



National Audit Office

Performance of the Department of Trade and Industry 2006-07



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Summary

- 1** This paper provides briefing for the Select Committee to provide an overview of the work and performance of the former Department of Trade and Industry in the financial year 2006-07 and subsequent months.
- 2** It takes as its basis the Department's Annual Report, drawing upon the work of the Select Committee and the National Audit Office (NAO), together with relevant findings and recommendations from other external and internal reviews of departmental performance.
- 3** The contents of the briefing have been shared with the Department to ensure that the evidence presented is factually accurate. Conclusions on the matters that the Committee may wish to explore are the sole responsibility of the National Audit Office.
- 4** Most of the responsibilities of the former Department for Trade and Industry, with the exception of its science and innovation brief, were transferred to the new Department for Business, Enterprise and Regulatory Reform (BERR) on 28 June 2007. This paper focuses on those departmental activities that are now carried out by BERR plus the work of the Better Regulation Executive which has been added to the new Department's responsibilities.
- 5** This paper comprises three Parts:
 - Part 1 (page 9) considers the Department's operating environment;
 - Part 2 (page 12) examines the Department's capacity to deliver its goals; and
 - Part 3 (page 19) looks at how key parts of the Department performed in 2006-2007.

The operating environment (page 9)

- 6** The recent transfer of responsibilities of the former DTI to BERR places the new department under additional pressure to show that it can deliver, especially in the area of regulatory reform. To achieve many of its aims, the Department's success will rest on its ability to influence a wide range of stakeholders in the UK, Europe and abroad.
- 7** The new Department will continue to face important policy challenges such as securing future energy supplies in an environment of declining domestic oil and gas production, and improving the UK's productivity and trade performance against the backdrop of a rapidly changing world economy.

Key areas the Committee may wish to explore

- The challenges presented to Departmental performance by moving from DTI to BERR.
- Whether the Department will take the opportunity to consider its delivery structures given its wide operational brief.
- The extent to which the Department feels it can influence, and measure its impact on, UK productivity.
- How the Department is planning for future changes in the source of energy supplies.
- How UK efforts to boost exports to emerging markets compare with those of our competitors.

1. Third Validation Compendium Report, NAO, December 2006.

Capacity to deliver (page 12)

8 The Capability Review identified Leadership as an area needing improvement.

In December 2006, the Cabinet office reviewed the Capabilities of the Department in: leadership, strategy and delivery. Focusing on ten areas it categorised the Department 'well placed' in four, 'development' in four and 'urgent development' in two (page 12, paragraphs 2 and 3).

9 The Department has reported efficiency savings of £500 million. It has exceeded its Gershon Report targets for both efficiency savings and reducing headcount (page 15, paragraphs 17 and 18).

10 Only half of the Department's Public Service Agreement (PSA) data systems are fit for purpose. Between October 2006 and March 2007 we examined the data systems for all the DTI's 2005-2008 PSA targets. We found that 56 per cent were fit for purpose, while a further 16 per cent were broadly appropriate (see Appendix 3, page 34). A previous NAO report on the data systems used by HM Treasury on PSA 7 identified weaknesses in the measurement of regional economic performance¹, a PSA shared with the DTI (page 17, paragraphs 30 to 33).

11 Two agencies had to write-down the value of major IT assets in 2006-07 totalling £19.7 million. Implementation of the Companies House Information Processing System (CHIPS) has been delayed and continues to pose challenges although action is being taken to address these. In addition, the Insolvency Service has terminated the contract for the development of the CAMEO IT banking system on the basis that it was unlikely to succeed (page 15, paragraph 16).

12 Our recent report on the Shareholder Executive concluded that it has a good shareholding model – with the exception of Royal Mail (page 16, paragraphs 20 to 22).

13 The Department has made significant improvements to financial management, including strengthening its finance team (page 14, paragraphs 11 and 12).

14 A recent survey of senior staff in the Department suggested that a majority felt challenged in their work but many felt that, compared to similar jobs in other organisations, their total benefits package was not reasonable (page 13, Figure 3 and paragraph 6).

Key areas the Committee may wish to explore

- The impact of Gershon efficiency savings on frontline resources.
- The impact of IT failures on the delivery of services.
- Challenges in recruiting and retaining staff.

Delivery in 2006-07 (page 19)

15 The Department has reported a mixed performance against its PSA targets. Against the nine Public Service Agreement targets covered in this paper, the Department reported that four are 'on course', one has experienced slippage, and two have experienced slippage in at least one of the sub-targets that underlie the PSAs. The remaining two PSAs have not yet been assessed. (See Appendix 1, page 31).

16 Following the Comprehensive Spending Review 2007 in October the Government announced a new set of PSA targets and a series of Departmental Strategic Objectives (page 18, paragraphs 34 and 35). Of the 30 new cross-Government PSA targets BERR is the lead department on three: PSA 1, Raising the productivity of the UK economy, PSA 6, Delivering the conditions for business success in the UK, and PSA 7, improving the economic performance of all English regions.

Supporting Successful Business (page 19)

17 The Department reports that it is on course to meet all PSA targets in this area, except for increasing the number of people considering going into business. It is difficult to separate the impact of departmental action to support UK business from the effects of the economic cycle. It is also difficult to obtain timely, reliable performance information (page 19, paragraphs 2 to 4).

18 The Department is seeking to rationalise the large number of support schemes available to business. The Government has set itself a target to reduce the number from 3,000 down to 100. No timetable has been set (page 20, paragraph 7).

19 Businesses surveyed by the NAO suggested that the Small Business Service was not well-placed to set a Government-wide agenda on small business. To improve its effectiveness, the Small Business Service (SBS) has since changed from being an Executive Agency to become a policy unit within the Department. (page 20, paragraphs 6 to 8).

2. Reducing the cost of complying with regulations: The delivery of the Administrative Burdens Reduction Programme, 2007, NAO, page 6.

3. Evaluation of Regulatory Impact Assessments 2005-06, NAO.

Key areas the Committee may wish to explore

- Whether the new public service agreements and Departmental Strategic Objectives will refocus the broad thrust of the Department's work.
- Whether incorporating the Small Business Service as part of the Department will improve its ability to influence decision-making in government.
- Whether the Department is making sufficient progress towards rationalising the number of business support schemes.

Ensuring fair markets that are efficiently regulated (page 22)

20 The Department reports success in achieving fair, competitive markets but slippage in achieving significant reductions in trade barriers (page 22, paragraph 16).

21 The NAO found that the Department is placing a firm focus on reducing the administrative burdens on industry, although three-quarters of businesses surveyed felt that Government does not understand business well enough to regulate it effectively² (pages 22 to 24, paragraphs 16 to 22).

22 The NAO report on Regulatory Impact Assessments (RIAs)³ concluded that the Department was performing more strongly than the other departments examined. We concluded that there was still room for improvement across all departments – such as ensuring that RIAs influence decision-making rather than simply being informative (page 24, paragraphs 23 to 25).

Areas the Committee may wish to explore

- Stakeholder concerns that Government does not understand business well enough to regulate it.
- Whether efforts to reduce administrative burdens are focusing on areas that are important to the business community.
- Ensuring that Regulatory Impact Assessments are done in a timely manner and in a way that influences the direction of policy.

4. Some £2.6 billion of this increase was due to a change in discount rate to align the calculation with HM Treasury guidance.

Ensuring secure, sustainable and affordable energy (page 26)

23 The Department reports difficulties in reducing carbon dioxide emissions and ending fuel poverty. Both of these targets are heavily influenced by energy prices, which are outside departmental control (pages 26 and 27, paragraphs 32 to 33).

24 Estimates of the likely cost of decommissioning civil nuclear sites continue to increase. The Nuclear Decommissioning Authority, overseen by the Department, is taking forward the task of decommissioning the UK's civil nuclear sites. This is a significant and, in financial terms, risky task. The Authority has invested effort into improving the methods used for estimating the potential future costs of decommissioning. Estimates of the discounted nuclear liabilities increased from £24 billion in 2005 to £37 billion in March 2007.⁴ Over the coming period, the Authority is due to complete the initial competitions to appoint parent body organisations to take forward decommissioning at these sites. The competition for the Low Level Waste Repository near Drigg in Cumbria is already well advanced and due to be completed by the end of 2007 (page 16, paragraphs 23 to 26).

Areas the Committee may wish to explore

- The Department's long term approach to resolving the issue of fuel poverty.
- The Department's long term approach to improving security of supply in the gas market.
- Progress in measuring the size of the nuclear liabilities and the efforts to reduce the uncertainties associated with these estimates.

The Department's operating environment

1 The new Department's responsibilities cover a wide range of policy areas aimed at promoting a successful UK economy. These responsibilities range from promoting fair markets and managing the Government's shareholdings, to securing and developing sustainable energy supplies. The recent transfer of the Better Regulation Executive from the Cabinet Office has added a further raft of responsibilities to the new Department's remit.

2 Many of the former DTI's responsibilities were delivered through its five executive agencies and 30 executive non-departmental public bodies. These bodies employed around 21,000 people and spent about 70 per cent (£4.7 billion) of the Department's total budget in 2006-07. This network of bodies, with the exception of the research councils, the Design Council, the National Weights and Measures Laboratory and the Patent Office, has transferred to the new Department.⁵

3 Control of public expenditure incurred in pursuit of the Department's objectives is achieved through the setting and monitoring of budgets, primarily its Departmental Expenditure Limits (DEL) budgets, regardless of which body or bodies within the client family manages the spend. These are sometimes known as resource budgets.

