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PRIME MINISTER

DTI have come down against allowing BT and IBM to undertake a joint venture to provide Value Added Network Services (e.g. ticketing for airlines, point of sale billing for retailing).

Put crudely, BT would have made more money and more would have been raised from privatisation if it had gone in with IBM. But DTI, rightly in my view, have given priority to the competition arrangements - and buttressed the authority of the Director of OFTEL in so doing.

I understand the Chancellor, though irritated at the lack of consultation, is prepared to go along with DTI.

Agree DTI proposals?

AT

Yes not

12 October 1984

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MRT AEG

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10 DOWNING STREET

From the Private Secretary

15 October 1984

Proposal from BT and IBM for a Joint Venture to Provide
Managed Data Network Services

The Prime Minister has seen Mr. Pattie's minute of 12 October. She is content with his proposal to turn down the application from BT and IBM for a joint venture to provide managed data network services.

I am copying this letter to Len Appleyard (Foreign and Commonwealth Office), David Peretz (HM Treasury) and Richard Hatfield (Cabinet Office).

Andrew Turnbull

Neil McMillan Esq
Department of Trade and Industry.

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PRIME MINISTER

PROPOSAL FROM BT AND IBM FOR A JOINT VENTURE TO PROVIDE
MANAGED DATA NETWORK SERVICES

I am writing on Norman Tebbit's behalf to let you know of how he had intended to deal with the difficult problem of the proposal from BT and IBM for a joint venture to provide managed data network services, which would require a licence from us.

2 The Secretary of State has a statutory duty to license services for which there is a demand. In practice, having satisfied ourselves that this demand exists, we have only two options: either to license the joint venture, on conditions which would attempt to provide safeguards against some of the risks associated with it; or to license IBM and BT separately. There is an attraction in agreeing to license the joint venture, as a means of rapidly providing services which are in demand. IBM and BT have suggested that arrangements could be devised to ensure that the

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venture would operate at arms length from both its parents, in such a way as to secure effective competition between the joint venture and BT's other services. But there is clearly a risk that the joint venture, based on two such dominant companies, would swiftly achieve a pre-eminent position in the market. If that were to happen, others would be deterred from entering the market place. I would regard this as unhealthy. This is not only my view: it is also the clear view of the newly appointed Director General of Telecommunications. I believe that it would be damaging if, on a subject of such importance and at such an early stage of his work, I were to run counter to his views. I have also formally sought the views of interested parties. These are now in, and show, as well as considerable demand for a joint service of this type, a clear balance against licensing the joint venture.

3 For these reasons, and despite the strong arguments advanced by IBM and BT, we have decided against licensing the joint venture. In my view it is better to ensure the early provision of services by licensing IBM and BT separately to provide services in competition with each other. I intend to make clear my willingness to license other suitably qualified entrants to this particular market, whenever they come forward.

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4 Competition should, in current market circumstances, be paramount in our considerations. The licensing of the joint venture would inevitably be reviewed as inconsistent with our competition policy in telecommunications and could be seen to have been governed by other considerations to do with the BT flotation.

5 In coming to our decision, we have also been influenced by the undoubted fact that to grant a licence to the joint venture would, whatever the conditions imposed therein, hinder rather than advance our drive to establish internationally agreed OSI standards. To safeguard the development of these I shall require each licensee - including IBM and BT - to provide connections to those users who have adopted Open System Interconnect (OSI) standards. This obligation will be a developing one, moving in line with the process of international agreement on standards, which still has some way to go before the full range of services can be provided to agreed specification. This is consistent with our initiatives taken earlier this year to advance the cause of agreed IT standards in Europe, particularly in relation to OSI and will be welcomed by the Commission, on whose behalf Commissioner Davignon wrote to Norman expressing his concern that we should not come to a decision to support a joint venture based on non-OSI standards.

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6 We recognize, of course, that refusal to agree to the joint venture will be considered a blow by both IBM and BT, and must have some adverse effect on the public perception of BT's prospects. We believe that any damage so caused to the flotation is containable. We intend to take care to explain that joint ventures between BT and others, particularly as circumstances change, are not ruled out as a matter of principle, but that the Government's policy of encouraging competition in this and other telecommunication markets must take priority in this case over other considerations. BT will be free to enter the market for managed data network services, despite a substantial body of opinion that BT should be excluded from it altogether. I have no doubt that Sir George Jefferson will not like this decision, but I hope to persuade him that it is contrary to both our interests to exaggerate its effect. Rather we should concentrate on expressions of confidence that BT, by themselves, will be able to do well in this market place. Incidentally, it will come as no surprise to potential American investors that a joint venture between IBM and BT is not to be permitted. There would be no question of licensing such a combination of market power in the United States.



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7 It is very important that we make an early announcement on this subject, well in advance of the BT flotation. I therefore propose to see Sir George Jefferson and Sir Eddie Nixon on Monday morning to explain the decision to them personally, and to issue the attached press statement later on the same day. There is intense speculation at the moment as to what our decision is; and I have no doubt that both IBM and BT and the press will be probing further over the weekend. I shall be grateful if the most stringent steps could therefore be taken to safeguard the confidentiality of this decision until I make it public.

8 I am copying this minute to Geoffrey Howe, Nigel Lawson and Sir Robert Armstrong.

A handwritten signature in blue ink, appearing to be 'G. Pattie', written over a horizontal line.

