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6 February 1990

John,

NBA
to his desk.
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BROADCASTING BILL: PERFORMANCE BONDS

Discussions which the IBA and my officials have had with a number of financial institutions suggest that it will be necessary to modify somewhat the provisions in the Bill on performance bonds. This letter invites you and other colleagues to agree to our introducing appropriate amendments in Committee.

As the Bill is currently drafted, Channel 3 licensees would be required to post a bond (a) as a guarantee that any fines imposed by the ITC for failure to live up to programme promises would be met; and (b) as a sum to be forfeited in the event that the licence is revoked before the end of the licence term. The value of the bond would be set by the ITC at a sum not less than the minimum licence price, and the bond would have to be valid for the whole 10 year term of the licence. Where the bond was called in, in whole or in part, the proceeds would be passed by the ITC to the Consolidated Fund.

The banks and insurance companies who have commented on these proposals have indicated that they would not be prepared to provide bonds of this kind on the basis envisaged. There are three main problems:

- (a) they see bonds as a means of indemnity, compensating those who have suffered a specific loss, not as providing windfall gains to the Treasury;
- (b) they would not regard it as appropriate for a bond to back fines for failure to maintain quality standards in view of the subjective and unpredictable nature of the judgments involved;
- (c) they would have difficulty in contemplating issuing a bond for as long as 10 years.

These objections are in no way fatal to the concept of a performance bond, to which I continue to attach great importance as a means of safeguarding quality in commercial television. But they do, I think, mean that we shall have to adjust the way in which the bond will operate. My proposals are as follows.

The Rt Hon John Major, MP.
Chancellor of the Exchequer
Treasury Chambers
Parliament Street

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First, the performance bond should no longer be used to underwrite any fines imposed by the ITC. Instead, fines for failure to live up to performance promises would be treated in exactly the same way as fines imposed by the ITC for other reasons, and would be recoverable as civil debts.

This should in any case be a more effective way of treating the performance-related fine, since it would fall directly on the licensee, rather than being met as we originally envisaged through a form of insurance arrangement.

It follows that the bond itself would, on this approach, only come into play in the event of the licence being revoked, either because the licensee had ceased to broadcast or because the ITC had terminated the licence as a result of continuing poor performance. In this situation the bond would be used to indemnify:

- (a) the ITC for costs incurred in connection with their decision to revoke the licence and in arranging a temporary service for the vacant area until the franchise could be re-awarded;
- (b) the Treasury for loss of tender revenue during the period between revocation of the licence and award of the new licence (in practice between six and twelve months).

Any surplus proceeds from the bond, beyond those necessary to meet the expenses at (a) and (b) above, would be returned to the displaced licensee.

My third proposal relates to the duration of the bond. It appears that licensees are unlikely to be able to obtain a bond for an initial period of more than three years. Financial institutions would, however, be prepared to operate an evergreen facility, whereby each year they would roll the bond forward for a further year. We must make clear that such an arrangement would be acceptable, and the bonding requirement should therefore simply be that at all times during the currency of the licence the licensee was covered by a valid bond.

Finally, I see some advantage in changing the basis of calculation of the value of the bond. Rather than leaving this effectively to the discretion of the ITC by linking it to the minimum licence price (which they will themselves set), I think it would be better to fix the level of the bond at 7% of annual turnover, or £2 million, whichever is greater. Given that bonds will need to be reissued during the currency of the licence, I propose that the ITC should be able to revalue the bond at regular intervals on the



basis of 7% of the latest year's turnover at the time of revaluation. I estimate that the 7% figure would normally meet in full the proposed calls on the bond mentioned above. Where this was not the case, however, I think that the first call on the proceeds of the bond should be to enable the ITC to arrange for the substitute regional service and thereby in effect compensate the viewers directly affected by the failure of the licensee.

These proposals seem to me to retain the essential features of the performance bond within a framework which will be acceptable to potential bond providers. It is obviously in everyone's interest to create a bonding requirement of a kind which the mainstream financial institutions will readily embrace, since otherwise the cost of bonds - if obtainable at all - would be prohibitively expensive and licensees may be driven to use less reputable and experienced sources of cover. I hope, therefore, that you and other colleagues will be able to agree that we should amend the relevant provisions of the Bill in the way I have indicated. (Although this letter is couched in terms of licences for Channel 3, similar considerations apply to the bonding requirements for Channel 5 and national commercial radio).

It would be desirable for us to get the necessary amendments down as quickly as possible, since the first relevant clause of the Bill (clause 18) could be reached in Committee next week. I should therefore be grateful for a reply by 12 February.

I am copying this letter to the Prime Minister, MISC 128 colleagues and Sir Robin Butler.