4 Resource budgets and their reported outturns are not subject to audit by the Comptroller and Auditor General. However, we note from Chapter 6 of the Annual Report that in 2006-07 the Department recorded an underspend of £213 million against total resource DEL budget of £5,718 million, and an underspend of £126 million against a total capital DEL budget of £1,292 million.

5 Resource budgets should not be confused with the Consolidated Resource Account which only includes the expenditure of the Department and its executive agencies.⁶ The primary accountability statement for the Consolidated Resource Account is the Statement of Parliamentary Supply which is subject to external audit by the Comptroller and Auditor General.

6 For the purposes of the Resource Accounts, the Department of Trade and Industry's estimate of net resource requirement outturn of around £6.8 billion in 2006-07 placed it amongst the smallest of the departments. Compared with the former DTI, the new Department's budget will reduce further with the transfer of the science portfolio to the Department for Innovation, Universities and Skills (some £3.1 billion in 2006-2007). BERR remains, however, a significant financial entity in terms of the assets and liabilities on its balance sheet (**Figure 1, page 10**).

7 In 2006-07, the Department had a net resource outturn, as shown in the Statement of Parliamentary supply, of £6,111 million, a similar amount to 2005-06. This outturn represented a £713 million underspend on its final Estimate of £6,824 million.⁷ Page 177 of the Annual Report outlines in detail the main reasons for the difference between estimate and outturn.

8 Consolidated Fund Extra Receipts increased by more than £5 billion compared to the previous year. The annual report shows that the increase was due to: a special dividend received from BNFL plc; the early repayment of a £575 million BNFL debenture; and the liquidation of the Nuclear Liabilities Investment Portfolio (NLIP) following the transfer of the responsibility for the discharge of nuclear liabilities to the NDA.

5. Department of Trade and Industry Annual Report 2006-07, paragraph 3.36.

6. It also includes its administration expenditure on UK Trade & Investment, and expenditure on ACAS.

7. Department of Trade and Industry Annual Report 2006-07, page 177.

1 Summary Balance Sheet

	2005-06 £m	2006-07 £m	Change %
Fixed Assets			
Investments	4,537	5,639	24
Other	184	210	14
Net Current Assets	1,435	1,595	11
Creditors > 1 year	1,095	541	51
Provisions for liabilities			
Coal	2,309	1,621	-30
Nuclear	2,575	2,544	-1
Other	380	331	-13
Total Assets less Current Liabilities	203	2,407	1186

Source: Department of Trade and Industry Annual Report and Accounts 2006-07, figures for the core Department, page 204. Fixed asset investment data is on page 229 of the Report and Accounts.

NOTE

Figures do not cast correctly due to rounding.

9 The summary balance sheet at Figure 1 shows that the Department moved from total net liabilities of £203 million in 2005-06 to a position of total net assets of £2,407 million in 2006-07, a net increase in asset value of £2,610 million. The main reasons for this change, as stated in the annual report, are:

- an increase of £1,286 million in the valuation of the Coal Pension Investment Reserve following the Government Actuary Department's triennial valuation (categorised as 'Fixed Assets – Investment' in Figure 1);
- a £430 million increase in the Department's investments in Royal Mail Holdings plc in order to inject funds into Post Office Limited, the subsidiary that provides the post office network arm of the business (categorised as 'Fixed Assets – Investment' in Figure 1); and
- a £769 million net reduction in provisions, primarily due to £522 million of claims being paid in the year in connection with the Chronic Obstructive Pulmonary Disease element of Coal provisions (categorised as 'Provisions for liabilities' in Figure 1).

10 Tangible fixed assets increased by £26 million in 2006-07, reflecting a small reduction in the assets of the Department's agencies and a £31 million increase in assets in the core Department. Increases in the core Department's assets resulted from an increase in assets under construction including additional work on the National Physical Laboratory, improvements to buildings on the Departmental estate and spend on major IT projects (see page 15, paragraph 16, on write-downs on IT projects).

The success of the new Department will hinge on its effectiveness in influencing the work of others

11 In many policy areas, the DTI's effectiveness was heavily dependent on its ability to influence the work of others. Of the 11 PSA targets set out in the 2004 spending review, five were joint targets with other departments and its success on the others was dependent on working with bodies outside Government, including business and the European Commission.

12 The transfer of most of the former responsibilities of the DTI to the Department for Business Enterprise and Regulatory Reform will have a number of implications for the new Department:

- the increased emphasis on regulatory reform will create further pressure for the Department to demonstrate that it can reduce the regulatory and administrative burdens on businesses – the Government estimated the total regulatory burden imposed by all departments at May 2005 as some £20 billion, of which the former DTI accounted for around 25 per cent;
- the tighter policy focus will challenge the Department to show that it can make a real impact; and
- the continued drive to reduce headcount to the level set in the Gershon Report has increased the pressure on the Department to deploy its remaining resources effectively.

The future

13 The Department faces some important policy challenges over the next few years. The most prominent of these include:

- securing energy supplies against a backdrop of declining domestic oil and gas production;
- taking forward the programme of nuclear decommissioning and whatever decisions are taken following the current consultation on the future of nuclear energy;
- tackling the need to improve UK productivity;
- addressing climate change via the reduction of greenhouse gas emissions and the promotion of energy efficiency;
- determining the future shape of postal services; and
- securing good access for UK businesses to emerging markets.

Areas the Committee may wish to explore

- The challenges presented to Departmental performance by moving from DTI to BERR.
- Whether the Department will take the opportunity to consider its delivery structures given its wide operational brief.
- The extent to which the Department feels it can influence, and measure its impact on, UK productivity.
- How the Department is planning for future changes in the source of energy supplies
- How UK efforts to boost exports to emerging markets compare with those of our competitors.

Drivers and enablers of performance

1 This part examines the Department's capacity to deliver its policy goals. It looks in turn at:

- capability;
- financial management; and
- performance measurement.

Capability

Capability Review

2 In December 2006 the Cabinet Office published a Capability Review of the Department of Trade and Industry. It assessed the Department's performance in three key areas of capability: leadership, strategy and delivery.

3 The Department's capability was assessed as "well placed" in four of the ten elements in the model of capability; four were assessed as "development" areas; two as "urgent development areas". There were no areas of serious concern. **Figure 2** summarises the reviewers' findings.

4 One area the Review commented upon was the relationship the Department had with NDPBs. The reviewers observed "Relationships are often characterised by financial control rather than by joint strategic priority-setting and follow-through". Strategic priority setting is crucial for a Department which uses a large number of third parties to deliver its policy objectives.

Access to the right skills

5 The Review also noted that the Department needed to do more to identify and develop the skills and competencies required for the future. The Department subsequently committed to build, during the course of 2007, on existing work to identify its skills' needs and ensure that its recruitment, retention and development strategies reflected these priorities.

2 Assessment of the DTI's capability for future delivery

Leadership

Set Direction	●
Ignite passion and drive	●
Take responsibility for leading delivery and change	●
Build capacity	●

Strategy

Focus on outcomes	●
Base choice on evidence	●
Build common purpose	●

Delivery

Plan, resource and prioritise	●
Develop clear roles, responsibilities & business models	●
Manage performance	●

● Strong	● Well placed	● Development area
● Urgent development area	● Serious concerns	

Source: Published by the Cabinet Office in December 2006

6 In October 2006 senior staff at the Department were surveyed for their views on: leadership; working in the Department; and improvements which need to be made to the Department. These answers were then compared to the rest of the Civil Service. Some 160 staff (68 per cent of the population) completed the survey. The majority felt challenged in their work,

but many felt that, compared to similar jobs in other organisations, their total benefits package was not reasonable. **Figures 3 and 4** show the statements receiving the highest and lowest favourable responses, and how this level of response compared to the wider civil service.

3 Highest Favourable Scores

Question	% Favourable	Variance from Senior Civil Service overall
3. I understand how my work contributes to the objectives of the Department	98	0
49. I am committed to seeing my Department succeed	95	-3
24. I feel confident I have the leadership skills required to do my current job effectively	93	+5
36. My job gives me a feeling of personal accomplishment	93	+3
26. I have challenging work objectives	93	0

Source: SCS Survey 2006, ORC International

4 Lowest Favourable Scores

Question	% Favourable	Variance from Senior Civil Service overall
41. In comparison with similar jobs in other organisations, I feel my pay is reasonable	27	-12
40. The way pay is determined is clear and transparent	27	-5
42. In comparison with similar jobs in other organisations, I feel my total benefits package is reasonable	30	-11
29. Poor performance is dealt with effectively in my Department	38	+19
21. The Executive Board/Management Board/Top team in my Department model a culture of effective teamwork	39	+13

Source: SCS Survey 2006, ORC International

8. The Shareholder Executive and Public Sector Businesses, NAO, Paragraph 1.15.

9. Gas distribution networks: Ofgem's role in their sale, restructuring and future regulation, PAC, Fourth report of the Session 2006-07, Paragraph 8.

10. The Office of Gas and Electricity Markets: Sale of gas networks by National Grid, NAO, Paragraph 2.6.

11. Department of Trade and Industry Annual Report 2006-07, page 194.

12. Department of Trade and Industry Annual Report 2006-07, page 198.

7 Our value for money (VFM) audit reports have highlighted a recurring challenge faced by the Department and its agencies and NDPBs in recruiting and/or retaining staff with the right skills. For example:

- The Shareholder Executive has found that departmental pay constraints have sometimes had an adverse impact on the ability to attract, retain and incentivise experienced management teams in some of its businesses.⁸
- Ofgem reported that it is properly staffed for its normal business but not for one-off projects, including commercial transactions which require specialist expertise in corporate finance.⁹ We reported that it did not have enough staff throughout the two years of the sale of the regional gas distribution networks which were finalised in June 2005.¹⁰

8 The Department has sought to deploy its staff more effectively and flexibly. In 2006, it established a 'Project Pool' of 150 staff to ensure that key priorities are resourced adequately. Policy makers in the Pool specialise in different aspects of policy making and are expected to develop their expertise in project management.

