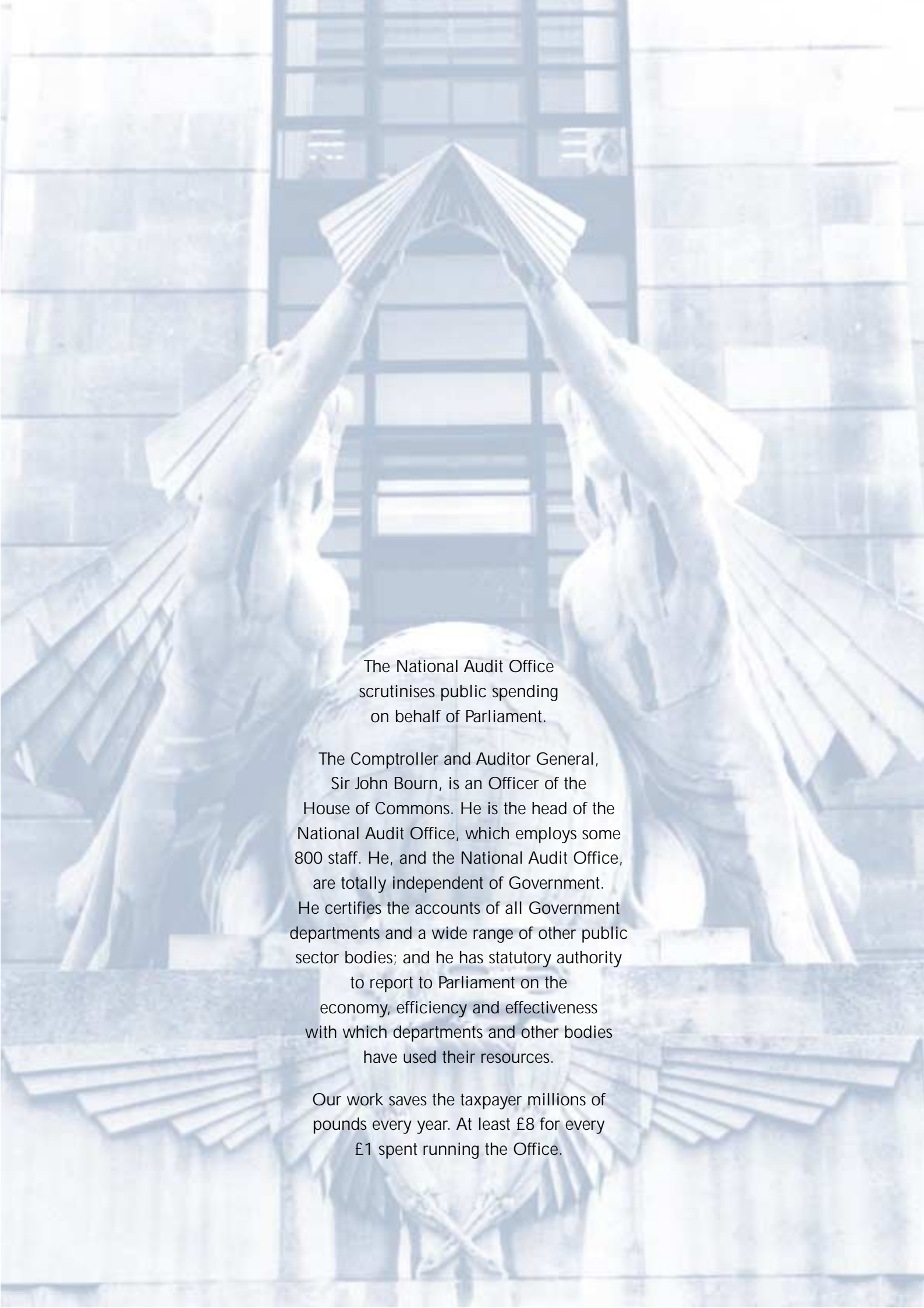


The Office of Telecommunications:
Helping consumers benefit from competition
in the telecommunications market

REPORT BY THE COMPTROLLER AND AUDITOR GENERAL
HC 768 Session 2002-2003: 11 July 2003





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This report has been prepared under Section 6 of the National Audit Act 1983 for presentation to the House of Commons in accordance with Section 9 of the Act.

John Bourn
Comptroller and Auditor General

National Audit Office
1 July 2003

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executive summary

- 1 The telephone is an integral part of modern life in the United Kingdom and 92 per cent of households have a fixed line telephone. Although the range of telecommunication services has increased in recent years, such as mobile telephones, consumers spent some £7 billion on residential fixed line services in 2002. BT Group plc (BT), the former monopoly supplier, received 70 per cent of this expenditure and is dominant in the market.
- 2 Under the Telecommunications Act 1984 the Director General of Telecommunications, who is the head of the Office of Telecommunications (Of tel), has a duty to promote the interests of consumers in respect of the prices charged for and the quality and choice of telecommunications services. Of tel aims to ensure that consumers get the best value for money and seeks to achieve this primarily by promoting competition. This is supported by regulatory action where, for example, competition is insufficiently established or would not result in basic affordable services for all. Of tel's regulatory action includes facilitating access to BT's network for its competitors, price controls to limit tariff increases, or reduce tariffs over time, and the requirement to provide geographically uniform prices for basic services¹.
- 3 We examined two aspects of Of tel's work that are intended to help consumers benefit from competition in the fixed line market:
 - **Raising consumers' awareness of the choices available to them and how to take up the benefits** (Part 1 of this Report). Many consumers are not taking up the potential benefits from competition in the fixed line telecommunications market. Consumers are ultimately responsible for deciding which telecommunication services to purchase, and from whom. Although suppliers take steps to inform consumers of their own offerings, the market is complex, and Of tel has a more general role in helping to ensure that consumers are aware of the choices available to them and the factors they should take into account in reaching a decision.
 - **Stopping and deterring anti-competitive behaviour** (Part 2). There is a risk that suppliers might take advantage of their position in the telecommunications market. Anti-competitive behaviour can be detrimental to consumers, in the form of higher prices and less choice, and to competing companies, who might be driven out of the market or suffer reduced income. Of tel therefore investigates all complaints of anti-competitive behaviour and other licence breaches, and where appropriate takes action, both informally and through legal enforcement measures.
- 4 Our methodology is at Appendix 1. When considering our specific recommendations, Of tel will need to advise the Office of Communications (Of com), which is due to take over Of tel's functions in December 2003, on any longer term action.

¹ National Audit Office report 'Pipes and Wires', April 2002 (HC723/2001-02): Figure 23.

Helping consumers take up the benefits of competition

5 Our main findings are:

- Consumers need to be well informed to benefit fully from competition. In any market, there is a risk that suppliers' actions alone cannot be relied upon to generate sufficient market awareness to meet the needs of consumers. This risk is significant in the telecommunications market where many consumers are not fully aware of alternative ways of buying telecommunication services. Although some consumers will have good reasons for not choosing the best deal in terms of price, others may be missing savings which they would enjoy if they were better informed.
- Suppliers and other consumer organisations have an interest in raising consumers' awareness of the issues to be considered in choosing a supplier. Oftel, however, has a particular interest in view of its policy of encouraging the development of effective competition, especially as it seeks to move away from direct regulation of consumer prices towards placing reliance on the effective operation of the market to protect the interests of all consumers. It recognises this by making 'well informed consumers' one of its main objectives.
- Since competition was introduced into telecommunications, the markets for gas and electricity have opened up to competition. Oftel's objective and approach have been less pro-active than Ofgem and *energywatch*, the regulator and consumer protection body for gas and electricity, which have frequently encouraged consumers to consider switching supplier. Oftel considers the markets to be substantially different in that in telecommunications there is a much wider range of services and tariffs than in the other utilities and it has more in common with service industries. It believes that differences in the nature of the market, rather than the regulator's approach, can explain differences in the rate of switching by consumers. For example, where consumers have access to a cable service (some 60 per cent of UK households) the level of switching is similar to that in the gas and electricity markets.
- A distinctive feature of the telecommunications market is that the majority of consumers are not well motivated to make changes and are not prepared to switch to an unknown supplier with an unfamiliar brand. Oftel's research has shown that in the residential fixed line market, only BT has a strong brand image and that customers may not trust alternative suppliers. The effort involved in switching may also dissuade consumers from exercising their choice.
- An important feature of an effectively competitive market is access to reliable and good quality information which consumers can use with confidence to make choices between competing offers. Many consumers are not aware of important features of the market, such as indirect access operators, though regular international callers, who are likely to benefit most from this service, do have greater awareness. It is not straightforward for Oftel to measure the adequacy of the information in the telecommunications market and whether existing levels are sufficient to prevent market failure. We found that although consumers can make savings, these are not uniform and are limited to certain areas. It is not easy to identify which consumers can benefit and to quantify the level of savings available. Oftel's starting point is to encourage suppliers and third parties to provide consumers with relevant information and to develop approaches to supplement this information on the basis of its research.





- Oftel has for many years undertaken extensive research into the behaviour of telecommunications consumers, supplemented by less frequent in-depth studies of consumer motivation and preferences. This research has been high quality. Oftel has recognised that this research by itself has not enabled it to make fully informed judgments on the extent to which it should supplement the information already available in the market. During 2002 it therefore sought to develop approaches to profile groups of consumers across the market and to identify and quantify the extent of any detriment that these consumers experience.
- Suppliers offer a wide range of tariffs and discount schemes and we found that it is difficult for consumers to calculate which tariff, from which supplier, would amount to the best deal or an improvement on their existing service. To make a fully informed decision, consumers would need a detailed breakdown of their call profile (the number, type, duration and timing of calls made) which none of the suppliers routinely provide. Suppliers would incur costs in providing such information which would not necessarily be justified by the benefits. Oftel has encouraged the development of price comparison services and endorsed www.phonebills.org.uk which provided a comparison of both direct and indirect access prices. While the participating companies accounted for the majority of revenue in the market, the number of firms represented was disappointing. It was discontinued at the end of 2002 in the light of the development of alternative price comparison sites. Oftel has developed an accreditation scheme to help build consumer confidence in such services. Oftel accredited the first company, *uSwitch.com*, in June 2003. The accredited schemes may, as with the 'phonebills' site, also experience difficulties in obtaining information from suppliers, although the *uSwitch.com* site includes over 20 companies.
- Oftel uses various methods of distributing information to consumers. During 2002 it began to use new, targeted outlets for distributing hard copies of its consumer guides, rather than relying on libraries and offices of Citizens Advice Bureaux and local trading standards services. Oftel also uses the media, especially local radio, as a way of obtaining free publicity for its consumer information. It has also improved its website.
- Oftel has sought to remove barriers to switching supplier. For example, its introduction of number portability enables consumers to keep their telephone number when changing supplier. Oftel is also working to lower the perceived risks of switching by playing a leading role in the setting up of the Telecommunications Ombudsman Service.
- We identified several areas of the market where there might be scope for targeting consumer information. The new approach to research that Oftel has developed has been accompanied by a re-focusing of its efforts, from late 2002, on more sophisticated targeting of information on different groups of consumers, based on its analysis of detriment and potential savings. It hopes that this approach, announced formally in April 2003, will also enable more rigorous evaluation of the impact of its initiatives.

- 6 In summary, Oftel has recognised that in working towards its objective of having 'well informed consumers' it needs to have a better understanding of the underlying drivers of consumer behaviour and to target its resources on improving consumer information. It, and in due course Ofcom, need to build on the useful initial steps that Oftel has already taken to use its 'leverage' as a regulator to encourage initiatives to improve information from within the industry and to provide supplementary sources of information where appropriate, while ensuring that it makes best use of its resources.

- 7 The Chief Executive of Ofcom has stated that Ofcom will be a 'reaching out' regulator that embraces consumer protection through the promotion of effective competition and choice. We consider that the following recommendations, most of which should be relevant to Ofcom as it begins to formulate its own strategy in detail, will be important in helping to achieve this. **Oftel and Ofcom should:**



- **Develop a fuller understanding of the needs and motivations underlying consumers' behaviour** by developing Oftel's existing programme of research work into a more systematic review of the drivers of consumer behaviour. This should build on the survey work we undertook in examining the subject. Oftel should feed the results of its research into its analysis of consumer detriment and its targeting of information. The research should include such factors as geographical location, age and ethnic group.
- **Complete and maintain Oftel's assessment of the extent of detriment suffered by consumers through a lack of information**, and hence identify the opportunities for consumers to make savings or to get more for their money and the types of consumer that can take advantage of these potential benefits. This work should enable it to assess better the need for regulatory intervention and to prioritise resources. Oftel or Ofcom could consider extending this work to include small and medium sized businesses, further sub-dividing residential consumer profiles to aid targeting, and measuring other forms of detriment beyond that arising from a lack of price transparency.
- **Provide, where appropriate, more practical guidance that reaches the consumers it is targeting**, as part of its consumer information strategy. For competition to be effective, Oftel and Ofcom need to actively encourage consumers to think about the way they buy their telecommunication services. In doing so it is important to target more precisely its consumer information initiatives to help ensure that the groups most likely to benefit from these initiatives are reached by way of the most effective communication channels. Oftel and Ofcom should also ensure that the results of its evaluation of the impact of its consumer information work are reflected in revisions to its strategy.
- **Consider how to make it easier for consumers to make choices in the fixed line market**, in particular by:
 - assessing whether the benefits to customers seeking to compare tariffs of having available their detailed call profile are proportionate to the costs of requiring or incentivising suppliers to provide the profile;
 - actively promoting changes to, or the interpretation of, EU legislation that would facilitate the inclusion by tariff and service comparison websites of a wide range of suppliers, and encouraging links between price and service quality sites that provide consumers with a 'one stop' service.

