whom will have passed the strengthened quality hurdle I have announced today. We must avoid a return to the opaque and sometimes arbitrary selection procedures of the past. But some flexibility needs to be written into the procedure. We propose therefore that the ITC should be required in the normal course to accept the highest bid, but that it should have a power in exceptional circumstances to select a lower bid. This power would operate only in exceptional circumstances and the ITC would be required to give its full reasons. Exercise of the power would be subject to judicial review. In addition, there would be an exceptional power by the Home Secretary acting on the recommendation of the ITC, to veto the selection of the highest bid if its funding came from a politically undesirable source.

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The White Paper proposed that in addition to the sum bid at tender applicants would have to make a levy payment to the Exchequer. The proposals I have just announced for the fixing of a proportion of advertising or subscription revenue as part of the tender price overtake our original proposals for a levy. Successful candidates will have only to pay the two-part tender price I have outlined. There will be no levy in addition.

There has been some speculation as to whether the Government would impose a moratorium on takeovers at the beginning of 1993 and whether it would insist on compulsory networking for Channel 3. The Government's view on both issues has not changed since the publication of the White Paper. I understand that the Chairman of the IBA intends to permit takeovers in the period up to 1993, subject to the normal anti-monopoly rules and bearing in mind our proposals for the regime after 1992. It would not in the circumstances be either sensible or necessary to impose a moratorium thereafter. Networking will be a matter for the Channel 3 companies themselves to decide without Government compulsion. Basic fair trading laws should ensure that no companies are excluded unfairly from any networking arrangements. We shall consider whether any further provisions are needed in the legislation to regulate the operation of any new network system in the interests of free access and fair competition.

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We have received a number of representations on behalf of the four million viewers who are deaf or hard of hearing. We agree that particular provision should be made for them. We have therefore decided that 3 and Channel 5 licensees should be required to provide teletext sub-titling for some of the programmes in their schedules.

The White Paper proposed that Channel 5 should be shared between at least two licensees. In the light of the start-up costs of the new Channel and the competition it will face from the established terrestrial channels, we have now decided that Channel 5 should form a single licence. It will thus be better equipped to compete with the existing terrestrial channels.

Similarly, the White Paper proposed that there should be a separate night hours licence for Channel 3. Many of those who responded to the White Paper expressed doubts about the financial viability of a separate night hours licence. We have accordingly looked at this again. We want to ensure so far as possible that the night hours are fully used. I accept the argument that they may be better exploited commercially if they are linked with services provided at a more commercially attractive part of the broadcasting day. We have therefore decided not to disturb the

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present situation under which the night hours may remain connected with the peak viewing period. This position will be reviewed if the night hours are not being fully exploited. Under our proposals, the ITC will be free to allocate licences for other times of the day, such as a breakfast time service.

The White Paper proposed that the ITC would be responsible for the geographical division of Channel 3 into regions. This has been generally welcomed. The Government has noted with understanding the statement of the Chairman-designate of the ITC, Mr George Russell, that he would see advantage in retaining the existing regions, if possible.

I turn to Channel 4. The White Paper made clear the Government's intention to maintain the remit of Channel 4 while at the same time providing for the selling of its advertising separately from that on Channel 3. The White Paper proposed three options ranging from a fully independent commercial service licensed by the ITC, through an option linking Channel 4 with the new Channel 5, to an arrangement whereby Channel 4 would continue as a subsidiary of the ITC with a possible minimum guaranteed income.

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We have considered the comments we have received on these options and in particular the helpful Report by the Home Affairs Select Committee. I have written today to the Chairman of the Committee expressing the Government's gratitude for its work on Channel 4 and setting out the Government's decisions. A copy of that letter has been placed in the Library of the House.

In considering the various options, the Government has decided that it would not be feasible at the present time for Channel 4 to become an independent commercial company competing with the other broadcasters if, as we think essential, it is to retain its remit. The financial outlook for Channel 4 remains uncertain with the prospect of new competition. We believe that the requirement in addition to provide a return for shareholders in a private company could put too much pressure upon Channel 4 finances and place its remit in serious jeopardy. But we see some difficulty in Channel 4 continuing to be owned by the authority who would be responsible for regulating its output; and we believe that any financial underpinning given to the Channel should be carefully circumscribed to provide clear incentives for cost-efficiency.

We have therefore decided that after 1993 Channel 4 should become a public trust, which would be licensed by the ITC, and

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would continue to provide the service set out in the special remit. Channel 4 would sell its own advertising, and would be subject to a baseline budget of 14% per annum of terrestrial net advertising revenue. The baseline could be amended in secondary legislation. If the Channel's revenue fell below the baseline, the difference would be funded by the ITC to a maximum of 2% of terrestrial net advertising revenue levied on the Channel 3 companies. Any surplus revenues above the baseline would be shared equally between Channel 3 and Channel 4. The Trust would be required to hold their share of any surplus revenues to be used as a first call in the event of deficits in later years. To reduce the need for a call on the guarantee, the ITC would be empowered to require cross-announcement of programmes between Channel 3 and Channel 4. Complementary scheduling would be possible, but would not be a requirement. The Channel 4 licence would run for ten years, but these arrangements would be reviewed after seven. I believe this is a satisfactory way of securing the future of Channel 4 with its present remit.

The White Paper concluded that the arrangements for the Welsh Fourth Channel should remain unchanged. Some have argued that it would not be consistent with the new and more free approach to regulation for the Channel to be funded by a direct

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subscription on the commercial companies. The situation is particularly anomalous in Scotland where the ITV companies are required to finance Welsh programmes as a first call on their resources before even they make provision for their own Gaelic speakers. The Government is sympathetic to these concerns, and has decided to make a small change to the funding arrangements for S4C. Henceforth, S4C revenues will not be charged as a first call on the commercial companies but will be funded out of the proceeds of the tender through the ITC.

My statement today covers most of the major decisions on the future commercial television system following the publication of the White Paper. We shall make announcements on the remaining issues before long. These decisions will be incorporated in new broadcasting legislation which the Government hopes to bring forward in due course.

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