Financial management

Financial Control

9 Strong financial controls help departments to operate effectively. The Accounting Officer is responsible for maintaining a sound system of internal control that supports the achievement of the Department's policies, aims and objectives, whilst safeguarding public funds. In his statement on internal control¹¹ the Accounting Officer confirmed that the effectiveness of the system had been reviewed and reported no significant issues in 2006-07 in the core Department.

10 In undertaking the external audit of the Department's resource accounts the National Audit Office was able to place reliance on the Department's overall control environment; we found no major control issues that required the attention of senior management.

11 Over the last two years the Department has made some significant improvements in financial management. In particular, the finance team has been strengthened through the appointment of a qualified accountant to the role of Director General of Finance and Strategy and the quality of the monthly financial reporting has improved. The Department recognises, however, that there is scope for further improvement and has launched the Excellence in Financial Management Programme. This programme seeks to establish the Department as one of the best in Whitehall at financial management.

12 This year, as in 2005-06, the Department met the challenging pre-summer recess deadline for laying of the audited resource accounts before Parliament. Additionally, the Department has been amongst the first to participate in a Treasury-led pilot to produce a combined departmental and annual report. This represents a significant step forward in terms of transparency of reporting and, despite the time pressure, the Department produced a comprehensive and well-structured annual report.

13 With regard to the Department's agencies, and NDPBs the Comptroller and Auditor General issued a qualified audit opinion on the Design Council's 2005-06 accounts on regularity grounds in July 2007. The Design Council implemented its 2005-06 pay award, which amounted to a 6.86 per cent increase in average earnings growth, without obtaining the required approval of the Department. Subsequently the Department, in accordance with Treasury guidelines, retrospectively approved an increase of 3.5 per cent in average earnings growth. On the instructions of the Department, the Design Council has recruited a qualified accountant to ensure HM Treasury guidance is adhered to in future. The Design Council have also modified their audit and risk management processes.¹²

Risk management

14 The Department notes in its annual report that since 2005-06, it has developed a long term risk register to improve early identification of future risks. The intention is that these risks will be reviewed every six months. Should the threat increase, these risks are escalated to the BERR Management Board risk register to take appropriate action.¹³

15 We have examined risk management in action across a variety of departmental activities. Recent reports have highlighted examples of good practice, for example the arrangements put in place by the Department to manage the risks associated with the closure of the Coal Health Compensation Schemes.¹⁴ Following the closure of MG Rover in 2005 the Department identified that it could make better use of its formal risk management processes as a mechanism for raising corporate awareness in such situations.¹⁵

16 Recent problems encountered at Companies House and within the Insolvency Service highlight, however, the potential risks associated with the management of activities undertaken by the Department's agencies and NDPBs. Indeed two agencies were forced to write-down the value of major IT assets in 2006-07:

- Implementation of the Companies House Information Processing System (CHIPS) has been delayed. A review of the capitalised project cost for CHIPS was carried out at year end, resulting in a write down in the value of the assets of £7.5 million. With £4.6 million written off during 2005-06, the total impairment for which there has been no appreciable benefit is now £12.1 million. The Agency's Accounting Officer warns that the programme continues to be challenging and further risks remain but actions have been agreed to mitigate or provide contingencies for these risks.

- Following a decision taken by the Insolvency Service to terminate the contract for the development and procurement of the CAMEO IT banking system on the basis that it was unlikely to succeed, the Service has written off a capitalised balance of £3.4 million representing the associated assets under construction. Over the life of the project, the Service expended a total of £7.64 million under the CAMEO contract for which it received little appreciable benefit.¹⁶

Operational efficiency

17 The DTI has been active in seeking efficiency savings in pursuit of the targets set by the Gershon Report.¹⁷ The DTI's Annual Report for 2006-07 reports efficiency savings of some £500 million at the end of the second year of the programme, against an overall target of £380 million for the period. These savings include 1,251 staff reductions, already ahead of the 2007-08 target of 1,010.¹⁸

18 The main sources of the Department's reported savings are detailed at page 141 of its Annual report. The NAO has reviewed the robustness of the Department's estimates of efficiency savings on most categories, but not all. Our report on The Efficiency Programme¹⁹ agreed the departmental calculations of efficiency savings on: estates, information, communication and technology; and procurement. We could not, however confirm the reported savings on consultancy, as a lack of output measures meant the Department could not demonstrate that reduced spending was due to efficiency as opposed to yearly variations in demand.

Managing Assets and Liabilities

19 The Department holds considerable assets such as government shareholdings, and manages significant liabilities such as nuclear decommissioning costs and compensation claims relating to personal injuries suffered by former British Coal Corporation mineworkers.

13. Department of Trade and Industry Annual Report 2006-07, Page 195.

14. Managing Risks to Improve Public Services, NAO, Case studies annex.

15. Treasury Minute, 57th Report 2005-06, The Closure of MG Rover, Paragraph 5.

16. Department of Trade and Industry Annual Report 2006-07, Page 198.

17. Releasing resources for the frontline: Independent Review of Public Sector Efficiency, Gershon, 2004.

18. Department of Trade and Industry Annual Report 2006-07, page 141.

19. The Efficiency Programme: A Second Review of Progress, NAO, page 45.

20. The Shareholder Executive and Public Sector Businesses, NAO, February 2007.

21. Royal Mail Group, House of Commons Trade and Industry Committee, October 2006.

22. Royal Mail Group, House of Commons Trade and Industry Committee, conclusion 18.

Assets

20 The Shareholder Executive (the Executive), an operational group within the Department, is responsible for the management of shareholdings in 17 Government-owned businesses either on behalf of, or in co-operation with, the sponsoring departmental shareholding team. These include, for example, Royal Mail, British Energy, British Nuclear Fuels Limited and the Royal Mint. It also plays an advisory role to the relevant team for a further 10 businesses.

21 Our value for money audit report on the Executive²⁰ found that:

- in general, it has a good shareholding model (with the exception of Royal Mail, where the Executive is responsible for: departmental policy on the postal market and the Post Office network; oversight of the postal services consumer watchdog; and, in some respects, the statutory regulator, while also managing the shareholding);
- it makes effective use of its shareholder powers, such as the removal of directors, and there is good use of non-executive directors and communication channels to improve the performance of trading funds;
- it needs better targets, such as an overall portfolio target plus individual business targets; and
- if it had the ability to provide businesses with access to finance, it would have an additional lever to help it manage for value.

22 The Trade and Industry Select Committee, in its October 2006 report on the Royal Mail Group²¹, concluded that the Government was acting as a responsible shareholder in its financial support for the business. The Committee voiced concern about the conditions that the Royal Mail Group had placed on agreeing to the Government's financial support package. The Committee cautioned that the Government might need to continue subsidising parts of the post office network if it proved commercially unviable to keep sufficient offices open to provide a universal service.²²

Liabilities

23 The expected cost of decommissioning civil nuclear legacy sites accounts for the largest set of liabilities in the BERR family group. The Nuclear Decommissioning Authority (NDA), took on responsibility for the clean-up of 19 designated civil nuclear sites on 1 April 2005. This is a significant and, in financial terms, risky task.

24 Since taking on this responsibility the NDA has invested resources in improving the methods used for estimating the future costs of decommissioning and cleaning up the sites for which it is responsible. Drawing on the Life Time Plans (LTPs) – previously known as Lifecycle Base line (LCBL) methodology developed for the DTI's Liabilities Management Unit – the NDA aim to have established a robust baseline by 2008. Estimates of the discounted nuclear liabilities increased from £24 billion in 2005 to £37 billion in March 2007.

25 Over the last two years, gaps in the previous estimation of the decommissioning tasks were identified, for example: in understanding the quantity and physical state of waste in legacy ponds and silos; assessing the costs associated with waste for which no final disposal route is identified; and beginning an estimation of the impact of cleaning up contaminated land. Each one of these areas has increased the overall cost of the liabilities by over £1 billion. Additionally, in the first year of the NDA's responsibility there was an increase of £2.6 billion in the liabilities as the rates at which the provisions had previously been discounted were aligned to the rate set by HM Treasury.

26 The C&AG's audit for both 2005-06 and 2006-07 concluded that the methods used were sufficient to determine a reasonable nuclear provision for the NDA accounts, although he included a 'matter of emphasis' paragraph in his audit certificate to draw attention to the uncertainties with the nuclear provision.

27 The liabilities also include £1.6 billion for the discharge of the remaining compensation claims relating to personal injuries suffered by former British Coal Corporation mineworkers (see Figure 1, page 10). Both the Committee and the NAO have reported on the administration of these compensation schemes.²³

28 The Committee looked at future risks to closure and found that there remained issues to be resolved. We reviewed the whole life of the scheme and found that the Department's lack of preparation in the early stages made its task significantly more difficult, and weaknesses in negotiation with claimant's representatives might have led to increased costs.