Stopping and deterring anti-competitive behaviour

8 Our main findings are:

- There are risks that the behaviour of telecommunications suppliers may work against competition in the market or be anti-competitive. Oftel is aware of these risks. It initiates its own investigations of potential anti-competitive behaviour and resolves disputes between companies, which may involve allegations of anti-competitive behaviour. In the two years to June 2002, Oftel conducted 187 investigations and found grounds for action in 62 cases (33 per cent), showing the value of such investigations in improving the competitiveness of the market.
- The proportion of investigations initiated by Oftel has fallen since the Committee of Public Accounts last reported in 1998. Oftel considers complaints to be the best indicator of anti-competitive behaviour. In Oftel's view this approach reflects its policy of responding directly to concerns from BT's competitors and of giving more importance to its statutory *duty* to resolve complaints referred to it than to using its statutory *powers* to undertake investigations on its own initiative. This is in line with its commitment to proportionate and targeted regulation. Oftel uses its awareness of market developments and trends in complaints to decide which investigations to initiate.
- Oftel took formal action in 19 of the 62 cases where it found grounds for regulatory action and made Directions and Determinations requiring a particular course of action. It did not make any Orders, which give rights to third parties to claim damages. Nor did Oftel use the stronger remedies available to it under the Competition Act 1998 as it had not found any behaviour that it judged sufficiently serious to justify such action. For the remaining cases, Oftel considered that the matter could be resolved voluntarily (for example, by the company concerned taking an agreed course of action).
- In deciding how to monitor a company's compliance with agreed enforcement action, Oftel makes decisions on a case by case basis depending on the type of action and the risk of non-compliance. Where Oftel considers that there is a risk that the problem will persist, it keeps the case under review and establishes monitoring criteria. Its Compliance Monitoring Unit, set up in April 2000 to strengthen monitoring arrangements, oversees all cases under review. Of the 62 cases where Oftel found grounds for regulatory action, 11 were reviewed in this way.
- Oftel set out in its 2001 Annual Report some types of behaviour it described as anti-competitive behaviour that had persisted from the previous year, but it has not provided an overall assessment of what it has achieved in investigating and stopping such behaviour.
- Oftel has accepted that it needs to speed up its investigations to meet the requirement of a new EU Directive, effective from July 2003, which requires all disputes under the Directive, except in exceptional circumstances, to be completed in four months. For investigations completed in the two year period July 2000 to June 2002, Oftel took, on average, just over six months to complete an investigation, an increase of four weeks (17 per cent) since we last reported on this matter. Significant delays occur during investigations because of re-assignment of cases (due to staff changes), insufficient case planning and management, and delays in receiving expert advice. Oftel took positive, and apparently effective, action to address these issues through changes to its management structure and systems. Performance information from the second half of 2002 shows that, despite opening more cases, the number of investigations taking more than four months fell from 56 per cent to 40 per cent.

- Oftel's internal assessment of the quality of its investigations, that 56 per cent of those completed in the two year period July 2000 to June 2002 were 'good' or 'very good' is supported, in broad terms, by the results of our survey of the companies involved. The companies that responded did not necessarily agree with the outcome of the investigation, and their views on the overall quality of investigations were very mixed, but two thirds of respondents considered that Oftel understood the main issues and that its investigations were thorough.

9 There is scope for Oftel to build on its improvements in stopping and deterring anti-competitive behaviour and to strengthen further its management in this area. Our specific recommendations, which should in due course be applicable also to Ofcom, are:



- **Keep under review the need for a more formal strategy for initiating investigations of potentially anti-competitive behaviour.** Ofcom, which will be a much larger organisation with more varied responsibilities, may have a greater need for a strategy. Oftel and Ofcom should, in addition to their existing activities, therefore consider initiating an internal overview, say every three months, by key staff engaged in identifying and investigating anti-competitive behaviour to identify new risks as telecommunications markets evolve. It is important that their approach provides a strong message to suppliers that anti-competitive behaviour will be quickly identified and rooted out.
- **Ensure that the latest changes in the handling of complaints and management of investigations enable it to complete investigations within four months.** Oftel should formally assess its progress in meeting the new target in August 2003 (once the Directive has taken effect) and again in April 2004 (12 months after the revised arrangements should have taken full effect).
- **Carry out each year a fuller overview of its work in identifying, deterring and stopping anti-competitive behaviour** to provide Oftel senior management with the assurance they need that Oftel is achieving its objectives. The assessment should identify trends in types of anti-competitive behaviour, set out how Oftel's investigations have progressed and how effective its enforcement action has been. It would help regulatory transparency if this assessment were published in its annual report.



Part 1

Helping residential consumers take up the benefits of competition

- 1.1 This report focuses on the residential sector of the United Kingdom fixed line telecommunications market, where BT Group plc (BT) is still the dominant company with over 70 per cent, by value, of market share. Residential consumers spent some £7 billion on fixed line telephone services in 2002. **Figure 1** shows relative expenditure on each type of charge and a breakdown by call type.
- 1.2 Individual households spend, on average, some £310 each year on fixed line telecommunications, though this masks significant variations by individual consumers. For example, the cost of line rental exceeded call costs for almost half of consumers. In addition, the expenditure

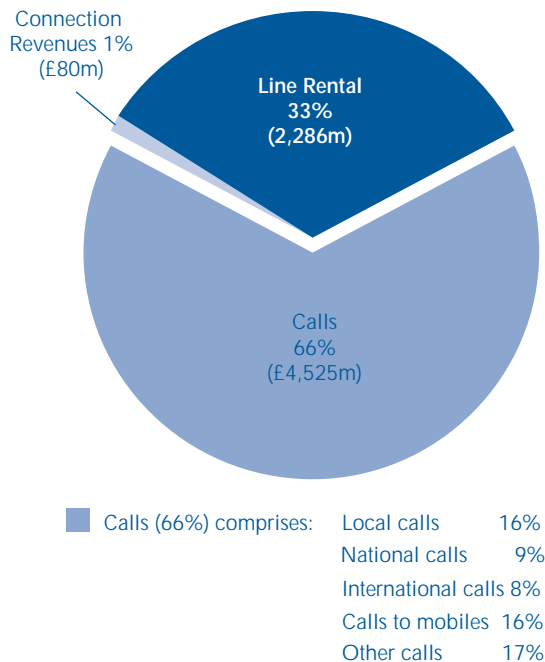
breakdown does not necessarily reflect actual usage, in terms of the number of calls made and their duration, as the cost of different call types can vary significantly.

- 1.3 Most residential consumers have a choice of three types of fixed line telephone service: the original (mostly BT) network; one of two cable networks that provide television and telecommunication services²; and over 200 indirect access operators (independent companies that provide a retail service to consumers by purchasing wholesale network capacity from network owners³).

- 1.4 Part 1 of this report examines what the Office of Telecommunications (Of tel) has been doing to help consumers make informed choices. It also considers why many consumers are still not taking up the potential benefits from competition in the telecommunications market. Of tel's work to prevent anti-competitive behaviour is covered in Part 2.

- 1.5 Appendix 1 explains our methodology. The two main elements for Part 1 are an analysis of telephone tariffs to identify ways that consumers can save money (Appendix 2) and an analysis of consumer preferences and experiences based on an omnibus survey we commissioned of 2,100 adults in the United Kingdom (Appendix 3).

1 Breakdown of expenditure by residential consumers on fixed line telephone services for 2002



Source: Of tel's Market Information Fixed Update: December 2002

Of tel aims to obtain the best deal for consumers, primarily through promoting competition

- 1.6 The Director General of Telecommunications, who is the head of Of tel, has a duty under the Telecommunications Act 1984 to promote the interests of consumers in respect of the prices charged for and the quality and choice of telecommunications services. To reflect the convergence of broadcasting, telecommunications, television and the management of the radio spectrum,

2 The cable networks are provided by NTL Group and Telewest Communications plc. Their networks, which cover separate areas, are available to about 60 per cent of households.

3 BT is required to offer this service under its licence, but cable companies are not because they are not deemed to have significant market power.

the Office of Communications Act 2002 set up Ofcom to take over the functions of Oftel and four other regulatory bodies. This transfer is planned to take place in December 2003. The Chief Executive of Ofcom has stated that Ofcom will be a 'reaching out' regulator that embraces consumer protection through the promotion of effective competition and choice.

1.7 Oftel aims to ensure that consumers get the best deal in terms of value for money. It seeks to achieve this primarily by promoting competition. Competition should place pressure on suppliers to improve price and quality, and provide innovative products and services. In addition to the Government's decision in 1984⁴ to allow competing networks, Oftel has pursued many initiatives to increase the level of competition in the fixed line telecommunications market. Important initiatives in recent years have been:

- **Indirect Access.** When making a call, consumers can now choose to route it through a supplier that does not own the network where the call originated. This is usually achieved by dialling a four-digit routing prefix, and results in separate bills for calls and line rental.
- **Carrier Pre-Selection.** An extension of Indirect Access, which allows customers to opt for certain defined classes of call to be carried by an operator selected in advance without having to dial a routing prefix.
- **Wholesale Line Rental.** This was introduced in autumn 2002 and allows alternative suppliers to BT to provide an integrated service comprising calls and line access by renting the exchange line from BT. It results in a single bill for the customer.

Oftel regulates to protect consumers where competition is not effective

1.8 Some regulation is still necessary to ensure that consumers' interests are safeguarded. This need arises in four main ways:

- **Where competition is insufficiently established.** Oftel has since 1984 imposed controls on some of BT's retail charges to consumers. Oftel has proposed withdrawing these controls when BT's charges have fallen sufficiently or if the introduction of Wholesale Line Rental is successful.

- **Because BT's network is the major way of delivering services to consumers.** Oftel has included in BT's licence a requirement to allow competitors access to its network, and has separately capped the prices of such connections under the network charge control it has imposed on BT⁵.
- **Where competition may not result in affordable basic services for all.** Oftel has imposed a universal service obligation on BT and requires BT to provide geographically averaged prices.
- **To prevent anti-competitive behaviour** (covered in Part 2 of this Report).

Consumers are more likely to benefit from competition if they are well informed

1.9 Competition and regulatory action may give consumers a better deal without them having to do anything (for example, the more well informed consumers there are, the more all consumers stand to benefit from competition), but they do not automatically give individual consumers the best deal. To achieve this, consumers need to be aware of the choices available and how to take advantage of these choices, and be prepared to exercise their choice. Consumers exercising choice put suppliers under pressure, thereby further strengthening competition. Oftel recognises the importance of consumer awareness by setting itself a high level objective of having 'well informed consumers'.

1.10 The Office of Fair Trading (OFT) has identified insufficient consumer information as a potentially important cause of market failure⁶. It concluded from its research⁷ that consumers need to be well informed if they are to get the full benefits of competition and that it cannot be assumed that suppliers will provide the optimum amount of information in the best way for consumers. The OFT observed that imperfect information can result in consumers not buying the product or service at the cheapest price, not buying the most appropriate product, and not receiving the level of quality expected.

⁴ The Telecommunications Act 1984 removed BT's monopoly.

⁵ The National Audit Office report *Pipes and Wires* of April 2002 included an examination of Oftel's Network Charge Control (October 2001 to September 2005) on BT and similar controls imposed by other economic regulators. Our analysis showed that customers had seen lower prices and higher quality of service, and regulated companies had been able to cut costs and invest in their networks, while continuing to finance their functions (HC723/2001-2002 paragraph 3).

⁶ Market failure is a term used to describe the situation where the optimum allocation of resources has not been achieved within a market. This can arise in several ways, including inadequate competition and insufficient consumer information, education and redress.

⁷ Research Paper 11 of August 1997 (Consumer detriment under conditions of imperfect information).

- 1.11 The Sandler Review of July 2002⁸, which studied competitive forces within the retail savings industry, emphasised the link between information and competition. The review found that "information on underlying costs and performance is often opaque - or even, in the case of many with-profits products, entirely absent. Partly as a result, competitive forces do not always work effectively to deliver value".
- 1.12 In any market there is a risk that suppliers' actions alone cannot be relied upon to generate sufficient market awareness to meet the needs of consumers. Suppliers are more likely to highlight positive aspects of a product, rather than less appealing ones, in any promotional campaign. In telecommunications markets, when promoting a particular tariff, suppliers often highlight features such as a free call allowance or a low 'per minute' charge, rather than call connection charges or minimum call charges. There is therefore a risk that telecommunications consumers will not get the best deal in terms of price, quality and the most appropriate product.

Many consumers are not aware of alternative ways of buying telecommunication services

- 1.13 Since the telecommunications market was opened up to competition in 1984, additional ways of obtaining a fixed line service have been introduced. Since 1991 cable companies have been permitted to offer a fixed line telephone service and the majority of cable networks now provide telephony as well as television services. Coverage, however, is not universal. As at December 2002 some 60 per cent of UK households were 'passed' by the cable network and most of these consumers are aware of this option. The level of take-up (in cabled areas) at December 2002 was around a third, giving cable companies some 19 per cent, by value, of the total UK market.
- 1.14 Using an indirect access operator (paragraph 1.3) is an important way of saving money, and one that will increase in importance with the introduction of wholesale line rental (paragraph 1.7), but consumers' awareness of such companies is low. Our survey in September 2002 found that 77 per cent of consumers could not name a single indirect access operator. Oftel's own research in February 2002 found that 48 per cent of customers were unaware of such operators. The variation in the results was due to differences in the questions asked. Both

surveys, however, showed material variations between different types of customer. For example, awareness was much lower in Northern Ireland and among the DE social group. Oftel's analysis also showed that of those who could benefit most (such as high users), two-thirds were aware of indirect access operators.

- 1.15 One reason why more than half of consumers are unaware of indirect access operators is that none of these suppliers has conducted a major direct selling campaign, either on the doorstep or over the telephone. Direct selling, widely accepted as being a very effective sales technique and a major driver of switching supplier in the energy market, has not been prominent in telecommunications, although Oftel expects this to change in response to the introduction of wholesale line rental. Direct selling, however, is not without its risks - in the energy market it has resulted in a significant number of complaints⁹.
- 1.16 In addition to the different fixed line services, consumers have a wide choice of tariffs. For example, in February 2003 BT offered more than 10 different tariffs for the fixed line residential consumer and NTL (one of the two cable companies) had six different options. Oftel has researched consumer awareness of two BT tariffs. Most recently, its May 2002 survey found that 44 per cent of BT's customers were not aware that several of its tariff packages include an allowance of free calls. For fixed line customers who use indirect access operators in addition to BT, the proportion rose to 51 per cent¹⁰.

