



National Audit Office

**REPORT BY THE
COMPTROLLER AND
AUDITOR GENERAL**

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Ofcom

The effectiveness of converged regulation

Summary

1 The Office of Communications (Ofcom) is the independent regulator and competition authority for the United Kingdom communications sector, which was worth over £50 billion in 2009 and encompasses broadcasting, telecommunications and wireless communications. Ofcom's principal duty under the Communications Act 2003 is to further the interests of: citizens in relation to communications matters; and consumers in relevant markets, where appropriate by promoting competition.

2 Ofcom was created in 2003 as the result of the merger of five regulators. It raises funds from broadcast licence fees and charges, and receives grant-in-aid from two government departments: the Department for Business, Innovation and Skills (£75.7 million in 2009-10, primarily for spectrum management); and the Department for Culture, Media and Sport (£0.6 million in 2009-10, for media literacy work).

3 In 2006 we reported on the merger process. We estimated the costs of the merger to be up to £80 million, whilst observing it was too early to assess the outcomes of Ofcom's work. We recommended that Ofcom should continue to deliver efficiency savings and seek to measure longer-term outcomes and benefits. The purpose of this report is to review Ofcom's performance in the two areas where we previously made recommendations, and the outcomes it has achieved in the seven years since its creation.

4 We constructed a framework to help us form a view of Ofcom's overall performance. We selected indicators of performance under four headings: Ofcom's use of resources; the outcomes for citizens and consumers; market indicators; and the views of stakeholders.

Key findings

Ofcom is making annual efficiency savings

5 **Since 2004, Ofcom's five largest efficiency initiatives have saved some £23 million.** As forecast by policymakers when considering the merger, most of these savings came from the rationalisation of the estate and staffing levels. These savings have averaged 3 per cent per year since 2004-05, which is a similar level to the savings target the Government set for departments in the Comprehensive Spending Review 2007 process (although, with the benefit of merger efficiencies, Ofcom would be expected to fare better).

6 Ofcom is doing more with less. Excluding additional responsibilities, Ofcom's annual expenditure (£122 million in 2009-10) is now some 27 per cent lower, in real terms, than that of its predecessor bodies.

Ofcom does not report clearly how its use of resources delivers outcomes

7 Since our 2006 report, Ofcom has developed a comprehensive management information system. This system supports both Ofcom's statutory financial and performance reporting to Parliament, and its management of cash resources and programme activity to allow it to live within the annual financial cap agreed with HM Treasury. Ofcom manages its expenditure within the cap. However, in our view, Ofcom does not consistently make clear the linkage between its outputs and market outcomes, or articulate publicly how it will measure whether it has achieved its intended outcomes through its work: it does not describe what success will look like, and therefore it is not possible for us to assess whether it is meeting its objectives.

8 The radio spectrum is a national resource that Ofcom manages, generating income of some £200 million per year for the Exchequer. Ofcom spends over £70 million annually managing the spectrum. We have seen evidence of how it considers value for money on a case-by-case basis for projects it undertakes in this area, but it has made less progress in bringing together management information into higher-level performance metrics for this aspect of its business than for activities such as promoting competition in telecommunications markets. Without such use of management and cost information, Ofcom is not well equipped to demonstrate to its stakeholders, including the Departments that provide the grant-in-aid that funds this work, how it will drive through efficiencies in a strategic and structured way, based on an understanding of what the different aspects of spectrum management should cost.

Outcomes for citizens, consumers and the market appear positive

9 Our analysis suggests that there are many positive outcomes in the market. Competition in communications markets appears healthy, with increasing numbers of television and radio broadcasters, and a range of providers of fixed and mobile telephone and broadband services now in the marketplace. The growth in fixed-line and broadband competition has been enabled by regulatory action requiring BT to allow other companies to access its infrastructure.

10 Ofcom's consumer research shows that levels of customer satisfaction are generally high. For consumers of communications products and services, outcomes – such as availability and choice, falling prices and good quality products and services – have been largely positive. For example, since 2004 a representative basket of mobile phone services has fallen in price from £36 per month to £15 per month in 2009.