29 The Department had set aspirational dates for completing the coal health schemes: 31 October 2007 for Vibration White Finger (VWF) scheme and 16 February 2009 for Chronic Obstructive Pulmonary Disease scheme. A significant proportion of the remaining claims raise more complex issues and will therefore pose a challenge to clear. It is likely that the Aspirational Scheme End Date for VWF will be missed.

Performance measurement systems

30 One key driver of a department's capacity to deliver its objectives is knowing when the action it takes leads to outputs and outcomes; it is important, therefore, to have robust performance measurement systems in place to evaluate success.

31 As part of its routine work, the NAO undertakes a cyclical review to validate the data systems used by departments to monitor and report performance against their PSA targets.²⁴ In 2006-07, we examined the systems supporting the PSA targets shared by the DTI with HM Treasury (PSA 1: Productivity and PSA 7: regional economic performance) and separately with DEFRA (PSA 4 (i): greenhouse gas emissions and PSA 4 (iv): eliminating fuel poverty).

32 We found the data systems to be generally fit for purpose, with the exception of PSA 7: regional economic performance. This target measures the relative growth rates of the three best performing regions in England against the other remaining regions, with the aim of reducing the gap between these two groups. The measure used to assess performance of these two groups is Gross Value Added (GVA) per head. A study commissioned by HM Treasury²⁵ and published in 2004 concluded, however, that "present estimates of regional GVA were not of sufficient quality to support analysis of the Government's policy objectives to increase growth in the regions". Because of these difficulties, a number of proxy measures are being used to look at performance in the interim period; these include progress against a number of drivers of regional economic performance. Our examination of these proxy measures suggest that they are likely to have an association with the underlying regional economic performance.²⁶

33 Between October 2006 and March 2007 we carried out a further examination of the data systems for all the Department's 2005-2008 PSA targets. This involved, for each individual data system, a detailed review of the processes and controls.

We assessed the data systems using a 'traffic light' system and rated:

- Eighteen (56 per cent) – as Green – 'fit for purpose'.
- Five (16 per cent) – as Amber – 'broadly appropriate'.
- Five (16 per cent) – as Red – 'not fit for purpose'.
- Four (13 per cent) – White – 'too early to form a view or not established'.²⁷

Appendix 3, page 34, gives a more detailed breakdown of our findings.

23. Coal Health Compensation Schemes, TISC, March 2005 and Coal Health Compensation Schemes, NAO, July 2007.

24. Third Validation Compendium Report, NAO, December 2006.

25. Review of Statistics for Economic Policymaking – Final Report, by Christopher Allsopp, March 2004.

26. Mind the Gap: Tackling Disparities in Regional Economic Performance, NAO, Paragraph 8.

27. Figures do not cast correctly due to rounding.

Performance measurement systems

34 The Comprehensive Spending Review 2007 (CSR07), published 9 October 2007, sets out 30 cross-Government PSA targets. BERR is the lead department responsible for delivering three:

- PSA 1: Raise the productivity of the UK economy;
- PSA 6: Deliver the conditions for business success in the UK; and
- PSA 7: Improve the economic performance of all English regions and reduce the gap in economic growth rates between regions.

This briefing assesses the Department's performance against its PSA objectives under CSR04, extant in the 2006-07 financial year.

35 In addition to the PSA targets CSR07 sets the Department seven Strategic Objectives:

- promote the creation and growth of business and a strong enterprise economy across all regions;
- ensure that all departments and agencies deliver better regulation for the private, public and third sectors;
- deliver free and fair markets, with greater competition, for businesses, consumers and employees;

- ensure the reliable supply and efficient use of clean, safe and competitively priced energy;
- manage energy liabilities effectively and responsibly;
- ensure that the Government acts as an effective and intelligent shareholder, and provide a source of excellent corporate finance expertise within departments; and
- provide the professional support, capability and infrastructure to enable BERR's objectives and programmes to be successfully delivered.

Areas the Committee may wish to explore

- The impact of Gershon efficiency savings on frontline resources.
- Challenges in recruiting and retaining staff with the correct skills.
- The potential for a better shareholder model for the Royal Mail Group.
- The reliability of PSA measures of regional economic performance.

Delivery in 2006-07

1 This part looks at how the Department performed in 2006-07. It is structured under the following three themes:

- supporting successful business;
- ensuring fair markets that are efficiently regulated; and
- ensuring secure, sustainable and affordable energy.

Supporting successful business

(Section 2.5, page 44, of the Annual Report)

2 The DTI had three PSA targets related to its objective of supporting successful business. Progress against these targets, as reported in the Department's annual report, is shown below.

PSA 6. Enterprise

"Build an enterprise society in which small firms of all kinds thrive and achieve their potential, with":

- i "an increase in the number of people considering going into business"; **SLIPPAGE**
- ii "an improvement in the overall productivity of small firms"; **ON COURSE**
- iii "more enterprise in disadvantaged communities"; **ON COURSE**

PSA 7: Regional economic performance

"Make sustainable improvements in the economic performance of all the English regions by 2008 and over the long term reduce the persistent gap in growth rates between the regions, demonstrating progress by 2006." A Joint target with HM Treasury and the Department for Communities and Local Government. **ON COURSE**

PSA 8: UK Trade and Investment (UKTI)

"By 2008 deliver a measurable improvement in the business performance of UK Trade & Investment's international trade customers, with an emphasis on new to export firms; and maintain the UK as the prime location in the EU for foreign direct investment". A Joint target with the Foreign and Commonwealth Office. **ON COURSE**

3 The enterprise and regional economic performance targets (PSA 6 & 7) address cultural and socio-economic issues where the Department's role is primarily one of influence rather than intervention. This presents a number of measurement challenges: it is not easy to separate the impact of Departmental actions from the effects of the economic cycle; or to measure recent progress, as it takes a long time to gather and disseminate performance information. The most recent data, for example, on the productivity of small firms refer to 2004. These challenges, together with the problems in obtaining accurate data on regional economic performance (see page 17, paragraph 32 above), mean that caution is advisable in drawing conclusions on departmental performance based solely on the PSA targets.

4 There has been mixed success in achieving departmental targets for supporting successful business:

- **PSA 6 (i):** The Department believes that it is unlikely to achieve an increase in the number of people considering going into business within the current spending review period. The most recent information shows that 11.6 per cent of adults in England were considering going into business in 2005, the same as in 2001. The annual report states that the initial target of 14 per cent has been reduced to 12.3 per cent, but even this target requires a change in the intentions of over 300,000 people.
- **PSA 6 (ii):** Progress has been better against the small firms productivity target. The Department reports that productivity growth for small and medium-sized enterprises has exceeded all-firms productivity growth in four out of the last five years for which data is available (1999-2004). Productivity may increase if the Business Simplification programme is successful (see paragraph 7 below on plans to rationalise the number of local and national business support programmes for small businesses).

28. Supporting Small Business, Public Accounts Committee, conclusion 1.

29. Department of Trade and Industry Annual Report 2006-07, Paragraph 2.132.

30. Supporting Small Business, NAO, Figure 13, page 29.

31. Supporting Small Business, NAO, Paragraph 2.2.

32. Supporting Small Business, Public Accounts Committee, Paragraph 4.

- **PSA 6 (iii):** In the year ending December 2006, of the working age population living in the 15 per cent most deprived wards in England, 6.5 per cent were self-employed. This was the highest rate seen in the last six years. The Department, however, cautions that an adjustment for the effect of the economic cycle should be taken into account.
- **PSA 7:** The Department notes that it only has limited data on which to assess progress and that a full assessment of trends in regional economic activity and disparities cannot be fully determined until the current economic cycle is complete. According to the data that is available for 2002-2005 (see page 17, paragraphs 32 to 33 for weaknesses in the data), performance was mixed. The three Northern Regions, the East Midlands, South West and London improved on baseline performance, with the West Midlands maintaining baseline performance whereas the South East and East regions did not improve on their individual baseline trends. The Department has noted that the target is still very challenging.
- **PSA 8:** UKTI is on course to meet all five indicators underlying the PSA target. These include measures of the business success of new-to-export and established exporters that are assisted by UKTI, plus measures of inward investment. The Annual report states that '£65 million spent on four key UKTI trade development schemes generated £1.1 billion – in other words £17 of additional net benefit for each £1 of UKTI spend'.

NAO coverage

5 Over the last year the NAO has reported on the work of the Small Business Service.

Small Business Service

6 The Small Business Service was launched as an executive agency in April 2000. Since April 2007, it has relinquished its service delivery role, as most of these responsibilities have been devolved to regional delivery partners, and now operates as a policy unit within the Department itself; from July 2007 known

as the Enterprise Directorate. The Committee of Public Accounts endorsed this restructuring as the former Small Business Service had failed to convince it that it was contributing cost-effectively to the achievement of Government objectives for small business.²⁸

7 The Enterprise Directorate is the Government lead for developing and influencing policies which aim to encourage an enterprise culture and a business environment favourable to entrepreneurs, and small and medium sized firms. It also leads projects such as the Business Support Simplification Programme.²⁹ The Budget in March 2006 announced the Government's intention that the number of support programmes should be reduced from over 3,000 to 100. The Committee of Public Accounts recommended that the Department needs to take a firm lead by developing an action plan with milestones to achieve this objective.