Complex tariff structures can make informed choices harder for consumers

- 1.17 The range of different tariffs available to consumers makes choosing the most suitable supplier and tariff a time consuming exercise. Unlike energy, where there are limited ways to price gas or electricity, telecommunications suppliers offer quite different pricing schemes. Consumers, particularly high users, may therefore have to spend considerable time applying individual schemes to their own circumstances to determine which one, or mix, offers the best value. There are two main aspects for consumers to consider:

⁸ *The Sandler Review of Medium and Long-term Retail Investment (9 July 2002).*

⁹ *energywatch, an independent gas and electricity consumer organisation funded by the Department of Trade and Industry from licence fees paid by energy companies, received 2,459 complaints about direct selling in the three months to 28 February 2003.*

¹⁰ *In its other piece of research, in August 2001, Oftel surveyed the level of awareness of BT's In Contact Plus tariff amongst customers on BT's basic In Contact tariff. No firm conclusions could be drawn.*

- **Their usage pattern.** Before comparing prices, consumers need to determine the number, type, timing and duration of calls made over a billing period. This will dictate which tariff, from their existing supplier or an alternative company, offers best value. The best source of information on individual usage is the customer's quarterly bills. Oftel requires all suppliers to provide fully itemised bills on request. However, bills are not broken down in a way that enables consumers to readily identify their exact call pattern, and are therefore of little use for making precise comparisons.
- **Contractual terms and conditions.** Some companies require new customers to pay an equipment installation fee and to enter into a contract for a minimum period (usually 12 months). Consumers have to be careful that such costs and restrictions do not outweigh any savings they might achieve, and therefore need to study carefully all aspects of a particular tariff or call plan.

1.18 Applying tariffs to a usage pattern can be a time consuming process without a computer assisted modelling programme. This is because suppliers have different pricing structures. For example, a company might be cheaper for weekend local calls but more expensive for other call types. And as noted in paragraph 1.12, connection charges and minimum call costs also have to be taken into account. To illustrate the difficulty of making comparisons, the graphs in **Figure 2** show three examples of how small variations in the duration of calls affect the competitiveness of the BT *Standard* and BT *Together* tariffs and that of a representative cable telephone company.

Making consumers well informed will not by itself ensure they benefit fully from competition

Consumers place a high priority on an established brand and service reliability

1.19 Because fixed line telecommunications are an integral part of modern life¹¹, consumers are likely to be more concerned about the potential risks from changing supplier than would be the case for less important purchases. This is reflected in the great importance placed by consumers on the strength of a supplier's brand. In our survey, 66 per cent of respondents stated that it was 'essential' or 'very important' to be with a telecommunications supplier they can trust. Oftel's 2001 research into the importance of brands in

consumers' decision making found that while some consumers felt it was worth changing supplier to get better value for money, they were not prepared to switch to an unknown supplier. In practice, few brands were familiar. BT had a strong brand, from its position as the only fixed line universal supplier and heavy expenditure on brand-building advertising, while indirect access operators were not seen as brands at all.

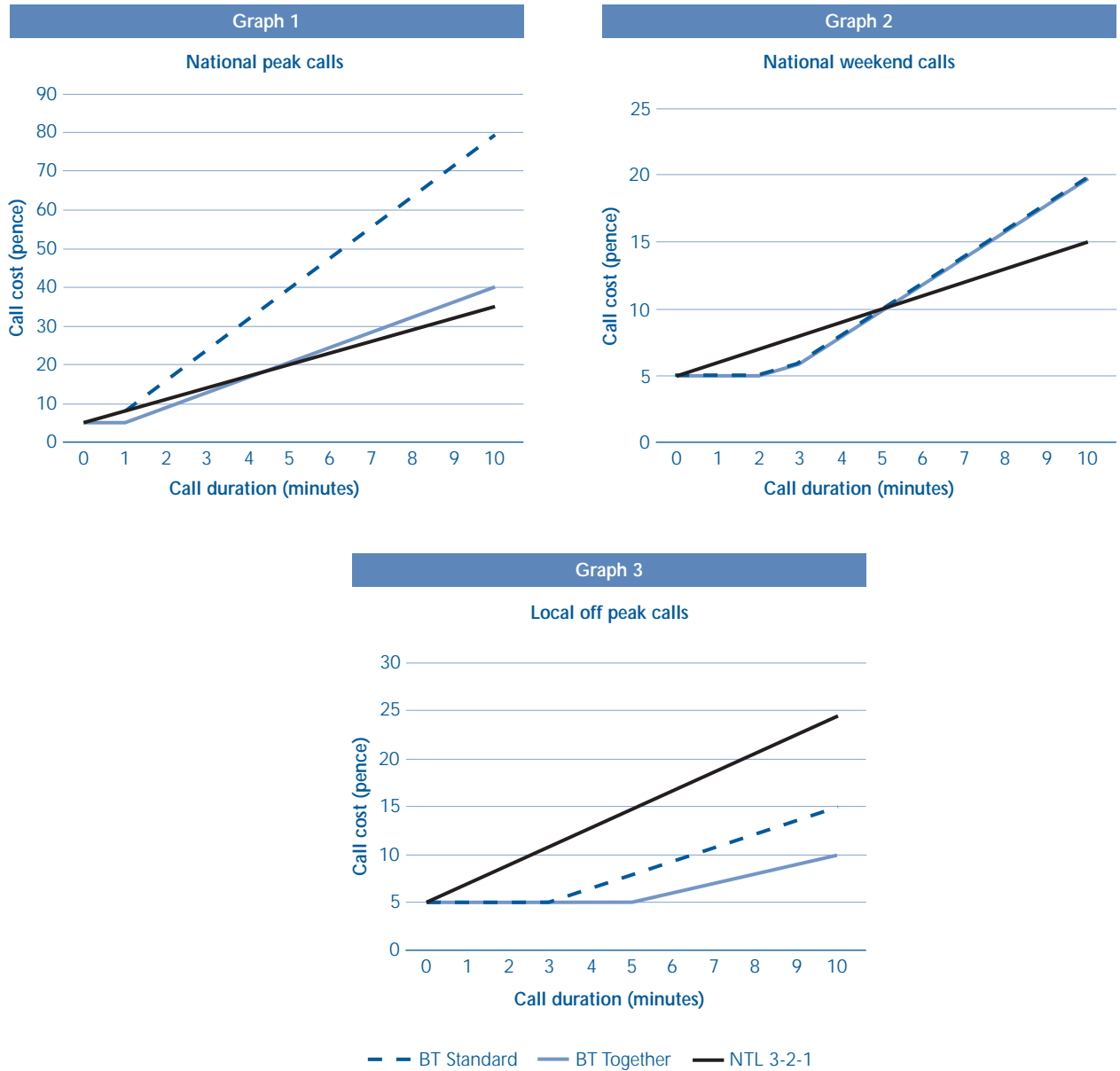
1.20 The two pieces of research indicate that brands are fundamentally important in telecommunications and that many consumers are unwilling to switch to a supplier that does not have a strong brand. The introduction in 2002 of wholesale line rental (paragraph 1.7) might address this problem. As at April 2003, several companies with strong brands were considering entering the fixed line market.

1.21 Our survey found that consumers' highest priority from their telephone supplier is reliability (90 per cent of respondents considered this 'essential' or 'very important') and having any problems satisfactorily dealt with (89 per cent). Oftel's research, in October 2002, showed that 96 per cent of consumers were satisfied with their fixed line service. Most consumers are therefore not motivated to switch supplier. There is a risk, however, that the high level of satisfaction may simply reflect a lack of consumer awareness of alternative options. It could also result from consumers' self-justification for not changing supplier - our survey found that only 60 per cent of respondents said they would switch supplier if 'they had problems making or receiving a call' or if 'they were unhappy about the way a complaint was handled'.



¹¹ In November 2002, 92 per cent of total UK households had a fixed line telephone and 7 per cent had a mobile telephone but no fixed line - leaving just 1 per cent with no form of personal telephony. Forty-two per cent of UK households had internet access through their fixed line.

2 The cost of calls made on BT's *Standard* and *Together* tariffs and NTL's 3-2-1 tariff at December 2002¹²



NOTES

Graph 1 shows that for a national peak call, BT *Standard* is the most expensive tariff after one minute, with BT *Together* cheaper than NTL for calls of less than five minutes duration and NTL the cheapest for all calls over five minutes duration.

Graph 2 shows that for a national weekend call, BT *Standard* and BT *Together* which cost the same, are cheaper than NTL for calls of less than five minutes duration and NTL the cheapest for all calls over five minutes duration.

Local off peak calls are one of the cheapest types of call and as such minimum call charges and connection charges have a bigger effect. **Graph 3** demonstrates that NTL is the most expensive provider, with BT *Together* and BT *Standard* costing the same for calls up to 3 minutes duration, after which BT *Together* becomes cheaper.

Source: OfTel's Market Information Fixed Update: December 2002

12 BT revised its prices for BT *Together* from 1 June 2003.

The effort involved in switching may dissuade consumers from exercising their choice

1.22 Consumers need to expend effort to switch to an alternative supplier or change tariff with their existing supplier, but need do nothing to leave their arrangements unchanged. Taking action therefore always has a cost, which may deter some consumers from taking advantage of competition. There are three elements to this cost:

- **Time.** For consumers with busy lives, time can be more important than day to day expenditure - a situation that has come to be known as 'cash rich / time poor'. These consumers may not be motivated to review their fixed line telephony, especially if such expenditure is low or is not a significant proportion of their income;
- **Financial.** An alternative arrangement may require an immediate payment, such as an equipment installation fee (paragraph 1.17);
- **Inconvenience.** The main fixed line alternative to BT is 'cable', which requires a new connection into the home. Using an indirect access operator results, at present, in two separate bills or the purchase of a pre-payment card.

The level of financial saving needed to persuade individual consumers to switch is often higher than the saving achievable

1.23 The factors deterring consumers from making changes (paragraphs 1.17 - 1.21) may explain the high level of financial savings that most people say they would need to persuade them to switch supplier. When we asked consumers whether they would change their fixed line arrangements, either with their existing supplier or by switching to a different supplier, to achieve savings of 10, 25 and 40 per cent we found that:

- At each level, consumers are more likely to look for changes with their existing supplier than change supplier (Figure 3). And even then the level of savings has to reach 40 per cent before the majority of consumers are 'highly likely' to act;
- A significant minority of consumers are reluctant to change 'at any price' - 32 per cent of consumers would be 'unlikely' or 'highly unlikely' to switch supplier for savings of 40 per cent, and 25 per cent of consumers would not even make changes with their existing supplier.

1.24 This tendency is confirmed by the fact that relatively few consumers have changed their arrangements in the last two years. Our survey results indicated that 11 per cent of respondents had switched or added to their fixed line supplier and 21 per cent had made changes whilst staying with their existing supplier. The likelihood that consumers will change is linked closely to age, social group, location and spend. The respondents that had acted were most likely to be in their thirties, in social groups A and B, and spending most - the last factor indicating those with most to gain are those most likely to have acted.

1.25 In contrast, our survey also found that 49 per cent of respondents were 'fairly likely' or 'highly likely' to take action to achieve savings of 10 per cent with their existing supplier. This reduced to 32 per cent if it meant switching supplier. To establish whether the availability of savings is a reason for the significant variations between interest and action, we examined the extent to which savings of 10 per cent are possible. Our findings are set out in detail in Appendix 2, including descriptions of the five consumer types used, and can be summarised as follows:

- the *Lowest User* would be significantly worse off by making any changes if they are on BT's Light User Scheme¹³. As at September 2002, 1.45 million out of four million eligible customers were on this scheme. And the *Low User* could only make savings of around 5 - 7 per cent;

3 Consumers' motivation to change their fixed line telephone arrangements

Level of saving	Likelihood to change within supplier (per cent)				Likelihood to change supplier (per cent)			
	Highly unlikely	Fairly unlikely	Fairly likely	Highly likely	Highly unlikely	Fairly unlikely	Fairly likely	Highly likely
Saving of 10 per cent	23	28	35	14	34	34	25	7
Saving of 25 per cent	17	17	37	29	24	23	38	15
Saving of 40 per cent	14	11	23	52	19	13	26	42

Source: National Audit Office public survey

13 BT informs any customer that meets the terms of its Light User Scheme of its existence and offers this service to them. This a requirement of BT's licence. But consumers are barred from the Scheme if they use an indirect access operator, a mobile telephone or have more than one line.

- the *Medium User* could typically make savings of between 4 and 19 per cent. The largest saving is achievable only if the user is still on BT's Standard tariff¹⁴;
- the *High User* and *Highest User* could each make a maximum saving of around 29 per cent if still on the BT Standard tariff. However, relatively few are likely to be on this tariff and the saving would reduce to around 8 per cent if they are on BT Together with the Friends and Family discount.

1.26 Our survey indicates that the difficulty for many consumers to achieve savings of even 10 per cent is likely to deter them from making changes. This may partly explain why in August 2002 the market share retained by the incumbent supplier (BT) was 79 per cent, with 10 per cent of consumers using both BT and an indirect access operator. For the 60 per cent of UK households that have access to a cable network, the only alternative to BT prior to the introduction of indirect access, BT's market share is lower at around 64 per cent. This is similar to the market shares of the incumbent suppliers in the residential gas and electricity markets¹⁵.

Oftel has acted to help consumers to be informed and to remove barriers to switching supplier

1.27 A market that provides an on-going service to the public, the cost of which is met with regular small payments, or has a dominant supplier, tends to reinforce the existing pattern of supply. Fixed line telecommunications is unusual in having all three features. As the incumbent and by far the largest supplier in this market, BT enjoys certain advantages over its competitors in retaining customers and winning new business:

- As the previous monopoly supplier, only BT can benefit from consumers taking no action to change the way they buy their telecommunication services;
- The unit cost of advertising is much lower as it can be spread over far more customers. This gives BT an advantage in developing brand awareness and image (e.g. BT's '*It's good to talk*' campaign in the 1990s) and in marketing its products (e.g. BT's broadband packages). The latter also helps to build BT's brand even if a consumer is not interested in the advertised product.

1.28 The choices available in the telecommunications market, coupled with BT's dominant position, mean that the availability of information to consumers is very important. To achieve its high level objective of 'well informed consumers' (paragraph 1.9), Oftel has:

- prepared written guidance for consumers;
- used a variety of ways to distribute information to consumers;
- promoted facilities that enable consumers to make comparisons;
- taken steps to remove barriers to switching.

Oftel produces guidance for consumers

1.29 Oftel has published general written guidance on the rights and choices of consumers, supplemented by more detailed guidance on specific aspects of the market (**Figure 4 overleaf**). Oftel's intention is to 'enable' consumers to be in a position to benefit from the choices available. There is a limit, however, to what this approach can achieve. Oftel considers that it would compromise its role as the independent, impartial regulator if it listed the 'cheapest' suppliers or the ones that provide the 'best' all-round service. It does, however, point consumers to useful sources of information and suggest things to consider.

