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P.0792

PRIME MINISTER

Liberalisation of Telecommunications

(E(TP)(82)5)

BACKGROUND

At its previous meeting, on 22 April, E(TP) discussed future telecommunications policy and in particular the Secretary of State for Industry's proposal that British Telecommunications (BT) should be privatised. The Sub-Committee concluded that, whatever the attractions of privatisation, the Government's most important aim for telecommunications must be to increase competition and efficiency. You asked whether, in addition to the Government's existing plans to liberalise telecommunications, there was scope for further substantial measures to increase competition without privatising BT.

2. In E(TP)(82)5 the Secretary of State for Industry argues that the Government's policies on liberalisation are correct, although he identifies a number of detailed legislative changes which would make it easier for the Government in due course to insist on liberalisation against opposition from BT, should this become necessary.

3. You will be aware from your meeting on Friday 25 June that if Ministers were to press further and faster on liberalisation than the Secretary of State for Industry envisages, for example in relation to additional alternative networks, there would be some important security implications.

MAIN ISSUES

4. You will want the Sub-Committee to consider whether it agrees with the Secretary of State for Industry's judgement that present policies are broadly satisfactory subject to the various detailed legislative changes which he proposes.

5. In three areas, the paper describes existing policies and what is being done to implement them (ie alternative networks, network services, and apparatus). It

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then goes on to identify four areas where more might be done (interconnect, resale, international, and the prime instrument and PABX maintenance) and explains the constraints affecting further progress. Each of these items is discussed below in turn.

Alternative networks

6. Present policy is to make Mercury an effective competitor to BT. To go further and permit other competing networks might make the return on the heavy investment involved in setting up a new network unattractive and, perversely, safeguard BT's monopoly.

Network services

7. The Secretary of State for Industry licenses operators. But BT have a statutory right to be consulted about licence applications; potential competitors may be put off by the fear that BT will learn their commercial secrets. The Secretary of State for Industry plans to introduce a general licence which would avoid BT's being involved in individual applications. This is an important and valuable step in exposing BT to more competition in the business sector of the market. You may therefore wish to ask the Secretary of State for Industry when the general licence will be in force.

Apparatus

8. New arrangements for approving apparatus, based on a new British Approvals Board for Telecommunications, will start to come into effect in July. The Department of Industry are trying to liberalise before then the supply of some pieces of equipment which BT have already approved and used.

9. It is not clear from the Secretary of State's memorandum how long it will take for the new approvals machinery completely to replace the present arrangements under which BT approves equipment and is able to inhibit competition by preventing manufacturers from supplying it other than to the Corporation. If there is to be a fairly long transitional period then it would seem to be important to keep up the pressure on BT to "release" items of equipment it has

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approved: the Secretary of State records that Mr Baker has written to Sir George Jefferson to this end.

Interconnect

10. The Secretary of State for Industry wants to have interconnection between BT and Mercury. This would mean that Mercury customers would be able to dial over Mercury circuits and link up with any BT subscribers, and that BT subscribers would be able to do the reverse. This is most important for the commercial future of Mercury. The policy at present is to leave this to negotiation between BT and Mercury; in the last resort the Secretary of State has no powers to direct BT to provide interconnect with Mercury. It is clearly desirable that, whether or not BT is privatised, BT's freedom to deny interconnection to Mercury on reasonable grounds should be removed. The CPRS paper, E(TP(82)9, strongly supports this.

Resale

11. Permitting the resale of capacity on lines leased from BT would ultimately be a very radical means of providing more competition. In effect spare capacity on the tie-lines of major companies could be used to provide the customer with several alternative telephone services. The Secretary of State for Industry is however disposed to move gradually. Rapid liberalisation of resale could undermine the viability of Mercury before it has become established. It might also force down BT's tariffs for business customers so far that the impact on tariffs for domestic customers would be undesirable; this latter effect cannot be assessed properly until BT has better management accounts. The Secretary of State for Industry therefore intends to take powers to require BT to permit resale but not to force resale until Mercury has become established and there is a better basis for assessing the impact on domestic customers. It seems unlikely therefore that significant resale would occur until the late 1980s.

International

12. Mercury has at present been allowed an international outlet on a restricted basis - the provision of international tie-lines but not international switched services. The Secretary of State hopes to permit Mercury to provide



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an international switched service in due course and he is also exploring whether the operators of network services referred to in para 7 above might be able to use BT's international circuits. At present however he merely proposes a study with options for consideration by Ministers at the end of this year.