8 The NAO findings on the Small Business Service will offer some guidance to the Enterprise Directorate as it moves forward:

- The Small Business Service needed to increase its influence in and outside Government. Sixty-eight per cent of Government respondents to our 2005 survey felt that SBS was not well-placed to set a Government-wide agenda on small businesses,³⁰ although it was considered to be a reliable source of information.
- The Small Business Service needed to improve its strategic planning. It had a very complex system of targets and objectives that didn't match clearly with the government objectives for small business.³¹
- The Small Business Service needed to get better at measuring its performance so as to demonstrate the value of its work. It has been difficult to isolate the impact of the Small Business Service from broader economic drivers. The Committee of Public Accounts found, for example, that the Small Business Service had not reported on progress, for example, against the Government Action Plan for Small Business published originally in January 2004.³²

Business Link

9 The Business Link service offers help and support to anyone running a business or thinking of starting a business. The strategy and funding for Business Link is set by the Department; it is administered and managed by the Regional Development Agencies. Our report on Supporting Small Business found that although historically the performance of Business Link Operators had varied in terms of volume and quality of service, customer satisfaction was high.³³

10 At the time of our report in May 2006, Business Link's performance measures were being reviewed to better capture the value added by the service. The Department's 2006-07 Annual Report states that the number of customers helped had risen to 792,741 in the 12 months ending March 2007 (an increase of more than seven per cent on the same period in the previous year and more than double the number helped five years before).

11 Business Link has also been successful in attracting customers to its web portal, businesslink.gov.uk.³⁴ Between April 2004 and March 2006 the Business Link web portal received over 15.4 million 'hits' – significantly above the target for that period of 12.9 million.³⁵ To set up the portal, the Department had, in our view, worked successfully to bring a number of public sector organisations together to pool information and take collective decisions for the benefit of the programme as a whole.

UK Trade & Investment

12 The Select Committee reported on the work of UK Trade and Investment and its new five year strategy in June 2007. The Committee supported many aspects of UK Trade and Investment's new sector strategies and its increased focus on emerging and high growth economies.

13 The Committee emphasised the importance it attached to UK Trade and Investment's ability to demonstrate the value it is adding through its work in these areas. Also, key to its commitment to becoming a more "client focused" organisation would be the development of the skills of its staff and greater charging for services. In both of these areas the Committee believed that UK Trade and Investment had the potential to be more ambitious and innovative.

14 The Committee registered concern over the role of the English Regional Development Agencies (RDAs) in promoting inward investment and, in particular, their presence overseas. It concluded that this was diluting the "UK brand" and confusing potential investors. The Department is addressing this by working with UK Trade & Investment and the RDAs to deliver, by April 2009, the bringing together of the management and branding of RDA and UKTI overseas activity."

15 The NAO expects to conduct a value for money examination of UK Trade and Investment in 2008.

33. Supporting Small Business, NAO, Paragraphs 6.6 & 6.9.
34. Delivering Successful It-enabled business change, NAO, page 17.
35. Supporting Small Business, NAO, Paragraph 6.20.

Areas the Committee may wish to explore

- Whether the assessment that PSA 7 is ON COURSE is accurate given that measurement is difficult and that the Department still feels that it is very challenging.
- The plan for establishing the Enterprise Directorate (formerly the Small Business Service) as a credible and influential policy centre within central Government.
- Progress in implementing the Business Support Simplification Programme.

36. Peer Review of Competition Policy, KPMG, June 2007.

Ensuring fair markets that are efficiently regulated

(Section 2.6, page 67, of the Annual Report)

16 The Department had three PSA targets related to its objective of ensuring fair markets that are efficiently regulated. Progress against these targets, as reported in the Department's annual report, is shown below.

PSA 3 – Competition and consumers

"Promote fair competitive markets by ensuring that the UK framework for competition and for consumer empowerment and support is at the level of the best by 2008, measuring the effectiveness of the regime through international comparisons, supported by a broader evidence base". **ON COURSE**

PSA 5 – Trade barriers

"Ensure that the EU secures significant reductions in EU and world trade barriers by 2008 leading to improved opportunities for developing countries and a more competitive Europe". A Joint target with the Department for International Development. **SLIPPAGE**

PSA 10 - Maximising potential in the workplace

"By 2008, promote ethnic diversity, cooperative employment relations and greater choice and commitment in the workplace, while maintaining a flexible labour market". **NOT YET ASSESSED**

17 The Department reports success in promoting competitive markets and slippage in significantly reducing trade barriers. There are significant challenges in assessing progress in these policy areas either because comprehensive data is unavailable or success depends on the actions of other parties. PSA 3 (competition and consumers) is an exception to this, as progress here is measured using timely evidence from stakeholder surveys.

- **PSA 3:** The Department's Annual Report offers a wide range of evidence to demonstrate current satisfaction levels with the UK competition regime. The Department has commissioned KPMG to carry out a series of Peer Reviews of Competition Policy, using a survey of expert commentators. The most recent review³⁶ found that the UK regime was ranked third behind the US and Germany, although it was closing the gap on those countries. In the Office of Fair Trading surveys in 2006, businesses awarded the UK a score of 7.4 out of 10 for the extent to which its markets are free from illegal practices and anti-competitive behaviour, while 78 per cent of consumers felt well protected and confident in using their rights. These results have now been consistent for three years.

There is evidence of the Department amending targets to align better with policy goals. For example, a number of Government initiatives relevant to consumer empowerment are underway, including the Unfair Commercial Practices Directive, the Consumer Credit Act 2006 and the Consumers, Estate Agents & Redress Act. The Department intends to consider possible indicators for assessing the level of consumer empowerment to be used to benchmark progress in these areas.

- **PSA 5:** Success in achieving significant reductions in trade barriers depends very much on influencing policy-makers in other countries. Any assessment of the quality of Departmental performance in this area must of necessity be highly subjective.
- **PSA 10:** In most cases, the baselines for the indicators that make up this PSA have only recently been established. The annual report states that data on progress will not be available until dates ranging from autumn 2007 to 2009.

NAO coverage

18 Our VFM reports on the theme of ensuring fair markets that are efficiently regulated have covered Regulatory Impact Assessments³⁷ and the Administrative Burdens Reduction Programme,³⁸ together with the role of the Small Business Service in helping reduce the burden on small businesses,³⁹ and the work of the Office of Fair Trading.⁴⁰

19 We have also reported on the creation of Ofcom;⁴¹ the work of Postcomm; and, the sale of the gas distribution network by Ofgem. The latter is covered in the section below on energy.

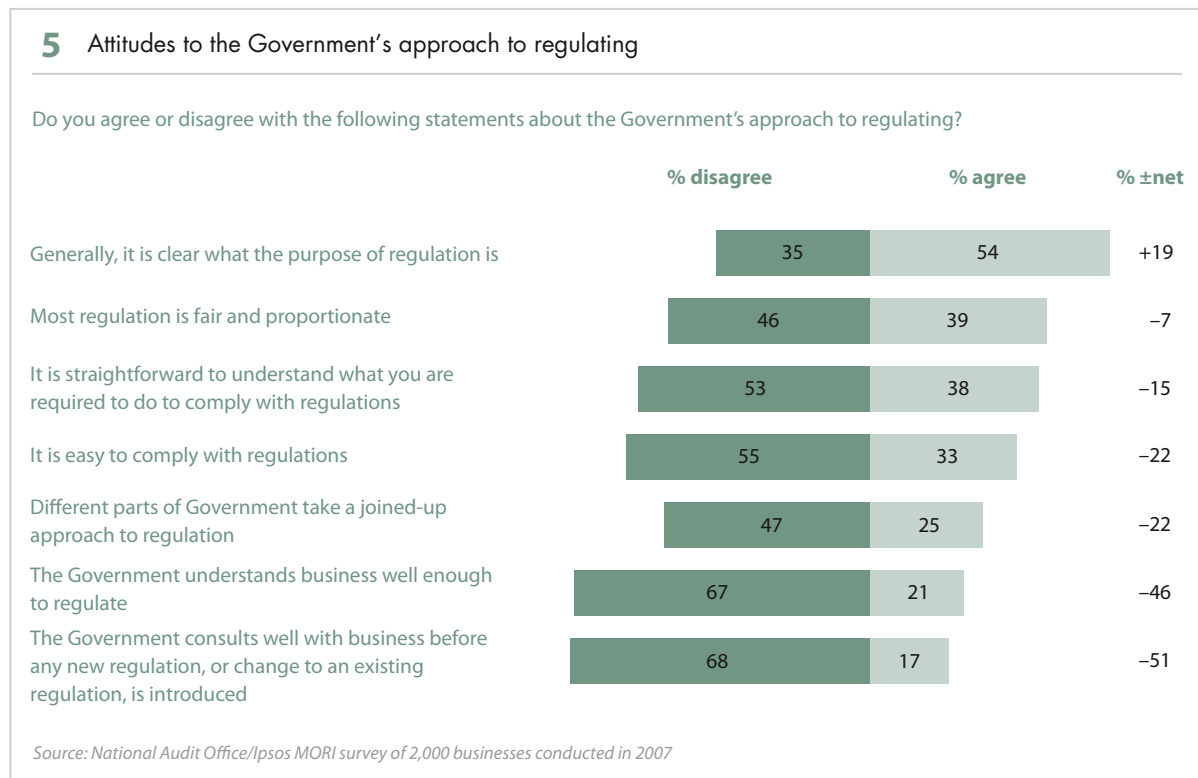
Reducing the regulatory burden

20 When regulations are implemented it is usually to overcome some form of market failure, but these benefits come with costs attached: when an organisation complies with a regulation there

are, usually, but not always, two costs. The first cost is of the compliance itself. The second cost is the administration this requires. The Government has set itself a target of reducing the second of these costs, which are termed Administrative Burdens.