1.30 Research by Oftel in October 2001 found that consumers wanted more than just basic information. Oftel re-launched its written guidance in June 2002 to reflect those issues that consumers had found most important. Oftel stated that it provided 'clear, practical advice to consumers on how to make the best choice from the different companies and services on offer'. The guidance advises consumers of the kinds of issues they should think about, but does not provide a basis for making decisions. In particular, it does not provide any practical examples of how consumers might go about making choices. Subject to testing consumer opinion, Oftel could make its guidance more useful to consumers by:

- giving advice on 'choosing the right telephone company' a higher profile. The information is embedded in Oftel's general guide entitled 'Your rights and choices as a telephone customer' after sections on 'your rights as a telephone customer' and 'how to complain about your telephone service';
- doing more to point consumers in the direction of savings. For example, its guides do not refer to the fact that many consumers can gain from changing tariff with their existing supplier;
- being more positive about the potential benefits so as to encourage consumers to act. For example, it could provide practical examples, by way of illustration, of the benefits consumers could gain in particular circumstances.

¹⁴ At July 2002, eight per cent of BT's customers were on its Standard tariff.

¹⁵ In June 2002 Centrica supplied 65 per cent of residential gas customers and the local electricity companies supplied 64 per cent of residential electricity customers.

4 Oftel's consumer guides

Title	Summary of content	Date published
General guidance <ul style="list-style-type: none"> Your rights and choices as a telephone customer¹ 	The rights of telephone customers, how to complain about one's telephone service, and how to choose the right telephone supplier including an explanation of direct and indirect access. The role of Oftel is also explained.	June 2002
Specific guidance <ul style="list-style-type: none"> Carrier pre-selection² How to access the internet at home Getting the best deal from your mobile phone service New 'Line and Calls' services (the public term for wholesale line rental) 	<p>The benefits and practicalities of using this type of service.</p> <p>What is needed, what to consider when choosing an internet service provider and package, and what is broadband.</p> <p>Choosing and changing services, controlling expenditure, and the theft and safety of handsets.</p> <p>Explanation of this type of service and the benefit, answers to questions consumers are likely to have, and what to consider when deciding whether to change suppliers.</p>	<p>December 2001³</p> <p>September 2002</p> <p>September 2002</p> <p>October 2002</p>

NOTES

1. Issued as four separate guides in April 2001. With the help of consumer feedback, Oftel revised the content and reformatted it into a single guide.
2. Oftel also provide a list of suppliers currently offering carrier pre-selection services, but inclusion is at the initiative of individual suppliers and most are not listed.
3. First published November 2000.

Source: National Audit Office public survey

1.31 Oftel's later consumer guide for mobile phone users 'Getting the best deal from your mobile phone service', published in September 2002, is different in format. It provides detailed information on choosing and changing a mobile service, and includes advice to consumers on how to make savings (for example, by switching network when using the phone overseas).

Oftel is increasing the ways in which it distributes information to consumers

1.32 Oftel's website is the principal means by which consumers can access its publications. The website receives about 40,000 visits a month, of which about 10,000 view the initial consumer page and 3,000 proceed to the consumer guidance section. This amounts to some 36,000 visitors a year to the consumer section, which represents 0.15 per cent of residential fixed line consumers. Oftel does not collect data on how many of the visits to its website are repeat visits or on the characteristics of visitors.

1.33 In carrying out our preliminary work, we found that consumer information was not easily accessible on Oftel's website. The section on consumer guidance was five levels down from the home page and it was not clear which link to select at some of the intermediate levels. Also, the web page that contained the consumer guides did not lead consumers step by step from Oftel's general guidance to its specific guidance and some of the terminology used was unlikely to be readily understood by the majority of consumers. Oftel re-launched its website in January 2003 with improved site presentation and easier access to its consumer guidance.

1.34 It has been a long-standing practice of Oftel to place 'hard copies' of its written guidance in libraries, and offices of Citizens Advice Bureaux and local trading standards services. Oftel is aware that this limits the number of consumers that can access the information, since the use of public libraries has dropped significantly in recent years, and the offices of Citizens Advice Bureaux and trading standards services are not generally sited in prominent locations. To make guidance more readily available, Oftel has begun using additional outlets for a limited range of guidance. For example, some 180,000 copies of the guidance on mobile telephony (paragraph 1.31) have been circulated through relevant shops, and the internet guidance is now made available through www.ukonline.gov.uk, the UK Government's information and services website.

1.35 For 2002-03, out of a total budget of £19.5 million, OfTel allocated £45,000 for external publicity. Because of the high cost of national advertising¹⁶, OfTel seeks media channels that provide a free, or low cost, way of reaching a wide audience. It considers that local radio, which is more popular during daytime than national radio or television, to be a cost-effective way of informing consumers. In the second half of 2002, OfTel carried out some 50 radio interviews on general issues and specific topics, including about 25 on the launch of the new directory enquiry services. Although OfTel has not yet evaluated the outcome of its publicity campaigns, it is now committed to carrying out on-going research to assess the effect of its consumer information work.

The comparison websites promoted by OfTel have not been supported fully by suppliers

1.36 A price comparison website, www.phonebills.org.uk, was launched in December 1999 following concerns raised by the Committee of Public Accounts¹⁷. The Committee observed that tariff structures were complicated and confusing. OfTel confirmed that it was committed to seeing that the consumer got clear and precise information about tariffs. OfTel participated in the development of the website and endorsed it. The site used a price comparison model provided by independent consultants, who also managed the site. OfTel encouraged telecommunications companies to co-operate in developing the site and to provide tariff data, but it could not compel them to do so. At the outset, nine companies supplied data for the website, but four subsequently withdrew¹⁸. Of the five remaining companies, only one was an indirect access operator and that was owned by one of the other participating companies. As a result the website has not provided a comprehensive service. It was discontinued in early 2003.

1.37 By mid-2001 other price comparison websites not endorsed by OfTel began to appear (for example, www.uswitch.com with details of tariffs for 19 companies). OfTel concluded that an accreditation scheme would encourage good quality comparison services and increase consumer confidence in them. OfTel announced its accreditation scheme, the OfTel Price Assurance Standard Scheme (PASS), in September 2002. To be accredited, sites must pass a detailed technical assessment, including compliance with OfTel's code of practice, and provide free access to residential consumers. OfTel accredited the first company, uSwitch.com, in June 2003. At this date, the site included over 20 companies, the majority of which are indirect access operators.

1.38 A potential difficulty for any price comparison website is obtaining information from suppliers. Some suppliers have objected to their prices being included by claiming a breach of copyright, an issue that is outside OfTel's remit. An EU Directive¹⁹ that becomes effective in July 2003 will require suppliers to make their tariffs publicly available, but it is not yet clear whether providers of price comparisons will have a right to use tariff information in this way. The Directive applies only to 'end users' of telecommunications services and price comparison services may not be covered by this.

1.39 As indicated in paragraph 1.21 above, consumers are very concerned about quality of service, often giving this greater weight than cost. A quality of service website, www.cpi.org.uk, was launched in the mid-1990s. It provides performance indicators for faults, billing, order completion and complaint handling. As at April 2003, four companies participated - the two incumbent fixed line companies and the two cable companies. Although the website is updated every six months, it has suffered from incomplete information - a problem that OfTel considers should be resolved as the information systems of participants are improved.

1.40 OfTel draws attention to PASS and www.cpi.org.uk through its own website and its guidance, and www.cpi.org.uk also refers to PASS. It is too early to measure public awareness of PASS, but in November 2001 OfTel found that only 11 per cent of consumers were aware of www.phonebills.org.uk and www.cpi.org.uk.

OfTel has worked to remove barriers to switching

1.41 Through consumer research, OfTel has identified a number of barriers that may make consumers less likely to switch. These include the need to change telephone number when switching supplier and, with regard to using indirect access operators, the need to dial a four digit routing prefix and the receipt of at least two bills covering line rental and calls. OfTel has sought to address these barriers. The introduction of number portability enables consumers to keep their telephone number when changing supplier, while carrier pre-selection allows consumers to opt for certain defined classes of call to be carried by an operator selected in advance without having to dial a routing prefix. In due course wholesale line rental will allow a supplier to offer a consumer a single bill while still using BT's equipment. To date, the need to have a BT line, except in cabled areas, has meant that most consumers who wished to use alternative suppliers have had to maintain a billing relationship with BT.

¹⁶ For example, the total publicity budget would not be able to pay for a full page advert in a broadsheet Sunday newspaper.

¹⁷ Sixty-fourth Report 1997-98 (July 1998).

¹⁸ One on cost grounds, the others as a result of insolvency or withdrawal from the market.

¹⁹ Directive 2002/22/EC (Universal Service Directive).

1.42 Oftel has tried to lower perceived risks of switching by playing a leading role in the setting up of the Telecommunications Ombudsman Service to resolve complaints. The Service, which commenced operations in January 2003, is an independent body funded by its member companies. A complaint must already have been considered by the relevant member company²⁰. Oftel's involvement stems from EU Directives requiring that procedures exist to deal with unresolved disputes. Oftel hopes that all suppliers of telecommunication services will join the scheme in due course. As at March 2003, BT and eight other suppliers had joined²¹.

1.43 Oftel has actively supported the introduction of codes of practice by suppliers. The codes are intended to ensure consumers have a clear understanding of their rights and obligations. In September 2002 Oftel announced proposals to increase the number of codes of practice. By mid-2003 telecommunication suppliers will be expected to have codes on prescribed issues, such as billing, disconnection and debt policies, and services for disabled and elderly users. Suppliers will prepare their codes within a framework approved by Oftel, who will vet each code produced.

Oftel's new information strategy provides an opportunity to focus on those consumers who can benefit most

1.44 In November 2002 Oftel set out its proposals for a consumer information strategy. Oftel's aim is to gain a clearer understanding of consumer preferences and behaviour and to communicate more effectively. The strategy builds on the work that Oftel has already done and should help it to identify what else needs to be done, or done differently. For example, Oftel already designs and produces consumer information (paragraph 1.29) and is beginning to use different methods to target and disseminate information to ensure it reaches the right people (paragraph 1.34). But Oftel's strategy also identifies the need to assess the impact of its information, something it is only beginning to do systematically. Measuring changes in consumer behaviour and the financial benefits that have arisen is a key aspect of a good communications strategy. This is not a task that can be done quickly and Ofcom will need to carry forward the research that Oftel is now doing.

1.45 In the energy market Ofgem and *energywatch* have made considerable efforts to raise consumer awareness of available choices, believing there are good reasons for motivating consumers to think about switching:

- to raise awareness of competition in the supply of gas, *Ofgas*²² established an integrated publicity campaign involving leaflet drops to 20 million homes, regional press advertising and adverts (for example, on the sides of taxis) featuring 'Gus the Ofgas watchdog'. More recently Ofgem has explained the benefits to customers of 'switching and saving' in numerous media interviews and press articles.
- to equip consumers with the confidence, assertiveness and knowledge they need to enjoy the full benefits of competition, *energywatch* is embarking on a programme of 'outreach' activities that include exhibitions, advice surgeries and staffed information stands in public and community venues.

1.46 Oftel's approach has been less pro-active. It considers that the telecommunications market is substantially different in that there is a much wider range of services and tariffs. It considers that the differences in the nature of the market, rather than the regulator's approach, can explain the lower rate of switching by consumers (paragraph 1.26). Oftel has not encouraged consumers to engage in wholesale switching of suppliers. Instead, it has concentrated its efforts on facilitating the provision of alternative fixed line services and making information available (paragraph 1.29). The establishment of Ofcom provides an opportunity for those involved in regulating the telecommunications market to consider the benefits of taking the additional step of actively encouraging consumers to think about the way they buy their telecommunication services.

1.47 The potential for consumers to benefit from competition in the telecommunications market depends much more on individual circumstances (paragraph 1.17). As such, it is less evident that a simple consumer awareness campaign would be cost-effective as this would encompass those that cannot save, or could save little, from making changes, and might raise false expectations. This suggests that efforts should be focused on consumers with most to gain. Four examples of how savings can be made are given below. In deciding whether to make changes, consumers would also need to consider other factors, such as quality of service.

²⁰ Guidance on how to complain is available on The Office of the Telecommunications Ombudsman's website (www.otelo.org.uk).

²¹ Member companies at March 2003 comprised Broadssystem Ventures Ltd, BT, Centrica Telecommunications (OneTel and British Gas Communications), NTL Group Ltd, Powergen UK plc, Thus plc, United Utilities Consumer Sales Ltd, Virgin Mobile Telecoms Ltd and Vodafone Ltd.

²² The Office of Gas Supply and the Office of Electricity Regulation were merged in 1999 to form the Office of Gas and Electricity Markets.

(1) Using an indirect access operator for certain calls

1.48 Consumers with a BT line can choose to route some or all calls through an indirect access operator. For certain types of call indirect access operators offer significant savings over BT (Figure 5). The greatest savings (over 50 per cent) are on international calls, although savings of 38 and 69 per cent can be made on peak time local and national calls respectively. Using an indirect access operator is not, however, always cheaper - in this example, off peak national calls cost more.

1.49 Potential consumer savings are particularly pronounced for international calls. Figure 6 shows call charges for BT and a representative indirect access operator for six countries that attract a high volume of calls from the UK. In this case we have adjusted BT's Standard rate to include the discounts that are commonly taken. The potential savings range from 37 to 82 per cent. Based on market information for international calls, an average user could save 59 per cent (Appendix 2).

5 Cost per minute of indirect access operators compared with two BT Tariffs

Tariff	Local		National		Mobile		International	
	Peak	Weekend Off-peak	Peak	Weekend Off-peak	Peak	Weekend Off-peak	Peak	Weekend Off-peak
BT Standard	4p	1p	8p	2p	21p	4p	53p	43p
BT Together	3p	1p	4p	2p	19p	4p	33p	25p
Representative indirect access operator	2.5p	1p	2.5p	2.5p	20p	8p	11p	11p
Savings over BT's Standard rate if a representative indirect access operator is used	38%	0%	69%	-25%	5%	-100%	79%	74%

NOTES

1. All rates include VAT but exclude discounts, line rental, minimum call charge and connection charge.
2. Mobile rates are the call fees to each tariff weighted by the volume market share.
3. International call rates are the fees to the 134 busiest routes weighted by the volume of international direct dial calls.