Prime instrument and PABX maintenance

13. The main area in which there would be scope for further liberalisation of apparatus is the prime instrument (ie the first telephone attached to each direct exchange line; for most domestic customers this is the only apparatus they have) and PABX maintenance. There are at present no plans to remove BT's monopoly of supply of the prime instrument, or of PABX maintenance. The arguments against liberalisation are the maintenance of good customer service, protection of domestic supplies, and national security. The CPRS paper E(TP)(82)9 argues for keeping liberalisation of the prime instrument under review.

General assessment

14. The policy set out in E(TP)(82)5 was thoroughly examined by the Official Committee on Telecommunications Policy. In general the Committee endorsed the view that the first priority is to put Mercury on a viable basis as an alternative network. Speedy action should also be taken to bring into force a general licence for network services and to get the new system for approving apparatus into smooth and effective operation. On the four areas where more could be done the Committee:

- i. was keen that BT should not be allowed to drag its feet over providing interconnect facilities to Mercury; unless progress is achieved quickly the intention to legislate should be made known;
- ii. accepted the arguments about a gradual approach to resale but there was a feeling among some members that the pace might be somewhat more adventurous than the Secretary of State seemed to have in mind; this will need to be kept under review;
- iii. accepted that the issues about international services needed to be examined but hoped that the study available at the end of this year would provide a way forward; this again will need to be watched to ensure adequate progress towards liberalisation;



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iv. was sceptical that liberalisation of the prime instrument and PABX maintenance would in fact be detrimental to consumers and UK suppliers of apparatus but accepted that there might be other reasons (ie national security grounds) for going no further at present.

In general therefore the feeling was that the policy was broadly right; the main need was to keep up the pressure in implementing it, so that maximum feasible liberalisation was achieved within the constraints (including national security constraints).

HANDLING

15. You will wish to invite the Secretary of State for Industry to introduce his memorandum and then seek comments related to the main policy points listed in para 17(a) to (c) of E(TP)(82)5. Mr Sparrow may wish to comment.

CONCLUSIONS

16. You will want to reach conclusions on the following main questions:

- a. Does the Sub-Committee agree that the Government's present policy on liberalisation, as described in E(TP)(82)5, is correct; or are there any modifications which should be made or which the Secretary of State for Industry should be invited to consider further?
- b. Does the Sub-Committee agree that there should be legislation in the next Session of Parliament to remove the particular barriers to liberalisation mentioned in E(TP)(82)5?

Pg

P L GREGSON

28 June 1982



10 DOWNING STREET

Prime Minister

You were very disappointed by
Patrick Jenkin's BT liberalisation
paper, and wanted to consult some
friends in the industry before next
Thursday's E(TP).

When you see this interuption
paper I think you will see why
Patrick Jenkin's paper is as it is.
It is essentially a compromise between
what he would like to do and what
these considerations point to him doing.

Do you still wish to see friends
TOVER

in the industry & before the
E(TP) meeting?

Please also see the attached
note by John Verker which - without
taking account of ~~the~~ interception
points - suggests that the Do I
paper goes quite a long way in
the right direction.

MCS 16/6

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~~MR. SCHOLAR~~

Prime Minister
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Liberalisation of Telecommunications

We had a word about the Prime Minister's reaction to the Department of Industry's paper for E(TP) on the scope for further liberalisation of telecommunications, and I have discussed it further with Peter Gregson. Since the Policy Unit was in the van of those urging further liberalisation at the first meeting of E(TP), it may be helpful if I offer now some brief comments on this paper.

The issues were thoroughly worked over in the official group under Peter Gregson's chairmanship, and the CPRS was given - and took - every opportunity to press for specific further liberalisation measures. The outcome is a paper which to my mind does not do justice in its presentation to its actual content. Peter Gregson chose to let DoI write it, and it therefore seems needlessly defensive. But the same material could have been presented as a paper by the official group, which I think would have concluded that the DoI had now agreed to take what further measures were available and had identified where going further still would have involved reversing previous decisions or taking additional legislative powers. I am satisfied that the area of possible controversy is now narrowed to issues of the pace of liberalisation, or very marginal measures.

The Prime Minister will recall that at the first meeting of E(TP) three main areas of potential liberalisation were identified:

(i) Alternative networks.

Officials are agreed that the day may well come for the licensing of rivals to Mercury; but the first objective must be to get Mercury off the ground, and it will be several years

/before

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before we can safely license a further full network. To do so now would probably run counter to liberalisation, because the rival newcomers would destroy each other, leaving BT with a complete monopoly.