21 The Department is responsible for a large share of the total administrative burden imposed by government; with the total estimated as some £20 billion at May 2005⁴², of which the former DTI accounted for £5.3 billion⁴³ (some 25 per cent). An NAO survey of businesses found that 60 per cent reported that the level of regulation (compliance and administrative costs) is an obstacle to business success, while three quarters say that Government does not understand business well enough to regulate it effectively.⁴⁴ More findings of this survey are shown in **Figure 5**.

37. Evaluation of Regulatory Impact Assessments 2005-06, NAO, June 2006.
38. Reducing the cost of complying with regulations: The delivery of the Administrative Burdens Reduction Programme, 2007, NAO, July 2007.
39. Supporting Small Business, NAO, May 2006.
40. The Office of Fair Trading – Enforcing competition in markets, NAO, November 2005.
41. The creation of Ofcom: Wider lessons for public sector mergers of regulatory agencies, NAO, July 2006.
42. Reducing the cost of complying with regulations: The delivery of the Administrative Burdens Reduction Programme, 2007, NAO, page 6.
43. Reducing the cost of complying with regulations: The delivery of the Administrative Burdens Reduction Programme, 2007, NAO, Figure 7, page 16.
44. Reducing the cost of complying with regulations: The delivery of the Administrative Burdens Reduction Programme, 2007, NAO, page 6, Paragraph 7.



45. Better Regulation Simplification Plan, DTI, December 2006.

46. Reducing the cost of complying with regulations: The delivery of the Administrative Burdens Reduction Programme, 2007, NAO, page 8.

47. Delivering Successful It-enabled business change, NAO, Paragraph 4.3.

48. Evaluation of Regulatory Impact Assessments 2005-06, NAO.

49. Evaluation of Regulatory Impact Assessments 2005-06, NAO, Paragraph 7.

50. Evaluation of Regulatory Impact Assessments 2005-06, NAO, paragraphs 1.9–1.10.

51. Evaluation of Regulatory Impact Assessments 2005-06, NAO, Appendix 2.

52. Supporting Small Business, PAC, Paragraph 8.

53. Supporting Small Business, NAO, Paragraph 3.2.

22 The Government has set a target to reduce the administrative burdens of regulation by 25 per cent by May 2010. The former DTI had already taken steps to reduce this regulatory burden. Indeed, better regulation is now even more of an imperative, as responsibility for the Better Regulation Executive – the body charged with minimising bureaucracy for businesses and front-line staff in the public sector – passed to the Department from the Cabinet Office on 28 June 2007. Steps to date include, for example:

- Focusing on those regulations that impose the highest administrative burdens on businesses. In December 2006, the Department announced initiatives to reduce the burden by 14 per cent of the baseline, equivalent to some £700 million of savings for business.⁴⁵ We noted that the benefits to business of the 25 per cent target are uncertain. As the Government has not measured the total cost of complying with regulation, the relative importance of reductions in administrative burdens is not known. It is important, therefore, that departments are not driven exclusively by the need to meet this target;⁴⁶
- appointing Ministerial Challenge Groups to challenge the need for regulation;
- asking senior civil servants to incorporate better regulation into their objectives;
- creating an IT tool to show policy makers how changes in regulatory design will impact on administration costs; and
- persuading local authorities to change Trading Standards procedures to facilitate the introduction of the Consumers Direct helpline.⁴⁷

23 Our 2005-06 report on Regulatory Impact Assessments (RIAs)⁴⁸ concluded that the Department was performing strongly compared to the three other departments examined in our study: the Home Office, the Department for Transport and the Department for Culture, Media and Sport. The Department was the most proactive in disseminating good practice and in providing robust challenge to the policy makers. It was the only Department which delivered consistently in four key areas: offering appropriate support and advice; making best use of in-house expertise; having staff skilled in data gathering; and improving accountability.⁴⁹

24 Nevertheless, the NAO report also concluded that there was still room for improvement in all the RIAs examined. Across all departments, the purpose of the assessment was not always understood and they were often done too late in the process to be of benefit.⁵⁰ RIAs tended to be informative rather than integrated into the policy-making process. The RIA, for example, on the proposals to increase the adult and development rates of the National Minimum Wage in 2005 and 2006 was intended more as a communication document rather than an evaluation of options.⁵¹

25 We found that the Small Business Service could do more to ensure that regulators consult with, and take account of, the specific needs of small businesses. Both the Confederation of British Industry (CBI)⁵² and the Federation of Small Businesses⁵³ felt, at the time of our report, that the Small Business Service had not delivered on regulation.

The Office of Fair Trading

26 Our report in November 2005 examined the work of the Office of Fair Trading (OFT) in enforcing competition in markets. It concluded that the OFT should focus on three areas of weakness: making best use of its resources; improving the management of investigations; and improving the measurement of its achievements and the communication of its work.

27 The subsequent Committee of Public Accounts Report⁵⁴ made ten recommendations on the OFT's priorities, management of investigations and economic impact. In its Treasury Minute of July 2006 the OFT accepted the Committee's findings and implemented an internal transformation programme to ensure it is able to rise to future challenges and maximise its positive impact.

The creation of Ofcom

28 Our report⁵⁵ examined the creation of Ofcom in December 2003 to see what wider lessons could be drawn for future mergers in the regulatory sector. It found that the creation of Ofcom was a major challenge demanding decisive leadership and well structured project management. There were, however, no clear measures put in place at the outset to monitor whether the merger was a success. Although data is limited, the NAO has carried out a preliminary assessment which indicates that the merger has delivered many of the benefits expected.

29 The findings are particularly pertinent to the final finding of the Hampton Review⁵⁶, that 31 national regulators should be reduced to seven more thematic bodies. Our report observed that more could have been done to establish a clear framework for measuring the costs and benefits of the new organisation:

- When the merger was planned, the Regulatory Impact Assessment did not include detailed objectives or a framework for measuring costs and benefits.⁵⁷ For example, Ofcom now estimates that it will make savings in areas such as IT (where it will more than halve operating costs by 2008-09) and staffing.⁵⁸
- There was also a lack of clarity around the set-up costs. We estimated these at £79.3 million, but the costs could potentially be much higher, as many elements, such as the opportunity cost of

diverting staff from operational work to winding down activities, were not recorded at the time or are virtually impossible to quantify in retrospect.⁵⁹

- Ofcom could better demonstrate its value by measuring the benefits it delivers for consumers, such as price, choice, innovation and satisfaction.⁶⁰

30 The strategic management of the merger was commended by industry stakeholders, who told us that they felt reasonably well informed throughout the merger and that there was only a limited period of uncertainty as the previous regulators wound down.⁶¹ However, we also found that not enough due diligence had been carried out on the five predecessor regulators. There should have been a greater focus on the requirements of Ofcom's public corporation status, the finances of the previous regulators and the suitability of existing staff to carry out new roles.⁶²

Postcomm

31 Our report on Postcomm, published in March 2006, examined developments in regulating the quality of service provided by the Royal Mail. Our report noted that the regulation of quality of service had been the least well developed part of Postcomm's role. A new regulatory regime for Royal Mail for 2006-2010 is intended to improve the level of consumer protection (for example, by covering mail delivered to both the wrong address and addressee), although it does not target delivery and collection times nor items of mail lost by Royal Mail. Our report concluded that there was scope to improve implementation of the new regulatory regime so as to further reduce the regulatory burden:

- Postcomm does not have all the information it needs to make decisions on quality of service levels. There is no information, for example, on the cost of Royal Mail increasing the reliability of transit times.

54. Office of Fair Trading, Enforcing competition in markets Public Accounts Committee, Forty-second Report. April 2006.

55. The creation of Ofcom: Wider lessons for public sector mergers of regulatory agencies, NAO, July 2006.

56. Reducing administrative burdens: effective inspection and enforcement, Philip Hampton, March 2005.

57. The creation of Ofcom: Wider lessons for public sector mergers of regulatory agencies, NAO, Paragraph 1.7

58. The creation of Ofcom: Wider lessons for public sector mergers of regulatory agencies, NAO, Paragraph 2.14.

59. The creation of Ofcom: Wider lessons for public sector mergers of regulatory agencies, NAO, Paragraph 1.10.

60. The creation of Ofcom: Wider lessons for public sector mergers of regulatory agencies, NAO, page 6.

61. The creation of Ofcom: Wider lessons for public sector mergers of regulatory agencies, NAO, Paragraph 2.13.

62. The creation of Ofcom: Wider lessons for public sector mergers of regulatory agencies, NAO, Paragraph 2.5.

- Postcomm should develop a framework for investigations that details the likely circumstances in which it would investigate shortfalls in performance, the range of information it would require, and standard responses to common issues.
- Postcomm should monitor the development of competition in the postal sector and prepare to withdraw from detailed regulation when competition becomes effective (for example, by establishing criteria for adding and removing products from the universal service).

Areas the Committee may wish to explore

- Stakeholder concerns that Government does not understand business well enough to regulate it.
- Ensuring that Regulatory Impact Assessments are done in a timely manner and in a way that influences the direction of policy.
- Whether enough consumer protection is afforded by the regulatory regime for Royal Mail.
- Whether the Department has taken forward the lessons learned from the creation of Ofcom, for example, in the merger of energywatch, Postwatch and the National Consumer Council.