Source: National Audit Office analysis of tariff data.

6 Cost of calling a selection of countries at the weekend using available discounts

Tariff	Australia	Brazil	France	Germany	Pakistan	USA
BT Standard with discounts (Note 2)	22p	56p	13p	13p	56p	12p
BT Together with discounts (Note 3)	8p	56p	8p	8p	51p	8p
Representative indirect access operator	4p	22p	4p	3p	35p	3p
Savings over BT's Standard rate with discounts if a representative indirect access operator is used	82%	61%	61%	77%	37%	74%

NOTES

1. All prices are weekend rates in pence per minute, including VAT.
2. BT Standard rate includes Friends and Family Overseas, Premierline and Country Calling Plan discounts.
3. BT Together rate includes Friends and Family Overseas discount.

Source: National Audit Office analysis of tariff data.

1.50 Research by Oftel amongst international callers has found that consumers who regularly call international destinations tended to use calling cards²³ and indirect access operators to do so. Infrequent international callers were more likely to use their main home supplier for these calls as they considered them a very small part of their overall expenditure. Nevertheless, at December 2002 BT still accounts for 57 per cent of residential international call revenue.

(2) Taking full advantage of discounts with existing supplier

1.51 The larger suppliers offer a range of different tariffs tailored to different customer circumstances. For example:

- BT has six discount schemes, the best known being *Friends and Family*. Consumers who take maximum advantage of its schemes can save up to 44 per cent on call charges²⁴, though this level of saving is only applicable to a very small number of consumers.
- BT customers can also make savings by subscribing to a call plan; for example, with *BT Together* customers pay a monthly charge for line rental and a specified call allowance. We calculated that a typical medium user²⁵ on *BT Together*, taking advantage of all available discounts, would save £50 (almost 16 per cent) from their annual bill compared with BT's *Standard* tariff (Figure 7). It is important, however, for consumers to be on the call plan that best matches their particular call pattern. For example, specific internet tariffs are not appropriate for someone who spends less than three hours a week on-line (at off-peak rates).

(3) Paying by direct debit

1.52 Most suppliers offer a lower price on line rental to customers who pay by direct debit. This is worth £12 a year to a BT customer and £24 for a Telewest customer. As at January 2003, 39 per cent of consumers paid for their telephone service this way. This method of payment, however, does not suit everybody - some people do not have a bank account, while others, particularly those on low incomes, might have reservations about committing themselves in advance.

(4) Purchasing rather than renting a handset

1.53 Customers renting a handset from BT can save money by buying one. The rental charge is £17.88 a year (including VAT) for a basic dial telephone, compared with a high street price of £6.99 (the equivalent of five months rental) for a similar, but unbranded²⁶, model. Some three million residential consumers rent about four million handsets in total from BT. The main reasons for renting are '*buying did not occur to me*' (17 per cent of consumers who rent), '*easier to rent*' (17 per cent) and '*too much hassle to buy*' (14 per cent)²⁷. Only four per cent said they could not afford to buy a handset. Sixty-nine per cent of those surveyed had been renting a handset for more than 10 years. Oftel is concerned about BT's continuing high rate of return from rental of handsets and is investigating this matter.

7 The annual cost for a typical medium user of different BT tariffs

Tariff	Annual Cost £	Extra cost compared with the cheapest £
BT Standard	319	50
BT Standard with Domestic & International Friends & Family	315	46
BT Together with unlimited local calls	313	44
BT Standard with Domestic Friends & Family	313	44
BT Working Together	296	27
BT Together	274	5
BT Together with Friends & Family	269	-

Source: National Audit Office analysis of BT tariffs

²³ Calling cards are sold by indirect access operators, normally through newsagents, and entitle the purchasers to a specified value of calls (e.g. £10).

²⁴ By reference to BT's price list as at December 2002.

²⁵ A fixed line user who mainly uses the telephone during the off-peak, and whose call profile includes a small proportion of international, mobile and Internet calls (see Appendix 2).

²⁶ BT told the National Audit Office that the equipment that it rents is sold in the £20 to £25 range.

²⁷ Oftel research August 2002.

Oftel is carrying out more detailed research into consumer behaviour

1.54 Oftel has, until late 2002, concentrated its research on consumer behaviour and awareness. For example, its programme of quarterly consumer surveys has focussed on such matters as the proportion of consumers that have a fixed line telephone and awareness of number portability. Oftel has in addition collected data on the telecommunications market, notably call volumes and revenues for the largest companies. This has enabled Oftel to track changes in consumers' calling patterns and see how consumers are using certain types of service, such as premium rate services. Oftel has supplemented this work with more detailed research, in specific policy areas, into the underlying drivers of consumers' behaviour. Oftel's research has been carried out in accordance with good practice standards and has been of a high quality.

1.55 To be able to target its activities, Oftel, and in due course Ofcom, needs to have a better overall understanding of consumers' needs and priorities. This is important because they might be very different from consumers' actual behaviour, for example where consumers are constrained by a lack of choice or awareness of the options available. Our survey has shown that the telecommunications market is very segmented (that is, there are wide variations in consumers' behaviour across age, location and social class) and that consumers in each segment have different needs and different levels of awareness. For example, consumers in London are much more aware of indirect access operators than those in Northern Ireland and consumers in social groups DE are less likely to change supplier if they are unhappy with the standard of service.

1.56 Oftel has recognised the benefit of having a better understanding of consumer needs and behaviour. Since early 2002 it has been developing detailed profiles of six types²⁸ of consumer. In April 2003 Oftel published proposals for assessing the extent to which consumers can make savings in the telecommunications market. Oftel considers that by having a clear understanding of the level of savings available, it will be able to better target consumer information towards consumers for whom the benefits of switching supplier are greatest. Oftel considers that this approach will help Oftel and, going forward, Ofcom decide whether action is required and, if so, to properly target future regulation in this area. The Director General of Telecommunications stated that "by being able to identify which consumers are most likely to switch because of the potential savings they could make, Oftel will be able to target these groups with information on choosing the best deal for their telecommunications service." Oftel is seeking views on its proposals from consumer organisations and the telecommunications industry by 30 June 2003.

1.57 The Communications Bill currently before Parliament includes specific provisions requiring Ofcom to carry out consumer research and to consult with consumers on a range of market issues. In particular, the Bill proposes the establishment of a Consumer Panel to advise Ofcom on the interests of domestic and small business consumers.



28 One of the types is consumers who do not have a fixed line or mobile telephone, which represent about 1 per cent of households.



Part 2

Stopping and deterring anti-competitive behaviour

2.1 Preventing anti-competitive behaviour is a key part of Oftel's work and, like its initiatives in raising consumer awareness (Part 1), it helps consumers benefit from competition. This Part of the report examines what Oftel has been doing to stop and deter anti-competitive behaviour, and the steps Oftel is taking to speed up its investigations. In doing so, this Part covers the recommendations (summarised at Appendix 4) made by the Committee of Public Accounts in 1998.

Consumers are best served by a fully competitive telecommunications market

- 2.2 In general, competitive markets provide greater benefits to consumers than markets served by monopoly suppliers. Competition provides stronger incentives for suppliers to operate efficiently and constrains suppliers from charging prices above cost-reflective levels. This generally leads to lower prices and provides consumers with more choice.
- 2.3 Where a supplier has a very strong position in a particular market there is a risk that it might take advantage of its position and act anti-competitively (for example, by driving out new entrants). Similarly, where a market is dominated by a small number of suppliers they may act anti-competitively through collusion (for example, by agreeing not to compete on price). Such behaviour can be detrimental to consumers in the form of higher prices, less choice and poorer quality of service. It is therefore crucial for consumers that anti-competitive behaviour is stopped and deterred.
- 2.4 As suppliers pursue their business interests it is often the case that disputes arise between them, including their being unable to reach agreement on matters where they need to work together. Companies may differ on whether the circumstances giving rise to disputes, which may be operational practices or the terms of trade offered, are a fair way of retaining or gaining a competitive advantage or represent anti-competitive

behaviour. New entrants are especially likely to be concerned that established suppliers, especially the larger ones, do not act unfairly. While telecommunication services in the United Kingdom are becoming increasingly competitive, some companies, notably BT in the supply of residential fixed line services, retain a strong market position. BT has a further advantage in that it operates in both the network and retail sectors²⁹ of the fixed line market.

There are risks of anti-competitive behaviour in the UK telecommunications market

- 2.5 Oftel is aware of the risks of anti-competitive behaviour occurring. To help determine what level and type of regulation is appropriate for specific market segments, it carries out a rolling programme of market reviews to assess the competitiveness of particular segments. This approach has now been written into the regulation of European telecommunications markets. Oftel concluded in June 2002, following a detailed review of the domestic fixed line market, that while the level of competition in the provision of fixed line calls had steadily increased, with many consumers having a wide range of choice from other suppliers (paragraph 1.3), the market was not yet fully competitive and BT's continuing strong market position meant that immediate withdrawal from regulation would put consumers at risk.
- 2.6 While complaints made to Oftel may simply be a request to resolve a trading dispute, they may also allege or infer anti-competitive behaviour. Complaints are therefore an important pointer of where risks to competition may be materialising. Oftel receives about 80 such complaints a year, two-thirds of which are about BT. Other suppliers make most of the complaints, with the remainder arising directly or indirectly from their customers. In addition, Oftel itself identifies cases where anti-competitive behaviour or a licence breach may be occurring - around 12 a year, the majority of which, in relation to competition matters, involve BT.

²⁹ The network sector provides the infrastructure that enables the service sector to offer telephony services to individual customers. A company operating in both sectors is said to be vertically integrated.

The risks can be addressed by high quality and timely investigations

- 2.7 Effective investigation and enforcement action can reduce the risks of anti-competitive behaviour in two ways - it should stop anti-competitive behaviour, where found, and should deter other companies from engaging in such behaviour. The deterrent effect is likely to be strongest when investigations are of a high quality and the outcome well publicised. Strong enforcement action, including the use of penalties where appropriate, sends a signal to other companies that anti-competitive behaviour will not be tolerated.
- 2.8 The timeliness of investigations (when they take place and how long they take to complete) is vital to limit the amount of detriment to consumers and the commercial damage suffered by companies that have been the subject of anti-competitive behaviour.

Preventing anti-competitive behaviour is an important part of Of tel's work

- 2.9 The Director General of Telecommunications has a statutory duty to investigate all complaints, including those involving anti-competitive behaviour. He has statutory powers to carry out investigations of suspected anti-competitive behaviour and to stop it. In addition, he has a duty to resolve disputes about interconnection, the process of linking suppliers' networks³⁰. Preventing anti-competitive behaviour is one of Of tel's four high level strategic objectives and Of tel budgeted to spend £1.8 million on this work in 2002-03.
- 2.10 The potential importance of anti-competitive behaviour in the investigations undertaken by Of tel varies depending on the nature of the case. In some cases, where for example a company has not met its obligations in respect of number portability, anti-competitive behaviour may not be a central issue. In other cases, where for example there are allegations of *margin squeeze*³¹, the question of anti-competitive behaviour will feature more prominently. The parties to an investigation are also likely to view the matter differently. A complainant is more likely to see a dispute over access prices as an attempt to price it out of the market and therefore restrict competition. The company being complained about may see the prices charged as a legitimate means of recovering its costs. It cannot therefore be necessarily inferred that an investigation of anti-competitive behaviour or the taking by Of tel of enforcement action means that a supplier has deliberately sought to stifle competition. It may be that Of tel's role is to clarify 'grey areas' so as to promote a

more competitive market. In any case, Of tel's primary concern in resolving disputes is to change companies' behaviour in the market so as to promote competition.

- 2.11 Since its inception, Of tel has carried out its investigations under the Telecommunications Act 1984. From 2000 it has also been able to use the Competition Act 1998 for some types of investigations where anti-competitive behaviour is alleged³². The Competition Act provides stronger powers of investigation and enforcement. For example, Of tel can:

- require information to be provided, enter premises without a warrant to obtain information, and apply for criminal sanctions for non-compliance with its requests;
- take interim measures to prohibit certain behaviour;
- impose financial penalties on companies engaging in anti-competitive behaviour.

- 2.12 In July 2002, following two years experience of using the Competition Act, Of tel revised its strategy for investigating allegations of anti-competitive behaviour. Of tel now seeks to use the Competition Act in preference to the Telecommunications Act wherever possible. To date, it has used its powers under the Act to obtain specified documents and information. Of tel has powers under the Competition Act to intervene, during an investigation, to provide protection from a suspected infringement of the Act and to fine companies following a completed investigation. It has not yet found any behaviour that it judges sufficiently serious to justify taking such action, although it has confirmed that it will use these powers if the need arises.

Of tel considers industry to be best placed to identify behaviour that may work against effective competition

- 2.13 Of tel accepted the conclusion of the Committee of Public Accounts in 1998 that it should ensure that it is not too reactive in dealing with anti-competitive behaviour. In June 1998 the Director General told the Committee that Of tel's 'own initiative' cases had risen, from 10 per cent of investigations at the time of our examination, to 20 per cent. Of tel continues to initiate its own investigations of suspected behaviour that may work against competition, but complaint based investigations still dominate. In the two years to June 2002, Of tel-initiated cases accounted for 12 per cent of investigations. This does not, however, reflect the relative proportion of effort involved as Of tel-initiated cases tend to be more wide-ranging.

³⁰ Interconnection is the process of physically connecting suppliers' networks, thereby allowing the customers of one supplier to connect to customers of another supplier, or to access services provided by another supplier.

³¹ When a company uses its dominance in one market to gain an unfair advantage in another market.

³² Of tel generally resolves interconnection disputes using a framework based on its sectoral powers, rather than the Competition Act 1998, as it creates predictability about the way interconnection rules will be applied.

2.14 Oftel adopts a flexible and informal approach to identifying where, and in what form, behaviour that may work against competition might be taking place and the risk of it occurring. Oftel's market reviews (paragraph 2.5), together with its on-going work to promote competition, inform it of how the telecommunications market is developing. This information is then shared at senior levels within Oftel.