(ii) Apparatus.

I believe you have separate advice for the Prime Minister explaining the national security reasons for proceeding cautiously over the liberalisation of the prime instrument market, which is the main piece of apparatus left. DoI would also argue that BT's monopoly of the prime instrument is a major element in its profits, and will therefore make privatisation more attractive: it is an open question whether, security considerations apart, that would outweigh the need for competition.

(iii) Network services.

The Prime Minister should know that the present liberalisation policy for network services will provide quite extensive competition over a wide range of services. Together with resale and inter-connect, which are under negotiation, they will provide some degree of competition in telecoms as a whole.

I do not wish to exaggerate the significance of all these measures. However fast we go, BT is always likely to retain some 95 per cent of the market up to the mid-1980s, just as in the United States AT & T and GTE still dominate 95 per cent of the market after 13 years of liberalisation. But I believe that DoI have taken the message of the first meeting of E(TP) to heart. Their Ministers wrote immediately to BT asking them to behave less restrictively over the supply of attachments by rivals; and the Department has arranged a full scale seminar to discuss all aspects of liberalisation - the Prime Minister may care to see the programme, attached.

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I think the CPRS would take a similar view, while continuing to press for improvements at the margin. They made four specific proposals in the official discussions; two - a statement of intent to liberalise prime instruments, and licensing further operators - ^{are} covered above; one - concerning regulation of common carrier frequency - turned out not to be an issue because the Government do it already; and the remaining one - denying BT access to commercially confidential information - will be covered by the proposed new licensing arrangements.

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v.

J. M. M. VEREKER

15 June, 1982

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Telecommunications industry seminar, July 13 1982 : proposed programme

Telecommunications in transition :
from the Act to the Actuality.

9.00 a.m. for a 9.30 a.m. start.

Early morning session : legislative progress one year on.

9.30 a.m. Chairman's opening address : Government's concern to push ahead with implementation of the BT Act. John Butcher MP. Parliamentary Under-Secretary of State for Industry.

9.40 a.m. Ministerial address : the BT Act : a turning point. The Rt. Hon. Patrick Jenkin MP. Parliamentary Secretary of State for Industry.

9.50 a.m. British Telecom's point of view. Sir George Jefferson, Chairman, British Telecom

10.00 a.m. Questions/discussion.

10.10 a.m. The unions' viewpoint. B. C. Stanley, Esq. General Secretary Post Office Engineering Union

10.20 a.m. The private sector's viewpoint. S. C. Finch, Esq. Senior Regulatory Affairs Advisor, British Petroleum

10.30 a.m. Questions/discussion.

10.40 a.m. Coffee

Mid-morning session : the supply industry's progress.

11.00 a.m. Extension telephones : taking advantage of the pre-liberalisation initiative. To be confirmed.

11.10 a.m. Extension telephones : the approvals procedure is hindering market development. M. E. Percival, Esq. Managing Director, Conversation Pieces Ltd. Chairman, ITSA

11.20 a.m. Questions/discussion.

- 11.30 a.m. Key systems : gearing up for massive market growth. C. C. W. Box-Grainger, Esq.
Marketing Director
Telephone Rentals Ltd.
- 11.40 a.m. Key systems : a legislative minefield favouring entrenched positions. J. R. Harrold, Esq. Chairman,
Shipton Communications Ltd.
- 11.50 a.m. Questions/discussion.
- 12.00 noon Data transmission : liberalisation is in everyone's best interests. E. B. Stuttard, Esq. Technical
Director, Racal Milgo Ltd.
- 12.10 p.m. Data transmission : why can't the bureaucrats let us get on with it? To be confirmed.
- 12.20 p.m. Questions/discussion.
- 12.30 p.m. Telex : the opportunities. C. K. Rushton, Esq. Managing Director,
Transtel Communications Ltd.
- 12.40 p.m. Teletex : new equipment in a new environment. P. Breen, Esq. Chief Executive,
ITT Business Systems (UK) Ltd.
- 12.50 p.m. Questions/discussion.
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- 13.00 p.m. Lunch
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- Early afternoon session : progress on networks and VANS.
- 14.00 p.m. Chairman's address : Government's position on public network liberalisation. John Butcher MP. Parliamentary
Under-Secretary of State for Industry.
- 14.05 p.m. Project Mercury : providing a new dimension to consumer choice. J. L. W. Bird, Esq. Managing
Director, Cable & Wireless Ltd. plc.
- 14.15 p.m. Questions/discussion.