GEOFFREY PATTIE

12 October 1984

Department of Trade and Industry

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PRESS STATEMENT

GOVERNMENT'S POLICY TOWARDS VALUE ADDED TELECOMMUNICATION
SERVICES

The following is the text of a Statement issued by the
Department of Trade and Industry on Monday 15 October:

The Secretary of State has considered the licensing of value added telecommunication services in the light of the new licensing provisions in the Telecommunications Act and the proposal by British Telecommunications plc and IBM (UK) Ltd to provide managed data network services through a joint venture.

The Government wish to encourage the exploitation of the opportunities created by the convergence of telecommunications and computer technology for the provision of new value added telecommunication services. Proposals by BT, IBM and others suggest that there is a large potential demand in the UK for such services. The Government intend that this demand should be met and that users should be provided with a variety of good quality services. The Government believe that this can best be secured by promoting competition between providers and that competition will be advanced by use of the emerging Open Systems Interconnect standards.

The Government wish to ensure that British Telecommunications can compete fully and effectively - and in appropriate circumstances in partnership with others - in the market for new services. The Government would also see advantage in the participation in this market place of companies with



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overseas parents.

Managed data network services involve the conveyance of messages on behalf of third parties over circuits provided by public telecommunications operators and the addition of value by for example the provision of network management facilities, security services and traffic analysis. The provision of such services to others is not authorised under the existing British Telecom and proposed Mercury public telecommunications operator licences. These limit BT and Mercury to providing the basic telecommunication service of conveying messages from point to point without adding value. Nor is the provision of such services authorised under the General Licence for Value Added Network Services, which limits VANS providers to services which involve the storage, processing or multi-addressing of telecommunication messages. It will therefore be necessary to grant special licences under section 7 of the Telecommunications Act to those wishing to provide managed data network services.

The BT and IBM proposal, which envisaged the provision of such services through a jointly owned company, has been the subject of a recent consultation exercise initiated by the Secretary of State for Trade and Industry on 31 July. He has considered the many views expressed, including in particular the advice of the Director General of Telecommunications. Many potential users expressed support for the early introduction of services such as the joint venture would provide. Others expressed the view that the proposed joint venture would be inconsistent with the objective of introducing competition into telecommunications. It would combine the efforts of the two major potential market entrants who would otherwise be expected to enter the market separately to provide competing services. It also appears likely from the consultation exercise that a joint venture



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at the present stage of development of this market by two such powerful companies would be a significant deterrent to market entry by others.

In the circumstances the Secretary of State has decided that he should not license the proposed joint venture but that it would be in the public interest to license BT and IBM separately since this would create the conditions for the widespread provision of an increased variety of services. The Secretary of State is also willing, in accordance with the statement made by the then Minister for Information Technology (Mr Kenneth Baker) on 20 July 1984, to give favourable consideration to applications for special licences by other companies which wish to provide managed data network services of a similar kind.

Before licensing applicants the Government will wish establish that they have the technical and financial resources to install and operate the systems necessary to provide such services and that they will not damage the national networks. It will be a condition of such licences that within specified periods after the publication of OSI standards each licensee, including BT and IBM, should secure the provision of facilities that enable his customers to communicate with users of apparatus operating according to those OSI standards. However, licensees will be free from the outset to provide services using proprietary standards.

The Department will shortly be consulting interested parties about the modifications to the existing VANS General Licence required by the new legislation. The new licence will ensure that independent companies are authorised to provide VANS using the managed data network services provided by BT, IBM, and others.

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NB/M AT 11/10
Letter expected from N Tebbit
12/10.

MR TURNBULL

10 October 1984

BT/IBM JOINT VENTURE - VANS

The DTI have concluded their consultations on the BT/IBM joint venture to provide nationally connected value added network services (VANS). Norman Tebbit is expected to announce his decision this week.

VANS permit computer users to be interconnected and to access common databases - for example airline ticket booking systems. They represent the infrastructure on which the IT revolution will be built.

IBM has several years lead in this field and the fear is that by licencing the BT/IBM joint venture it will cut out competition for VANS but more importantly make it much harder for competitors to sell the computers and terminals that will be connected to the VANS.

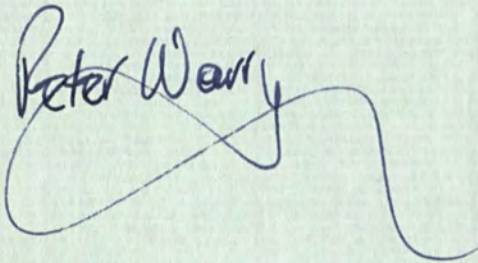
BT/IBM could be given a license under terms that force them to ensure there is no cost penalty to connecting competitors equipment: but this will be difficult to police and even harder to enforce. Alternatively the license could be refused hoping IBM and perhaps BT will develop their own competitive systems and ICL catch up.

OFTEL have informally advised against: we believe the arguments are finely balanced but that if we are serious about IT we should take the bold step now and support the joint venture. Competitors could help in framing a very tight license.

The decision needs to be taken before the release of the draft BT sale prospectus scheduled for 26 October. The joint venture could boost the price by £30 million.

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The Prime Minister may wish to discuss this with Norman Tebbit before he announces his decision this week.

A handwritten signature in blue ink that reads "Peter Warry". The signature is fluid and cursive, with a long, sweeping underline that extends to the right.

PETER WARRY