2.15 In practice, Oftel-initiated investigations can start from a variety of sources and cover such matters as predatory pricing and access by other suppliers to BT's network. While the majority arise from existing investigations, other sources include discussions with the industry, Oftel's general monitoring of companies and the outcome of its market reviews. Decisions to launch investigations are made by Oftel's Compliance Management Board³³ which meets weekly to ensure rapid decision making. Oftel, however, sees complaints from suppliers as the best indicator of what they feel is inhibiting competition. In Oftel's view, its approach reflects its statutory *duty* to resolve complaints and its statutory *power* to investigate, along with its commitment to proportionate and targeted regulation.

Oftel has a flexible approach to resolving disputes

2.16 Oftel set out in its 2001 Annual Report some types of behaviour it described as anti-competitive that had persisted from the previous year, but it has not provided an overall assessment of what it has achieved in investigating and stopping such behaviour. We reviewed the outcomes of the 187 investigations completed by Oftel in the two years to June 2002. Oftel found grounds for taking action in 62 cases (33 per cent) (Figure 8). Although these cases involved a wide range of matters, there were four common themes (Figure 9). Oftel found no grounds for action in 109 cases, and of the remainder most were withdrawn or subsumed into other cases.

Oftel uses a mix of formal and informal action

2.17 Oftel's policy is to keep regulatory action to the minimum necessary to achieve its aims. It took formal regulatory action in 19 of the 62 cases (31 per cent)³⁴. Where Oftel considers such action is needed, it can:

- issue *Directions* or make *Determinations* to require a company to behave in a particular way (for example, where there has been a dispute over interconnection or the interpretation of licence conditions). Oftel issued a Direction or made a Determination, including draft Directions and Determinations, in each of the 19 cases (examples at Figure 10 overleaf).

8 Outcome of Oftel's investigations, July 2000 to June 2002

Outcome of investigation	Number of cases	Percentage
Grounds for action	62	33
No grounds for action	109	58
Other	16	9
Total	187	100

Source: National Audit Office analysis of Oftel data

9 Common grounds for taking action found by Oftel in cases completed between July 2000 and June 2002

Type of behaviour by suppliers	Number of cases	Percentage of cases
Unfair contract terms (conditions that are unjust for the supplier's customers or its competitors)	8	13
Failure by suppliers to reach agreement on matters related to interconnection (disputes over price and the practical arrangements)	7	11
Wholesale charging (not giving reasonable notice for imposing new billing system)	7	11
Failure to provide number portability (the process of letting customers keep their existing telephone number when they transfer to another supplier)	4	6

Source: National Audit Office analysis of Oftel data

- make *Orders* under the 1984 Telecommunications Act to require compliance with licence conditions where it considers that a supplier is likely to continue breaching its licence. Orders can be *provisional* (with immediate effect and lapsing after two months unless confirmed) or *final* (where, after a 28 day consultation period, the obligation continues until the Order is withdrawn). Orders give rights to third parties subsequently harmed by a continued breach, notably the right to claim damages. Oftel did not make Orders in any of the 19 cases.

33 The Compliance Management Board, which comprises senior managers and specialists, was established to ensure that casework as a whole is suitably resourced and progressed as quickly as possible.

34 In one further case, a determination request was withdrawn when both parties agreed to Oftel's proposals.

10 Examples of Directions and Determinations made by Of tel, July 2000 to June 2002

Directions

- With regard to the co-location of network equipment in BT's exchanges by its competitors, Of tel required BT to meet all requests except where these are technically impracticable or would impair the integrity of BT's systems (October 2001).
- Of tel required BT to allow its competitors unescorted access to BT's exchanges in order to carry out maintenance of their equipment to provide broadband services to customers (December 2001).
- Of tel issued a direction to BT and another company to resolve a dispute over the interpretation of their Interconnection Agreement with regard to discounts (May 2002).

Determinations

- Of tel resolved a dispute between BT and its competitors regarding the charges and responsibilities for links to BT's national transmission system (June 2001).
- Of tel determined the level of charges that BT could levy on its competitors for using its facilities to enable carrier pre-selection to operate (February 2002).
- Of tel required four telephone companies to migrate to a new metering scheme that could improve the accuracy of bills (June 2002).

Source: Of tel

11 Examples of cases that were resolved without formal action between July 2000 and June 2002

- A telephone company complained that BT had refused to offer a retail price for a particular service. The complainant re-submitted its request to BT under the correct procedure and, following a technical change by BT, BT agreed to the required payment arrangements (February 2001).
- Of tel received complaints that BT's planned new voice messaging service, BT Answer, was incompatible with carrier pre-selection. Following discussions with Of tel, BT agreed to make certain adjustments to its procedures (April 2001).
- Following a complaint from a local authority trading standards service about unfair contract terms, a company agreed a number of amendments with Of tel (December 2001).
- Several competitors to BT claimed that a new contract clause for the supply of retail leased lines gave BT undue preference. BT agreed to remove the clause (March 2002).

Source: Of tel

- use its enforcement powers under the Competition Act 1998 (paragraph 2.11). Of tel has not yet concluded any investigations under the Competition Act that in its view required it to take formal enforcement action.

2.18 For the remaining cases (69 per cent), Of tel felt that it could rely on the companies to implement the action agreed with them, thereby resolving these cases without the need for formal action. Of tel considers this to be appropriate where it is satisfied that the matter can be resolved voluntarily. In some cases Of tel can get as far as drafting a Direction or Determination before companies agree to modify their behaviour. Examples of cases resolved without formal action are set out in **Figure 11**.

2.19 We sent a questionnaire to the 83 organisations, mainly companies in the telecommunications industry, involved with the investigations that Of tel had completed in the two years to 30 June 2002. The questionnaire sought their views and experiences of how investigations had been handled. We received 35 (42 per cent) completed questionnaires, 27 from complainants, six from those that had been the target of an investigation, and two that had been both a complainant and a target. The comments provided in questionnaire responses might have been influenced by the outcome of investigations and might also represent respondents' perceptions. It is, however, Of tel's responsibility to ensure that suppliers, particularly new entrants, have confidence that they will be protected from anti-competitive behaviour. If that confidence is dented, even if due to misconception, this is a potential problem for the market.

2.20 Two thirds of complainant companies consider that Of tel's investigation and enforcement action has an effect in deterring anti-competitive behaviour. Several companies, however, expressed some concerns:

"Until such time as Of tel finds that a company has behaved anti-competitively AND penalises them, there can be no effective deterrent"

Of tel monitors companies' compliance with agreed remedial actions

2.21 Of tel adopts a flexible approach in monitoring whether companies have complied with the course of action required of them or agreed with them. It makes decisions about which cases to monitor on a case by case basis depending on the action required of companies and the risk of non-compliance. In many cases, Of tel does not impose an on-going burden of regulatory monitoring:

- where companies take prompt action to rectify their behaviour, Oftel may conclude that no further action is needed;
- where Oftel considers that non-compliance will soon become apparent, for example with its Determinations about interconnection charges, it awaits further complaints.

2.22 Where Oftel considers that there is a risk that the problem will persist, it keeps the case under review and establishes monitoring criteria. Oftel's Compliance Monitoring Unit, set up in April 2000 to strengthen its monitoring arrangements, oversees all cases under review. Where it considers it necessary, Oftel requires the company concerned to produce a plan for achieving compliance and providing Oftel with information, such as financial returns, on a regular basis. Oftel examines this information to determine whether the company is complying with the actions agreed, and to decide whether further regulatory action or monitoring is required or whether the case can be closed.

2.23 Of the 19 investigations completed between July 2000 and June 2002 where Oftel took formal regulatory action, seven were reviewed in the compliance phase. All of these were resolved satisfactorily. Oftel also reviewed four cases where it had not taken formal action. In November 2002, Oftel was actively monitoring five cases (Figure 12).

2.24 Where decisions are taken not to keep cases under review, companies are not required to confirm in writing that they have done what was required. Nor are complainants asked, say six months later, to confirm that their complaint has been addressed. Oftel takes the view that if the problem persists, the complainants will complain again. One of the companies we surveyed expressed concerns about the effectiveness of Oftel's compliance arrangements:

"Once investigated, all parties were agreed on the course of action to be taken in conjunction with BT. Nearly two years later, the work is still not completed".

"The investigation was good. But the follow-through to ensure BT implements the deal has been very poor and has dragged on interminably".

Oftel is seeking to speed up its investigations

2.25 Timely completion of investigations is important in limiting the amount of detriment to consumers and the commercial damage suffered by companies that are in dispute. From 1998 to 2001 Oftel sought to improve its performance by:

12 Oftel's formal enforcement action at November 2002

- Two cases, in Compliance Phase since November 1997 and March 1999. A Direction was issued in response to complaints that BT was cross-subsidising its Managed Network Services Division, which supplied private networks to corporate customers. Apart from requiring no further cross-subsidy, BT was required to supply independently audited accounting data on a six-monthly basis. In Autumn 2002, Oftel conducted a consultation exercise with a view to revoking the Direction.
- In Compliance Phase since February 1998. An Oftel investigation found BT had failed properly to publish the tariffs for its FeatureNet service. BT agreed to review this area and found similar cases. As a result a Final Order was issued in 1998 compelling BT to publish an accurate and comprehensible price list in line with its licence. The Order also required BT to carry out a full review of the price list and notify Oftel of any errors and omissions within six weeks, and to prepare a compliance plan - both of which have been done. The Order still requires BT to comply with its licence obligations in relation to price publication. For most services this is now one day rather than 28 days, so BT is able to correct any errors instantly.
- In Compliance Phase since July 2002. A telephone company had breached its licence by failing to provide the TextDirect service due to technical constraints. An interim solution, not required but agreed with Oftel, resulted in the TextDirect service being provided, but the company is currently unable to bill for the service. Oftel is monitoring the implementation of the permanent solution, in line with the agreed action plan.
- In Compliance Phase since November 2002. A telephone company had contravened its licence by refusing to provide full number portability having been requested to do so by BT. The company is now working to complete its technical preparations and expects to be able to meet its obligation to provide portability to BT in January 2003. The case was moved into Compliance pending completion of these preparations.

Source: Oftel

- devoting more staff resources to investigations;
- improving staff retention and providing better training³⁵;
- introducing a new management information system to improve day to day control;
- updating its manual of procedures for undertaking investigations;
- clarifying the role of its Casework Panel (a formal internal group comprising specialists, managers and caseworkers to ensure consistency of decision making).

35 Poor staff retention was a particular concern of the Committee of Public Accounts in 1998.

2.26 Despite these changes, the investigations completed by Oftel in the two years to June 2002 took on average nearly 27 weeks to complete³⁶. This compares with 23 weeks for the six months ending June 1997, when we last examined Oftel's work in this area.

2.27 Oftel considers its slower performance has been due in part to the marked increase in the complexity of cases arising from the greater number of competitors in the telecommunications market and their increased interaction. Oftel's internal quality assurance appraisals, however, found that many cases featured lengthy periods when no progress was made. To identify the main reasons for these periods of inactivity, we analysed Oftel's assurance appraisals for the cases completed in 2001³⁷ and found that delays had mainly arisen due to:

- the need to re-assign cases due to changes in staff;
- problems with case planning and day-to-day management;
- delays in obtaining expert legal and economic advice;
- delays in receiving information from the companies involved in the case.

2.28 Overall, half of the companies that responded to our survey were "satisfied" with the time taken to investigate the allegation, but 29 per cent of complainants were "very dissatisfied". Some examples of companies' concerns are:

"Long, unexplained gaps prolonged uncertainty and stalled some commercial initiatives as a result"

"Given that the complaint made was not a complex one, it is disappointing that Oftel took more than four months to reach a conclusion from the date of our initial complaint"

Oftel is introducing a new approach so as to accelerate investigations

2.29 The April 2002 European Union Framework Directive, which must be implemented no later than July 2003, introduces new arrangements for resolving disputes between telecommunications suppliers. It requires the relevant national regulatory authority to issue a binding decision on disputes within four months, except in exceptional circumstances. Oftel is intending to introduce this new target for resolving disputes from April 2003. The Directive will not apply to Oftel's own - initiative investigations, which are normally wider in scope, though Oftel is publicly committed to completing these promptly.

2.30 In Spring 2002, in anticipation of the impending changes required by the EU and in order to improve the timeliness and quality of its investigations, Oftel implemented a substantial re-organisation of the way it manages investigations:

- it established its Compliance Management Board, comprising senior managers and specialists, to improve overall control of investigations. The Board ensures that casework is suitably resourced and progressed as quickly as possible;
- case management has been re-organised. A *Case Leader* is appointed to manage each case, with a *Case Sponsor* assigned to oversee and guide progress;
- Oftel introduced more flexible staffing arrangements and set up a new financial analysis unit to streamline economic and accounting input;
- *Case Leaders* use their extensive training to complete an initial analysis of each case and to prepare a case plan. Each plan is endorsed by the Compliance Management Board;
- information is gathered using the stronger powers provided by the Competition Act 1998 (paragraph 2.11), with deadlines for the return of information;
- the number of specialist advisors (lawyers, economists, accountants and technicians) within Oftel has been increased from 19 at the start of 2002 to 23 in January 2003.

2.31 Oftel is monitoring the impact of its organisational changes. Figures provided by Oftel show that cases both opened and closed in a calendar year took an average of 13 weeks to complete in 2002 compared to 20 weeks in 2001³⁸.

2.32 Oftel intends to supplement its management changes with improvements to the way it conducts investigations and has consulted stakeholders on this. From April 2003, Oftel will exert greater control over the cases it investigates and the way investigations are handled (**Figure 13**). In particular, there will be a more vigorous approach to defining individual complaints and stricter requirements for submitting information. Oftel does not, however, propose to routinely meet companies as part of its investigations.

2.33 As part of its revised approach, Oftel is unlikely to adjudicate in disputes between operators that do not have a dominant market position and will encourage them instead to use some form of alternative dispute resolution, as allowed by the European Framework Directive. Oftel forecasts that this will reduce the number of cases by up to 10 per cent. The organisational

³⁶ This excludes two cases not pursued by the complainants and which were closed straight away.

³⁷ This analysis formed part of our preliminary examination in Spring 2002.

³⁸ 43 cases were opened and closed in 2001 (representing 57 per cent of all those opened in that year) and 53 (72 per cent) in 2002.