14.25 p.m.	VANS : British Telecom's own commercial response.	J. Morris, Esq. Managing Director, Telecom Gold
14.35 p.m.	VANS : VANS suppliers as customers of British Telecom.	J. G. Graham-Smith, Esq. Managing Director, Answering Ltd.
14.45 p.m.	VANS : an opportunity for a major new service industry.	R. C. Smythe, Esq., Manager, Communication Services B. L. Systems Ltd.
14.55 p.m.	Questions/discussion.	

15.05 p.m. Tea

Mid-afternoon session : guidelines for the future from overseas.

15.20 p.m.	The USA : the market leader on innovative apparatus.	To be confirmed.
15.30 p.m.	The USA : experience on the development of network services.	To be confirmed.
15.40 p.m.	The commercial opportunities of international cooperation.	K. Edwards, Esq. Director of Technology, Northern Telecom (UK) Ltd.
15.50 p.m.	Questions/discussion.	
16.00 p.m.	Japan : land of communications and computing.	NEC film.
16.10 p.m.	The European scene.	Sir William Barlow, Managing Director, Thorn E.M.I. Ltd.
16.20 p.m.	Questions/discussion.	

Final session : the critical need to get the market-place moving.

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| 16.30 p.m. | The UK Market : role of the City in a growth market. | A. Hugh-Smith, Esq. Senior Partner,
Capel-Cure Myers. |
| 16.40 p.m. | The UK Market : union support for British industry. | R. Sanderson, Esq. National Officer,
E.E.P.T.U. |
| 16.50 p.m. | A consultant's view of Liberalisation : "too little, too late,
too slow". | J. Anderson, Esq.
Microelectronics Design Associates. |
| 17.00 p.m. | Chairman's panel session : questions/discussion. | |
| 17.30 p.m. | Chairman's closing address : summary of the day's proceedings and
resultant Government considerations. | John Butcher MP. Parliamentary
Under-Secretary of State for Industry. |

ACTION

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Prime Minister (4)

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E(TP)(82)5

COPY NO 1

- 4 JUN 1982

CABINET

MINISTERIAL COMMITTEE ON ECONOMIC STRATEGY

SUB-COMMITTEE ON TELECOMMUNICATIONS POLICY

SCOPE FOR FURTHER LIBERALISATION OF TELECOMMUNICATIONS

Memorandum by the Secretary of State for Industry

This is very disappointing. I should like to consult some friends with the

1 At E(TP)(82)1st Meeting, I was invited to report on what further progress could be made to liberalise and achieve greater efficiency in telecommunications under existing institutional arrangements.

industry before this is discussing no

2 We set out our policy on telecommunications liberalisation in July 1980. Our aims were liberalisation of the supply of all apparatus except for the prime instrument (first telephone) and certain private automatic branch exchanges (PABXs) by July 1983, liberalisation of access to BT networks for network services and examination of the scope for alternative transmission systems.

Networks

3 I issued a licence to the Mercury partners - Cable and Wireless, BT and Barclays Merchant Bank - in February 1982 -

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only 7 months after the passage of the Act. The licence is unique in the world and provides the Consortium with an opportunity to run a second national telecommunications network to compete with BT for services both at home and abroad. The licensing of Mercury has had a dynamic effect on BT as it responds to the perceived competitive threat. BT's participation in the British satellite project, its deal with Satellite Business Systems in America, its significant reduction in international and some trunk tariffs and its digital overlay can all be ascribed to potential competition from Mercury for the lucrative business market.

4 Mercury plans a gradual build-up from a City of London base in 1983. It is not easy to establish a competitive network; there have been several failures in the United States. It will take Mercury at least until 1985 to reach even 1% of BT's overall turnover. In these circumstances, I am sure that our best policy for the foreseeable future is to concentrate effort on making Mercury effective rather than contemplating more competitive networks which would only fragment what is bound to be a limited market to such an extent that Mercury itself would cease to be viable.

Network Services

5 We announced our policy to introduce liberalisation of network services such as mailbox, store and forward, videotext etc, in two phases in July 1981. The first phase, under which operators were licensed only to run services which would not compete with BT, is over. Since 1 April all network services, excluding resale of capacity over circuits leased from BT (see Annex) and international services, are free to apply to the Department direct for a licence.

6 I am now preparing a general licence to provide operators who wish to provide communication/computer services over the BT