Ensuring secure, sustainable and affordable energy

(Section 2.7, page 88, of the Annual Report)

PSA 4 Energy:

- i "Reduce greenhouse gas emissions by 12.5 per cent from 1990 levels in line with our Kyoto commitment and to move towards a 20 per cent reduction in carbon dioxide emissions below 1990 levels by 2010, through measures including energy efficiency and renewables." A joint target with the Department for Environment, Food and Rural Affairs and the Department for Transport; **ON COURSE**
- ii "Maintain the reliability of energy supplies"; **ON COURSE**
- iii "Eliminate fuel poverty in vulnerable households in England by 2010 in line with the Government's Fuel Poverty Strategy objective. Joint with the Department for Environment, Food and Rural Affairs"; **SLIPPAGE**
- iv "Ensure the UK remains in the top three most competitive energy markets in the EU and G7". **ON COURSE**

PSA 11 Nuclear Decommissioning Authority (NDA):

"Reduce the civil nuclear liability by 10 per cent by 2010, and establish a safe, innovative and dynamic market for nuclear cleanup by delivering annual two per cent efficiency gains from 2006-2007; and ensuring successful competitions have been completed for the management of at least 50 per cent of UK nuclear sites by end 2008"; **NOT YET ASSESSED**

32 The Department remains on course to deliver its security of supply and competitiveness targets, and the greenhouse gas components of the climate change target. It is finding meeting the carbon dioxide emissions and fuel poverty targets extremely challenging:

- **PSA 4 (i):** The annual report states that the UK is on track to meet its Kyoto Protocol target on greenhouse gas. Latest provisional estimates show that emissions in 2006 are 15 per cent below 1990 levels. The Department is finding the Carbon dioxide target more challenging, estimating that by 2010 emissions will be 16 per cent of the 1990 level, some four per cent behind target. This is, in part, due to higher than expected levels of economic growth, and a reliance on coal-fired electricity production as gas prices rise.

- **PSA 4 (ii):** The Department observes that the UK energy market is continuing to invest in new infrastructure; between 2006 and 2008 additional gas import capacity equivalent to some 70 per cent of Britain's annual consumption will come online. This will not prevent, however, gas supply shocks overseas affecting the UK. These risks grow as UK gas production dwindles.
- **PSA 4 (iii):** The number of households in fuel poverty in England was 1.2 million in the last progress report (using 2004 figures), one million of these households are vulnerable. Given the rise in fuel prices it is forecast that by 2006 some two million vulnerable households will be in fuel poverty. The Department has used many levers to combat fuel poverty, including the Warm Front Scheme and the Energy Efficiency Commitment. The main driver, however, is energy prices and this is outside its direct control.
- **PSA 4 (iv):** The Department cite the latest Oxera report on Energy Market Competition in Europe and the G7, published 2006, and based on preliminary 2005 data, which demonstrates that the UK has the most competitive gas and electricity markets in the sample. In spite of this level of competitiveness, energy prices in the UK in January 2007 were estimated to be only just below the European average (median).

33 PSA 11 is covered by the Department in its annual report under the section on assets and liabilities. It is included in the energy section of this paper for completeness.

- **PSA 11:** The efficiency gains component of this target is the only active element and this was reported to have been achieved by the NDA in 2005-06, a year early. This PSA target has been revisited as part of the Comprehensive Spending Review '07. There is now no PSA target directed at the NDA (see page 18, paragraphs 34 and 35).

34 The Trade and Industry Select Committee has reported on both local energy generation⁶³ and the Government's nuclear policy.⁶⁴

35 The Committee found that the Government could do more to encourage local energy generation, which could reduce carbon dioxide emissions. For example, Ofgem could ensure that local electricity generators received equitable treatment under the regulatory framework. The Committee was also concerned that the Department was not committing enough resources to supporting research and development of the microgeneration industry.⁶⁵ Although local energy has the potential to help reduce carbon dioxide emissions, the Committee cautioned that it was important not to ignore the value of energy efficiency measures in cutting emissions, especially in the short term. Given the high set-up costs for local energy technology, they were also unsure how it would help to reduce fuel poverty.

36. The Committee noted that nuclear policy has an important bearing on carbon emissions. The nuclear industry, however, felt that the current planning and licensing systems are a significant deterrent for investment in new nuclear power stations in the UK.⁶⁶ The Committee were concerned that the poor history of dealing with the disposal of spent fuel would dissuade both the nuclear industry and the public from wanting to build new nuclear reactors. There is still a great deal of uncertainty about the size of the civil nuclear liability, with the Committee expecting the overall quantified costs of £70.2 billion (undiscounted) to rise significantly as further investigative work is done at the most difficult sites.⁶⁷

63. Local energy – turning consumers into producers, House of Commons Trade and Industry Committee, January 2007.

64. New nuclear? Examining the issues, House of Commons Trade and Industry Committee, July 2006 & The Work of the NDA and UKAEA, House of Commons Trade and Industry Committee, July 2006.

65. Local energy – turning consumers into producers, House of Commons Trade and Industry Committee, conclusion 27.

66. New nuclear? Examining the issues, House of Commons Trade and Industry Committee, conclusion 11.

67. The Work of the NDA and UKAEA, House of Commons Trade and Industry Committee, conclusion 1.

68. The office of gas and electricity markets: Sale of gas networks by National Grid, NAO, February 2006.

69. Warm Front: Helping to Combat Fuel Poverty, NAO, June 2003 & Ofgem: Social Action Plan and Household Energy Efficiency, NAO, July 2004.

70. The restructuring of British Energy, NAO, March 2006.

71. The Office of Gas and Electricity Markets: Sale of gas networks by National Grid, NAO, Paragraph 1.

72. The Office of Gas and Electricity Markets: Sale of gas networks by National Grid, NAO, 1.10.

73. The Office of Gas and Electricity Markets: Sale of gas networks by National Grid, NAO, Paragraph 1.11.

74. The Office of Gas and Electricity Markets: Sale of gas networks by National Grid, NAO, Paragraph 2.5.

75. Gas distribution networks: Ofgem's role in their sale, restructuring and future regulation, PAC, conclusion 9.

76. Gas distribution networks: Ofgem's role in their sale, restructuring and future regulation, PAC, conclusion 6.

77. The Office of Gas and Electricity Markets: Sale of gas networks by National Grid, NAO, recommendation M, Page 8.

78. Gas distribution networks: Ofgem's role in their sale, restructuring and future regulation, PAC, Paragraph 38.

NAO coverage

37 Our recent VFM reports on the theme of Ensuring secure, sustainable and affordable energy have covered the sale of gas distribution networks by National Grid⁶⁸, tackling fuel poverty⁶⁹, and the restructuring of British Energy.⁷⁰

38 The NAO is currently examining the contracts put in place by the Nuclear Decommissioning Authority to take forward decommissioning since it was set up in April 2005. We expect to publish a report early next year.

Sale of gas distribution networks

39 The Office of Gas and Electricity Markets (Ofgem) cannot, itself, deliver consumer benefits but it must create a robust regulatory framework that provides incentives to encourage innovative and efficient behaviour by regulated firms. For a domestic customer, the cost of gas distribution amounts to approximately £80 a year, which represents the second largest component (some one fifth) of the average gas bill after raw product.⁷¹ We examined how far Ofgem had protected the interests of consumers via its approval of the sale of four of the eight regional gas distribution networks by National Grid plc in June 2005.

40 Our report identified many examples of good practice in the way that Ofgem handled the sales:

- On the sale of gas networks, Ofgem and DTI worked closely together, drawing on Ofgem's expertise;⁷²
- Ofgem sought to be helpful without compromising its independence, for example, by helping bidders and potential bidders to understand the regulatory framework;⁷³
- Ofgem established detailed risk and issue registers at an early stage and updated them regularly; and⁷⁴
- Ofgem had made a timely start to developing a robust reporting framework for collecting information on the costs and performance of the new network owners.

41 The NAO report and the subsequent report from the Committee of Public Accounts highlighted key lessons for the future. On securing benefits for consumers:

- Ofgem delayed its existing gas distribution price control review by one year to March 2008, thereby deferring the possibility of bringing early benefits to consumers. It should consider more carefully the costs and benefits of extending the future duration of price controls by quantifying the consequences of such decisions in terms of the likely impact on prices.⁷⁵
- Ofgem estimated the potential for cost savings of £830 million across the gas networks between 2008 and 2023, regardless of whether the sales proceeded. The Committee of Public Accounts has recommended that Ofgem should make clear to the owners of gas networks that it intends to set a challenging price control in 2008, using efficiency savings of at least three per cent per year as a starting assumption.⁷⁶
- Ofgem should continue its research into the regulatory implications of gearing⁷⁷, for example: whether highly-g geared gas distribution companies, which have financed the purchase of the networks largely via debt, are able to meet new investment requirements, such as extending gas networks to rural areas they do not currently serve, and replacing 'at-risk' iron gas pipes with more robust plastic pipes.⁷⁸

42 On handling structural change such as sales and mergers:

- As part of its sales approval process, Ofgem introduced unnecessary additional changes to the way gas networks operate. Ofgem subsequently decided to defer these reforms, known as gas exit reforms, until at least September 2007. On future projects, it should be confident that its proposed tasks are central to the fulfilment of its objectives and, therefore, that the regulatory burden imposed on the industry is justified.⁷⁹

Tackling Fuel Poverty

43 The Government aims to eliminate fuel poverty among vulnerable groups by 2010. One method of achieving this aim is to promote energy efficiency in vulnerable households via schemes such as Warm Front and the Energy Efficiency Commitment, the latter administered by Ofgem. These initiatives include the installation of insulation and other energy efficiency measures in the homes of eligible people.