13 Main changes proposed from April 2003 to the way OfTel handles investigations

Existing arrangements	New arrangements
<ul style="list-style-type: none"> ■ No mandatory form for a request to resolve a dispute ■ OfTel rarely rejects a request to resolve a dispute 	<ul style="list-style-type: none"> ■ Mandatory format and content ■ Inadequate submissions will be rejected ■ Alternative dispute resolution procedures to be used for parties that are not dominant
<ul style="list-style-type: none"> ■ Scope of dispute considered as part of investigation ■ Informal approach to gathering information ■ No time limit set for gathering information 	
	<ul style="list-style-type: none"> ■ Scope will be settled before investigation starts and only changed in exceptional circumstances ■ Normal practice will be to use formal powers under the Competition Act 1998 ■ OfTel will make a decision, on the best information available, on a deadline for the submission of information

Source: OfTel

changes introduced or planned by OfTel are intended not only to speed up investigations but also to identify earlier those cases where there are no grounds for regulatory action. Such cases accounted for 58 per cent of the investigations completed in the two years to June 2002 (Figure 8).

2.34 OfTel chairs the International Regulators Group's Implementation Working Group for the new EU Directives. This Group was set up in mid-2002 to develop processes and procedures, and to identify approaches which harmonise implementation of the Directives. OfTel is also currently involved in discussions with other National Regulatory Authorities about dispute resolution under the new EU Directives and about the resolution of cross-border disputes. At February 2003, OfTel was engaged in discussions about a workshop, planned for September 2003, to be hosted by OfTel and involving all European regulators, to examine the process of dispute resolution, identify best practice and critical factors for efficient case handling.

OfTel assesses the quality of its investigations

2.35 OfTel's internal assessment of its investigations into anti-competitive behaviour concluded that, for those completed in the two year period July 2000 to June 2002, 56 per cent were 'good' or 'very good'. Most of the remainder were 'satisfactory'. This is supported, in broad terms, by feedback from the companies that responded to our survey. Although companies' views about the overall quality of investigations were very mixed, companies were more positive about key attributes of OfTel's investigations (Figure 14). In particular, 25 out of 34 respondents felt OfTel understood the main issues involved and 21 out of 32 respondents considered that OfTel's investigations were thorough.

2.36 In attempting to meet the new four month deadline, there is a risk that the quality of OfTel's investigations will be compromised. For example, one of the companies that responded to our survey commented that "it was clear that timescales for a resolution became more important than a fair resolution". OfTel considers that it achieves high quality investigations and consistent decision making.

14 NAO survey results on the quality of OfTel's investigations

Topic	Very Good	Fairly Good	Not Very Good	Poor	Total
Overall quality of OfTel's investigations	8	8	10	9	35
OfTel's understanding of the main issues	16	9	8	1	34
Thoroughness of OfTel's investigations	11	10	7	4	32
Keeping parties to investigations informed of OfTel's progress	15	7	10	3	35

Source: Respondents to a National Audit Office survey in September 2002 of complainants and targets of investigations

Appendix 1

Study methodology

The key elements of our study methodology are set out below.

Analysis of telecommunications companies' tariff data

Using an illustrative profile of a consumer (in terms of number and types of calls made), we compared prices for a selection of fixed line tariffs from different companies and identified ways of saving money (Appendix 2).

Analysis of consumer preferences

We commissioned Ipsos-Capibus Limited to carry out an omnibus survey of 2,100 adults in the United Kingdom (Appendix 3). This provided up to date information on consumers' views and experiences about telecommunication services, including their priorities and the factors that would motivate them to change their arrangements. We analysed the results to assess the importance of characteristics such as age, location, social grade and the level of expenditure. We also examined the results of Oftel's own consumer research.

Review of Oftel's investigations into alleged anti-competitive behaviour

For anti-competitive behaviour investigations completed by Oftel during the two years ending 30 June 2002, we analysed Oftel's records to establish how long individual investigations had taken and to identify the reasons for delays in completing investigations.

Survey of telecommunications companies

We sent a questionnaire to 83 organisations, mainly companies in the telecommunications industry, that had been involved with the investigations of anti-competitive behaviour that Oftel had completed in the two years to 30 June 2002. The questionnaire sought their views and experiences of how investigations had been handled. We received 35 (42 per cent) completed questionnaires, 26 from complainants, six from those that had been the target of an investigation and two that had been both a complainant and a target.

Seeking the views of interested parties

As well as speaking to key staff at Oftel, we obtained the views of selected companies from the telecommunications industry and other interested parties:

- BT plc
- Centrica plc (parent of One.Tel)
- Telewest Communications plc
- Vodaphone plc
- Department of Trade and Industry
- National Consumer Council
- Consumers' Association

Expert Panel

We set up an expert advisory panel to provide us with informed comment on the scope of our study, study methods, findings and conclusions:

Panel Member	Details
Constantina Bichta	Research Officer at the Centre for the Study of Regulated Industries, University of Bath School of Management
Professor Martin Cave	Director of the Centre for Management under Regulation at Warwick Business School
Jill Johnstone	Head of Policy, Research and Strategy at the National Consumer Council
Professor Howard Williams	Strathclyde Business School, University of Strathclyde.
Ken Young	Head of Corporate Communications, Department for Work and Pensions

We thank the members of our expert panel, together with those we consulted and staff within Oftel, for their assistance in completing this study.

Appendix 2 Savings for consumers

- Using the results of our analysis of telephone companies' tariffs, we quantified some of the savings that consumers can make on their fixed line telephone services. We considered what individual customers of BT could save, or lose, by changing from one of a series of popular BT tariffs to their price optimal tariff, with BT or another supplier, taking full advantage of BT's discount schemes.
- The starting point for our calculation was Oftel's five main types of fixed line consumer³⁹, and the detailed call profile that Oftel has prepared for each type. To reflect on-going change in telephone use, we amended Oftel's medium user profile to include 20 minutes of internet usage per week. The user types are shown below in **Table 1**.
- In calculating the savings available to each type of user, our analysis closely followed the methodology of Oftel's international benchmarking study of June 2001. **Table 2 overleaf** is an extract of the type of data provided by that study. For the full source information, please refer to Annex F of Oftel's 'International benchmarking study of dial-up PSTN Internet access, mobile and fixed line services' (June 2001).
- We extracted details of BT's residential tariffs and discounts from its website and calculated the resultant annual cost using the illustrative user profiles above.

Our calculations include a number of assumptions:

- tariff prices are inclusive of VAT;
- international call charges are split in proportion to the direct dialling volume rates (as published by Oftel in 'Market Information: Fixed Update, August 2002 Q4 2001/02');
- calls to mobile telephones are split between the different national networks in proportion to the volume market share of those networks (as published by Oftel in 'Market Information: Mobile Update, July 2002 Q4 2001/02');
- consumers access the internet using a 'subscription free' Internet Service Provider and pay standard local call charges;
- All non-recurring charges (for example, installation charges) have been depreciated over five years and included in the calculation of annual telephone charges;
- Number porting charges are not included;
- Some operators levy a connection charge for each call. These have been included in the calculation of the annual telephone charges.

A summary of the calculations is shown in **Table 3 overleaf**.

Table 1: User types

Call profile	User Type	User characteristics
1	Lowest usage	The phone is mainly kept for security reasons, with very few outgoing calls.
2	Low usage	Lower than average usage - mostly national calls but with a small proportion of mobile and international calls.
3	Medium usage	Represents a median residential user. Some mobile and international calls are made. Most calls are off-peak.
4	High usage	Above average usage. Some international calls are made, and mobile phones are called regularly. Some internet usage is included. Most calls are off-peak.
5	Highest usage (2 lines)	Usage level well above average. A reasonable amount of international calling, and many calls to mobile phones. Internet usage justifies a second line. Most calls are off-peak and local.

Source: Annex F, Page 39 of Oftel's 'International benchmarking study of dial-up PSTN Internet access, mobile and fixed line services' (June 2001)

³⁹ The five types range from those that use their home telephone infrequently to those who use it a lot. Oftel's management plan outlines a sixth consumer type - an individual with no fixed line telephone.

Table 2: Annual call profile for a medium user

Measure	Local/ regional calls	National calls	Calls to international numbers	Calls to mobile numbers	Internet use	Total
Call duration (minutes)	4797	623	90	117	1040	6667
Number of calls made	827	123	20	30	50	1050
Average call duration (minutes)	6	5	5	4	21	6

Source: Ofcom's 'International benchmarking study of dial-up PSTN Internet access, mobile and fixed line services' (June 2001), with internet use added by the National Audit Office.

Table 3: The annual cost of BT's main residential tariffs and discounts (Note 1)

Tariff	Basket				
	1	2	3	4	5
BT Standard	£137	£155	£319	£584	£1,491
BT Standard Line & an indirect access operator for all calls	£134	£147	£267	£452	£1,236
BT Standard with Residential & International Friends & Family	£141	£158	£315	£570	£1,449
BT Standard with Residential Friends & Family	£137	£155	£313	£572	£1,459
BT Together	£153	£158	£274	£464	£1,209
BT Together & an indirect access operator for international calls	£153	£155	£259	£419	£1,099
BT Together with Friends & Family	£153	£157	£269	£451	£1,175
BT Together with unlimited local calls	£199	£215	£313	£475	£1,176
BT Together with unlimited local calls & an indirect access operator for international calls	£199	£213	£298	£430	£1,066
BT Working Together	£249	£249	£296	£485	£1,230
Light User Scheme	£88	£165	N/A	N/A	N/A
BT Broadband	£519	£543	£645	£821	£1,519

NOTE

1. The Light User Scheme tariff is not available to customers with call profiles 3 - 5 (Table 1). For completeness, the annual cost of the other tariffs listed here is shown for all the profiles. In practice, it is unlikely that all of these tariffs will be relevant to all profiles. For example, Profile 1, which covers customers that make very few outgoing calls, is unlikely to be relevant to BT Broadband, a tariff designed for those who use their telephone to access the internet.

Source: National Audit Office calculation

5. The calculation of savings available to an average user making international calls with an indirect access operator as opposed to BT's *Standard* tariff, including discounts, (referred to in paragraph 1.49) is set out in **Table 4**.

Table 4: Saving on the weighted average International Direct Dial cost

Provider	Peak	Off - Peak	Weekends	Volume Weighted Average
BT Standard, including discounts	30p	27p	25p	27p
Representative indirect access operator	11p	11p	11p	11p
Saving	19p (63%)	16p (59%)	14p (56%)	16p (59%)

Source: National Audit Office

Appendix 3

Results of the National Audit Office survey of residential users of fixed line telephone services

We commissioned Capibus (Ipsos-RSL Ltd) to carry out a survey of 2107 adults aged 15 years and older to obtain the views and experiences of the general public on telephone services in the United Kingdom. The survey was conducted by interview between 30 August and 5 September 2002. The findings are statistically correct to plus/minus two percentage points. This Appendix sets out the main findings.

Most people spend less than £100 per quarter on their fixed line telephone services

Less than two out of ten respondents spend more £100 per quarter on fixed line telephone services. There were significant variations by age and within social groups, with those aged over 65 years and in social groups DE spending least.

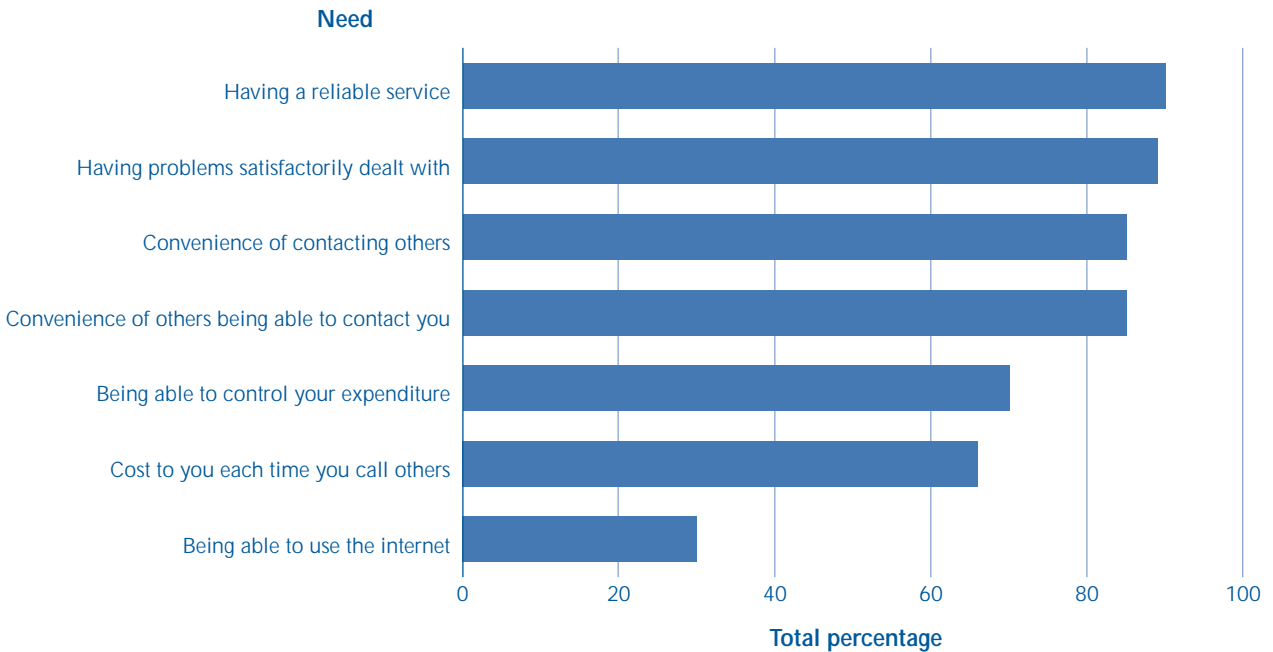
Spend per quarter	Total (%)	Age (%)						Social group (%)			
		15-24	25-34	35-44	45-54	55-64	65+	AB	C1	C2	DE
Less than £50	42	39	38	32	31	48	62	29	43	42	54
£50 - £100	43	41	47	47	48	38	34	49	40	44	38
Over £100	15	20	15	21	21	14	4	22	17	14	8

Sample size 1,686

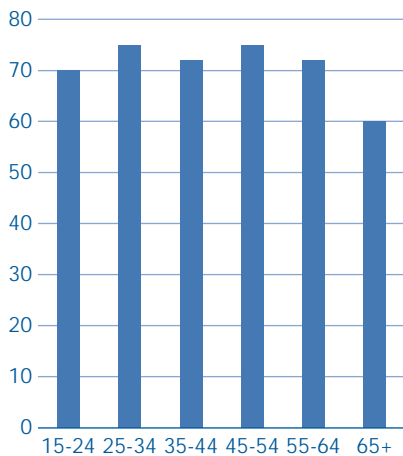
Service is more important to people than cost

For home telephone services, respondents rated service reliability and problem resolution much higher than cost or being able to control expenditure. Convenience was also rated higher than financial considerations, but lower than service. Being able to use the internet was least important of the seven 'needs' covered by the survey. Although age did not affect the relative importance of these seven needs, financial considerations and the internet were rated lower by older respondents than by younger ones.