11 There is still scope for improvement in some areas. Two of the top ten areas in which complaints were made to the consumer helpline Consumer Direct in 2009 were in the communications market. Ofcom's data demonstrates some specific areas where improvements are needed, for example:

- a** Switching: In a well-functioning market it is important for consumers to be able to exercise choice, for example by switching providers. The communications market has relatively low switching rates and it is important for Ofcom to understand whether this is through consumers' choice or whether they face barriers. Twenty-eight per cent of consumers feel it is difficult to switch. Ofcom is seeking to tackle barriers to switching as a priority for 2010-11.
- b** Broadband speed: Ofcom's research in May 2010 found that average speeds in the UK were some 45 per cent slower than advertised. Ofcom introduced a voluntary code of practice in 2008, and strengthened it in July 2010, to address this discrepancy between advertised and actual speeds. UK consumers experience broadband speeds that are lower than in many other countries.
- c** Silent calls: There are persistent issues where automatic dialling equipment in call centres fails to connect operators properly, which can cause nuisance or anxiety to the person called. Ofcom has imposed a number of fines, but despite an initial fall in complaints there has been more fluctuation since summer 2009. Parliament and the Government recently increased the maximum fine available to Ofcom after it called for stronger powers in this area.

12 The majority of stakeholders we engaged with felt Ofcom conducts its consultations well, but 44 per cent of those we surveyed felt that Ofcom does not go on to act in a timely manner on the relevant issues. Ofcom told us that its speed of action is hampered by the incentives on regulated bodies to appeal its decisions. Ofcom considers evidence submitted by regulated companies several months after the formal close of a consultation, as it feels not to do so could itself be grounds for appeal. The frequency of appeals is increasing and has cost Ofcom over £1 million per year since 2007-08. The Department for Business, Innovation and Skills began consulting on a proposal to change the appeals regime in September 2010.

Conclusion on value for money

13 Good value for money is the optimal use of resources to deliver the intended outcomes. Ofcom's assessment of its performance in delivering value for money, however, is driven by delivering its work programme within the annual financial cap agreed with HM Treasury, while taking on additional areas of responsibility for no further cost to the public purse. Ofcom has reduced its overall expenditure each year since its creation; we have seen many positive indicators in the communications marketplace; and most stakeholders speak positively of Ofcom. We have also seen that Ofcom is taking action to address some of the issues we have identified – for example, its 2010-11 Annual Plan has a greater focus on outcomes than in previous years, and it is implementing some very encouraging changes to its internal performance management processes – although a number of these developments have only taken place since we began work on this study. We have

seen evidence from some individual projects that Ofcom considers value for money in its decision making, rather than purely seeking to minimise costs. However, in the absence of a clear articulation of its intended outcomes, or the linkages between its inputs and outputs and those outcomes, there is still a gap between the way Ofcom assesses its own performance and our assessment of value for money. It is, therefore, not possible for us to conclude on the extent to which Ofcom has delivered value for money. This will remain the case until Ofcom develops a consistent capacity to link costs and activities to outcomes in a way that can help stakeholders assess its performance.

Recommendations

14 There are three areas of Ofcom's business in which we would expect to see improvements. These are: articulating success criteria; spectrum management accounting; and reporting of efficiencies.

- a Ofcom has developed an internal performance measurement framework, but it does not communicate clearly the linkage between outputs and outcomes.** For greater accountability and demonstration of value, Ofcom should communicate more clearly how it defines success in terms of the outcomes that it is striving to achieve and how its outputs contribute to delivering these. It should also develop, in consultation with the relevant Government Departments, the industries it regulates, and the citizens and consumers on behalf of whom it acts, a more integrated performance measurement system. This should include a framework for external reporting of performance against the outcomes it has set itself to deliver, in pursuit of its statutory duties.
- b Ofcom receives over £70 million grant-in-aid to manage the radio spectrum, but performance information in this area is relatively sparse, so that the extent to which value for money is being obtained from this expenditure is unclear.** Ofcom should undertake work to identify the key drivers of expenditure in managing the spectrum and use this information to ensure efficiency and value for money are maximised.
- c Ofcom does not routinely report efficiency savings to the Government Departments that agree and authorise its grant-in-aid funding.** The relevant Departments should, as a matter of routine, assess Ofcom's efficiency savings: we suggest annual meetings. Ofcom should also, as far as is practical, outline the key drivers of costs in-year for the benefit of its stakeholders, for example the consumers who ultimately pay for services.

On Ofcom's speed of action and the legislative environment:

- d The Communications Act sets a higher 'hurdle' for Ofcom in dealing with appeals against its regulatory decisions than is the case for other economic regulators.** The Department for Business, Innovation and Skills, should take into account Ofcom's evidence concerning the impact of the current regime as part of its review of the legislative framework for appeals.