44 The Committee of Public Accounts has been concerned that the schemes do not always target those most in need⁸⁰, or achieve their intended outcomes.⁸¹ In response to these, and other conclusions by the Committee:

- The Department for Environment, Food and Rural Affairs agreed to continue to look for ways to improve targeting and to maximise the proportion of those receiving assistance who are fuel poor.⁸²
- Ofgem agreed in principle that there should be a national campaign to stimulate consumer demand for energy efficiency measures, but noted that it could only undertake this type of campaign with additional funding.⁸³

British Energy

45 British Energy was privatised in 1996. In 2002, following a fall in electricity prices, the company applied to the Department for financial assistance. In November 2002, the Department agreed to provide financial assistance on condition that the Company's financial arrangements be restructured.

46 Our report, published in March 2006, concluded that the Department is now in a stronger position to monitor British Energy as it has better access to its financial information. The Government has taken responsibility for underwriting a large and uncertain nuclear liability (including spent fuel and decommissioning liabilities), recently valued at £5.3 billion.⁸⁴

47 In reality, these liabilities would have fallen to the Government in the event of British Energy's liquidation. However, no attempt had been made to estimate the potential size of these liabilities between privatisation in 1996 and the restructuring. Under the restructuring agreement, the Company is now required to produce estimates at not more than five-year intervals.

48 Our report recommended:

- The Department, working with the NDA, should consider whether alternative arrangements would provide British Energy with a stronger incentive to reduce the liabilities of the Nuclear Liabilities Fund.
- The Department needs to address Health and Safety Executive concerns about the way in which the regulatory regime would operate if the company went into liquidation. There were, for example, concerns that a liquidated company would have insufficient funds and perhaps insufficient experienced staff to make any changes necessary to meet health and safety requirements.⁸⁵

79. Gas distribution networks: Ofgem's role in their sale, restructuring and future regulation, PAC, conclusion 2.

80. Warm Front: Helping to Combat Fuel Poverty, PAC, conclusion 1.

81. Ofgem: The Social Action Plan and Energy Efficiency Commitment, PAC, conclusion 5.

82. Treasury Minute on the fifth, ninth and tenth reports from the Committee of Public Accounts, Session 2003-2004, April 2004.

83. Treasury Minutes on the tenth, eleventh and thirteenth reports from the Committee of Public Accounts, Session 2004-05, July 2005.

84. The restructuring of British Energy, PAC, conclusion 1.

85. The restructuring of British Energy, NAO, Paragraph 2.3.

49 The Public Accounts Committee published a report in July 2007 and a Treasury Minute followed in October 2007. The Treasury Minute observed that since our report and the Committee hearing (also March 2006):

- The Department has undertaken competitive tenders for two pieces of external advice on the conversion and sale of shares in British Energy;
- The Department has converted and sold (in June 2007) 450 million shares in British Energy, thereby diversifying the assets of the Nuclear Liabilities Fund (the Government-owned Fund established to meet British Energy's nuclear liabilities);
- Work is underway to provide more frequent updates on the estimated cost of British Energy's liabilities than took place before restructuring; and
- The Department said it had worked with the Health and Safety Executive to consider the need for a Special Administration Regime and concluded that the risk of an administrator being in a position to act against the wishes of regulators is negligible, but it will continue to review periodically whether such a Regime is needed.

Areas the Committee may wish to explore

- The Department's long term approach to resolving the issue of fuel poverty.
- The Department's long term approach to improving security of supply in the gas market.
- Progress in measuring the size of the nuclear decommissioning liabilities.

Public Service Agreement Targets extant in 2006, the Department's view on its performance, and the page reference in the annual report

Spending Review 2004 Target	Performance	Page
1 Productivity: Raise the rate of UK productivity, improve competitiveness and narrow the gap with competitors – a joint target with HM Treasury (HMT).	On Course	20
2 Science & Innovation: Improve the relative performance of the UK research base and increase the overall innovation performance of the economy.	On Course	26
3 Competition & Consumers: Promote fair competitive markets.	On Course	70
4 Energy: Lead work to deliver the goals of the Government's energy policy:		
a reduce greenhouse gas and carbon dioxide emissions (with the Department for Environment, Food and Rural Affairs (Defra) and the Department for Transport (DfT));	On Course	90
b secure energy supplies;	On Course	
c eliminate fuel poverty (with Defra); and	Slippage	
d ensure competitive energy markets.	On Course	
5 Trade Barriers: Ensure that the EU secures significant reductions in EU and world trade barriers.	Slippage	72
6 Enterprise: Build an enterprise society in which small firms of all kinds thrive and achieve their potential.	Slippage	47
a An increase in the number of people considering going into business.	On Course	
b An improvement in the overall productivity of small firms.	On Course	
c More enterprise in disadvantaged communities.		
7 Regional Economic Performance: Make sustainable improvements in the economic performance of all the English regions, and reduce the gap in growth rates between them. This is a joint target with Communities and Local Government.	On Course	53
8 UK Trade & Investment: Improve the business performance of UK Trade & Investment's (UKTI's) international trade customers and maintain the UK as the prime location in the EU for foreign direct investment. This is a joint target with the Foreign and Commonwealth Office (FCO).	On Course	64

Spending Review 2004 Target	Performance	Page
9 Gender Equality: Bring about measurable improvements in gender equality.	This target has transferred to DCLG	304
10 Maximising Potential in the Workplace: Promote ethnic diversity, cooperative employment relations and commitment in the workplace, whilst maintaining a flexible labour market.	Not yet assessed	77
11 Nuclear Decommissioning Authority: Reduce the UK's civil nuclear liability by 10 per cent by 2010 and establish a safe, innovative and dynamic market for nuclear clean-up.	On Course	105

Recent reports on departmental activity

On Value for Money

Reducing the cost of complying with regulations: The delivery of the Administrative Burdens Reduction Programme, 2007, August 2007

The compensation scheme for former Icelandic water trawlermen, June 2007

Mind the Gap: Tackling Disparities in Regional Economic Performance, February 2007

The creation of Ofcom: wider lessons for public sector mergers of regulatory agencies, July 2006

Evaluation of Regulatory Impact Assessments 2005-06, June 2006

Supporting Small Business, May 2006

The Restructuring of British Energy, March 2006

The Closure of MG Rover, March 2006

Re-opening the post: Postcomm and the quality of mail services, March 2006

The Office of Gas and Electricity Markets: Sale of gas networks by National Grid, February 2006

The Office of Fair Trading – Enforcing competition in markets, NAO, November 2005














On Financial Accounts











Design Council, 2005-06

Companies House, 2006-07

Insolvency Service, 2006-07

Results of the review of PSA target data systems

Key	PSA Target	Description	Rating
 Fit for purpose	1	PRODUCTIVITY – Demonstrate further progress by 2008 on the Government’s long-term objective of raising the rate of UK productivity growth over the economic cycle, improving competitiveness and narrowing the gap with our major industrial competitors. (Joint with HM Treasury)	 
 Broadly appropriate	2	SCIENCE AND INNOVATION – Improve the relative international performance of the UK research base and increase the overall innovation performance of the UK economy, making continued progress to 2008, including through effective knowledge transfer amongst universities, research institutions and business.	
 Not fit for purpose		World class research at the UK’s strongest centres of excellence.	
 Too early to form a view or not established		Sustainable and financially robust universities and public laboratories across the UK.	
		Greater responsiveness of the research base to the needs of the economy and public services.	
		Increasing business investment in R&D, and increased business engagement in drawing on the UK science base for ideas and talent.	
		A more responsive supply of science, technology, engineering and maths skills to the economy.	
	3	COMPETITION & CONSUMERS – Promote fair competitive markets by ensuring that the UK framework for competition and for consumer empowerment and support is at the level of the best by 2008, measuring the effectiveness of the regime through international comparisons, supported by a broader evidence base.	
		The UK framework for competition....is at the level of the best by 2008...	
		Consumer empowerment and support is at the level of the best by 2008...	

PSA Target	Description	Rating
	Maintain the UK as the prime location in the EU for foreign direct investment.	
9	GENDER EQUALITY – By 2008, working with other departments, bring about measurable improvements in gender equality across a range of indicators, as part of the Government’s objectives on equality and social inclusion. (Transferred to DCLG)	Assessed by DCLG
10	MAXIMISING POTENTIAL IN THE WORKPLACE – By 2008, promote ethnic diversity, cooperative employment relations and greater choice and commitment in the workplace, while maintaining a flexible labour market.	
	Raising the self-employment rate of under-represented ethnic minorities, relative to that of other groups.	
	Reducing the incidence of racial discrimination at work reported by ethnic minority employees.	
	Maintain and improve the overall level of UK labour market flexibility.	
	There is a statistically significant increase in the number of employees that have information and consultation procedures.	
	There is a statistically significant increase in the number of economically active people of working age who feel well or very well informed about their rights at work.	
11	NUCLEAR DECOMMISSIONING AUTHORITY – Reduce the civil nuclear liability by 10 per cent by 2010, and establish a safe, innovative and dynamic market for nuclear cleanup by delivering annual 2 per cent efficiency gains from 2006-07; and ensuring successful competitions have been completed for the management of at least 50 per cent of UK nuclear sites by end 2008.	
	Reduce nuclear liabilities by 10 per cent by 2010.	
	Deliver annual 2 per cent efficiency gains from 2006-07.	
	Establishing a safe, innovative and dynamic market, ... ensuring successful competitions have been completed for the management of at least 50 per cent of UK nuclear sites by end 2008.	
Standard	Maintaining the UK’s standing as one of the best places in the world for online business .	

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