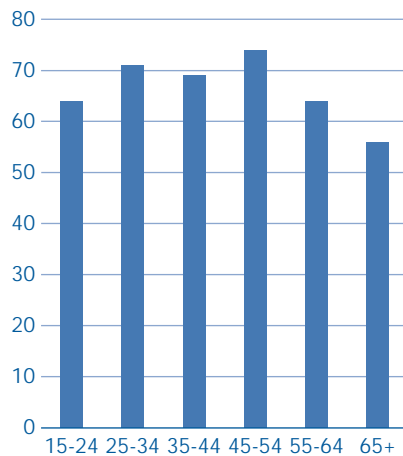
Proportion saying 'essential' or 'very important'



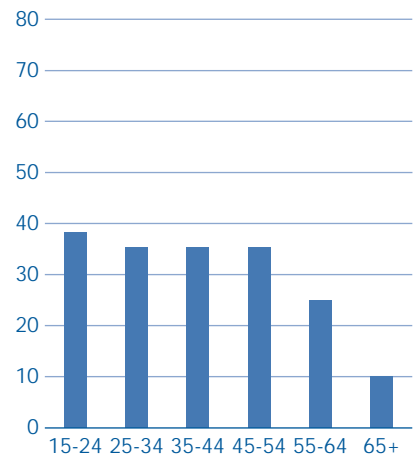
Being able to control your expenditure (%)



Cost to you each time you call others (%)



Being able to use the internet (%)



Age

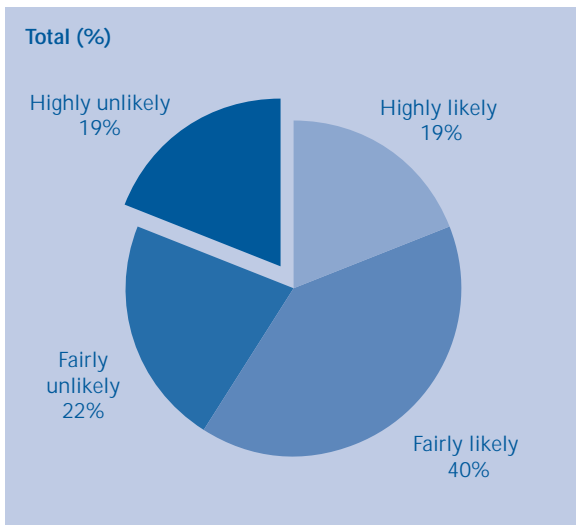
Sample sizes 1,998-2,049

Poor service would motivate many people to change their telephone company

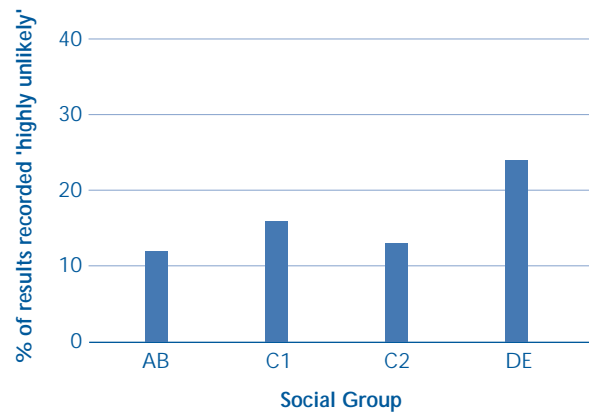
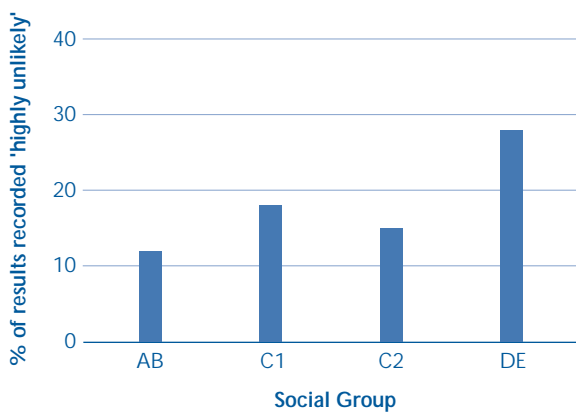
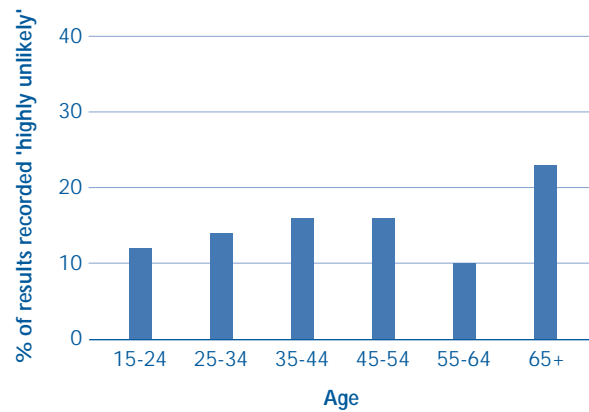
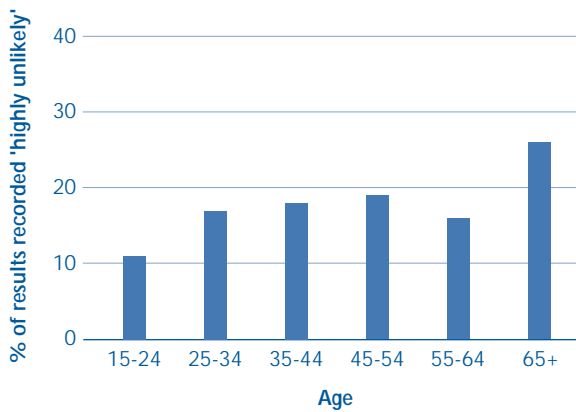
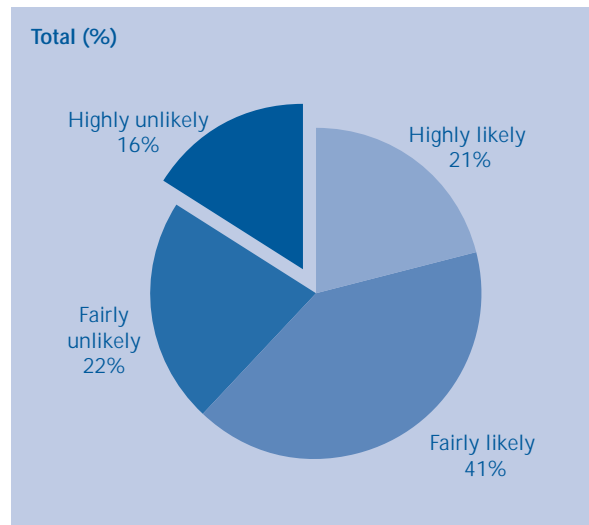
About six out of ten respondents said they would be 'highly likely' or 'fairly likely' to change the company providing their home fixed line telephone if they had problems making or receiving calls, or they were unhappy about the way a complaint was handled. But nearly two out of ten were 'highly unlikely' to change, particularly retired people and those in social groups DE.

Likelihood that respondents would change their home telephone company

If there were problems making or receiving calls (%)



If unhappy about the way a complaint was handled (%)



Sample sizes 1,820 (having problems) and 1,813 (complaint handling)

Savings would also motivate many people to change their telephone company

The likelihood that financial savings would motivate respondents to change the company providing their residential fixed line telephone, or make changes with their existing supplier, increases with the size of the savings. But a significant minority are unlikely to change, even if the savings are 40 per cent. Paragraph 1.23 of the main report looks at the findings in more detail.

In the last two years, most people have made no changes to their home telephone service

Nearly seven out of ten respondents have made no changes to the way they buy their residential fixed line telephone service in the last two years. Two out of ten, however, have chosen different tariff packages or discounts, and one of ten had changed or added to the companies they use. Respondents from social groups DE, the over 65's, and those spending under £50 per quarter had made the fewest changes.

By expenditure (per quarter)

	Total (%)	<£50 (%)	£50-£100 (%)	>£100 (%)
Changed or added to the companies used	11	8	15	11
Made tariff and discount changes with existing company	21	17	22	32
Made no changes	68	75	63	57

By age and social group

	Age (%)						Social group (%)			
	15-24	25-34	35-44	45-54	55-64	65+	AB	C1	C2	DE
Changed or added to the companies used	11	14	14	13	12	6	14	11	12	9
Made tariff and discount changes with existing company	22	24	18	27	21	14	26	21	19	16
Made no changes	67	62	68	60	67	80	60	68	69	75

Sample size 1,800

People say that making changes to telephone services has been easy in the last two years

The majority of respondents said they found the steps in the switching process to be 'easy' or 'very easy'.

Step	Very easy (%)	Easy (%)	Total (%)
Identifying the companies offering the services wanted	51	42	93
Getting information from companies	46	45	91
Understanding the information provided by companies	38	47	85
Making comparisons about prices	34	44	78
Making comparisons about quality of service	26	44	70
Completing the paperwork	37	56	93

Sample size 207

Many people are not aware of indirect access operators

Spontaneous awareness of indirect access operators was low, with four out of five respondents not being able to name a single company. Awareness was lowest amongst those aged over 65 years and those in social groups DE.

Respondents not aware of indirect access operators:

By age and social group

	Total (%)	Age (%)						Social group (%)			
		15-24	25-34	35-44	45-54	55-64	65+	AB	C1	C2	DE
Spontaneous	77	79	72	72	76	74	87	74	69	77	87

By region

	Scotland (%)	North (%)	Midlands (%)	South (%)	London (%)	Northern Ireland (%)
Spontaneous	78	76	79	79	70	82

Sample size 2,107

Appendix 4

Summary of findings of the Committee of Public Accounts in their 1998 Report 'Countering anti-competitive behaviour in the telecommunications industry'

Main points

- The telecommunications market is developing and changing rapidly, and speedy action by Of tel is critical in preventing anti-competitive behaviour by dominant companies from damaging smaller businesses and hurting consumers. Of tel's efforts to be more pro-active in initiating more investigations into alleged anti-competitive behaviour, as well as responding to complaints, are welcome.
- In order to undertake effective investigations and negotiations with dominant companies in the telecommunications industry, who have considerable resources and expertise at their disposal, Of tel needs staff with relevant experience at senior levels in commercial organisations. And it will be important for it to press ahead with their proposed training programme so staff can operate effectively under new competition legislation.
- There is a need for greater transparency and clarity in pricing structures if consumers are to make informed choices between different operators' services. Of tel should take swift action if it finds companies' tariff structures to be anti-competitive or detrimental to consumers.

Summary of specific conclusions and recommendations

On investigation and enforcement

- In a number of cases, enforcement action was not taken because the parties reached agreement between themselves or the operator stopped the alleged anti-competitive behaviour. Nevertheless, taking enforcement action at an earlier stage in more investigations would send a clearer message to the industry that Of tel is committed to tackling anti-competitive behaviour.

- Around 90 per cent of the investigations into anti-competitive behaviour undertaken between 1995 and 1997 originated from complaints received from companies in the industry. Of tel initiated only 10 per cent itself. The proportion of investigations initiated by Of tel has since risen to 20 per cent and there are other areas where it seeks to resolve problems before complaints are made. Of tel should ensure that it is not too reactive in dealing with anti-competitive behaviour.
- It is Of tel's assessment that, as a result of a series of cases leading to enforcement action, BT is giving higher priority to compliance. This underlines the importance of Of tel taking enforcement action in all appropriate cases.
- After enforcement action has been taken, Of tel largely relies on the original complainant to let them know if the anti-competitive behaviour persists. This absence of follow-up by Of tel runs the risk that such practices may continue and Of tel should follow up more systematically the actions it takes to stop anti-competitive behaviour.
- Of tel has set itself more demanding targets for the speed with which it handles investigations of anti-competitive behaviour. Although it is not yet meeting these targets, its performance has improved. As telecommunications is a fast moving industry where speed of action is critical, there should be no significant slackening in Of tel's targets for completing investigations of anti-competitive behaviour.

On staffing

- In Of tel's view it is under-resourced in certain areas and its work could be organised better and made more effective. It should complete its review of staffing and organisation as a matter of priority. Of tel should pursue its intention of agreeing a three-year budget with the Treasury that is sufficient to meet its needs.

- Oftel is constrained from offering senior staff rates of pay that compare with those in the private sector, and there is a lack of high level experience of commercial organisations. It is important that Oftel staff understand through practical experience the commercial pressures that businesses are under and what motivates business decisions. Oftel should seek to increase its expertise and experience in this key area.

On wider issues and future developments

- Oftel aims to give an increased focus to consumers in countering anti-competitive behaviour. Oftel has generally relied on discussions with consumer representative bodies to obtain the views of consumers, but has now commissioned a survey of customers' views on key issues. This development will enable Oftel to test consumer opinion directly.
- If customers are to be able to distinguish between rival companies, tariffs need to be transparent and easy to understand. But tariff structures are complicated and confusing for the consumer. Oftel recognises this problem and is currently investigating it, and expects to complete its research by the autumn of 1998. Oftel should act firmly on any evidence of anti-competitive behaviour or consumer detriment on the part of the companies concerned.

- The new competition legislation will significantly increase Oftel's powers, giving it authority to take interim action and to impose fines. Oftel will need to ensure that it is fully prepared to meet this challenge. Re-skilling and retraining may be necessary in certain areas. Oftel has already taken steps to improve training and produce a manual addressing the practical issues expected to arise. This momentum should be maintained.
- Oftel accepted the recommendations in the C&AG's report for improving its speed and effectiveness in countering anti-competitive behaviour. Oftel has prepared an action plan containing specific action points and a timetable for implementation which should result in all the recommendations being implemented by March 1999.