DO THE UK REGULATORY AGENCIES PROVIDE TAXPAYER VALUE?

Keith Boyfield and Tim Ambler

Centre for Marketing Working Paper
No. 04-902.1
March 2004

Keith Boyfield is an economist and freelance writer
Tim Ambler is a Senior Fellow at London Business School
London Business School, Regent's Park, London NW1 4SA, U.K.
Tel: +44 (0)20 7262-5050 Fax: +44 (0)20 7724-1145
http://www.london.edu/Marketing
Copyright © London Business School 2004
DO THE UK REGULATORY AGENCIES PROVIDE TAXPAYER VALUE?

Keith Boyfield and Tim Ambler

Abstract

This paper questions the extent to which the economic regulatory agencies provide value for money for the taxpayer. Over the last twenty years, they have grown in number, roles and costs to the point where their purposes may seem to have become confused. Originally they were temporary institutions to maintain proxy competitive markets whilst introducing true competition. Since 1997, they have been given a variety of social and quality control roles. The table below shows the increase in costs and headcount.

<table>
<thead>
<tr>
<th></th>
<th>1996/7</th>
<th>2002/3</th>
<th>FSA</th>
<th>Like for like % increase</th>
</tr>
</thead>
<tbody>
<tr>
<td>Expenditure £M</td>
<td>141.5</td>
<td>481.5</td>
<td>221</td>
<td>80</td>
</tr>
<tr>
<td>Headcount</td>
<td>2,061</td>
<td>4,879</td>
<td>2,313</td>
<td>23</td>
</tr>
</tbody>
</table>

By 1997, 11 regulatory agencies had been created, excluding related consumer monitoring groups. Since then, some new regulators have been established by the Labour government but the more important trend is the consolidation into larger units, such as OFCOM, and their new much wider remit spanning consumer affairs and information and educational matters. Examples of this trend include OFCOM, launched as a consolidated regulator for the communications and broadcasting sectors, which started work in January 2004.

All these regulatory bodies, along with the cluster of statutory consumer panels established in recent years, form part of government. The paper excludes, except by way of comparison, wholly voluntary regulators such as the Advertising Standards Authority and business regulation in general.

After reviewing the development, activities, costs, staffing, criticisms and plaudits for the offices of regulators, the paper identifies the key areas for clarification:

- Consumerist groups have become competitive with the regulators and should be cut back to advising the supplier boards.
- Regulators should not be responsible for vague goals well beyond their resources or remit, e.g. universal financial education by the FSA
- Demands for “accountability”, which turned out to mean reporting to Ministers, have compromised independence. Regulation should not be responsible for major initiatives or social policy but policing their original economic role to protect consumers. They
should answer to parliament. Policy is for government departments and the appellate system belongs to the courts.

- The other major area for the newer regulators (OFCOM, FSA) is product quality. This should not be a matter for government but returned to the industries once they have convinced government that the new arrangements would have teeth.

Two alternatives are presented. The more radical closes all regulators as soon as they have completed their, perhaps accelerated, task of bringing in competition apart from a small “Fair Trading Authority” modelled on the OFT but more selective in the number and depth of hypothesised transgressions it investigates. The less radical reverts, in essence, to the situation in 1997 with regulators reduced in size and scope and comparable with those in France and Germany. The more radical would improve Taxpayer Value by about £494m p.a. and the less radical by about £329m.

However, this analysis of the costs of regulators takes no account of the benefits from these offices. This is because the regulators do not report any such benefits and we therefore have no data. It is remarkable that these expanding functions are so blind to the benefits for the taxpayer. The FSA’s annual report, for example, gives no indication of what “success” means nor what measures identify progress toward that success.

The measure of success for the original regulators was clear enough: to establish competitive markets and leave the stage. OFTEL having nearly reached that point should be planning its demise but instead it is preserved for posterity within OFCOM.

Consideration of benefits prompts a fundamental review of how the roles of the offices of the regulators have changed. Today the regulators, notably the FSA, no longer have the development of competitive markets as their primary goal. They see themselves as police forces, if not gaolers, with permanent responsibilities to protect consumers and pursue the interests of government.

This is a serious shift of orientation and almost certainly negative for GDP. One might wonder if the regulators have forgotten that free market business profits provide the wealth and the taxes for the country as a whole.

Reverting to sector regulators, even with smaller budgets, would not achieve the re-orientation required to drive towards wealth creation. By contrast, a single Fair Trading Authority, as distinct from a super-regulator, could intervene only in cases of uncompetitive or unfair practices. Near-monopolies would still need to obtain approval for prices until their markets are competitive but that should be the dominant objective.
DO THE UK REGULATORY AGENCIES PROVIDE TAXPAYER VALUE?

This paper questions the extent to which the economic regulatory agencies - or offices – still provide value for money for the taxpayer. Over the last twenty years, they have grown in number, roles and costs to the point where their purposes may seem to have become confused. It is time to review alternatives.

OFTEL, launched in 1984, was the first of these agencies. Other agencies, in markets dominated by privatised state monopolies, have since been established in an attempt to mimic the consumer outcomes that might be expected from competitive markets. Separate regulatory bodies were set up to oversee the telecoms, gas, electricity supply, water, rail and postal services. The idea underpinning this initiative was that as open market competition developed, the need for and therefore the regulators would fade away.

By 1997, 11 regulatory agencies had been created, excluding related consumer monitoring groups. Since then, some new regulators have been established by the Labour government but the more important trend is the consolidation into larger units, such as OFGEM, and their new much wider remit spanning consumer affairs and information and educational matters. Examples of this trend include OFCOM, launched as a consolidated regulator for the communications and broadcasting sectors, which started work in January 2004.

All these regulatory bodies, along with the cluster of statutory consumer panels established in recent years, form part of government. However, the paper excludes, except by way of comparison, wholly voluntary regulators such as the Advertising Standards Authority and business regulation in general. It simply addresses value for money of the statutory offices of regulators.

Framework of the paper

The paper has seven sections; the first five deal with the status quo and the last two consider alternatives. It opens by reviewing the original purpose of regulation, namely its role as a proxy for competition within the marketplace. The second section examines the expanding role of regulators, a trend that has significantly accelerated following the election of the Labour government in May 1997. Thirdly, the paper looks at control and accountability issues as they relate to regulators. The paper then turns, fourthly, to consider regulatory agency budgets and headcount numbers in the period 1997 - 2003. This section also refers to projected budgets and payroll numbers. The fifth section deals with OFCOM, which only began work at the start of 2004.

The sixth section sets out two alternative regulatory regimes. The first would return regulators to their original economic role with the expectation that, as competition develops, the need for these
bodies will decline. Arrangements for addressing the other acquired roles are also discussed. This removes arguably unnecessary regulatory constraints and streamlines the size and scope of current regulators.

The second option is more radical and involves establishing a single competition authority, along the lines argued by Keith Boyfield in a previous study. This ‘one agency, one law principle’ approach borrows from Australia, following the publication of the Hilmer Report in 1993. Such a radical policy redirection would be a major step for any government, and a transitional phase would be required to implement it. Nevertheless, the potential benefits to be gained from adopting this approach and the arguably decreasing value from the current regime justify its serious consideration. The present regulators were supposed to make themselves redundant through establishing competition, or the equivalent. If they have failed to do that over the last 20 years, why should we suppose the next 20 will be different?

The final, seventh, section quantifies the difference in costs for the taxpayer between these two regimes and the projected costs of the present arrangements. In principle, taxpayer value could increase by that amount since no reduction in competitiveness is envisaged. We estimate the direct savings for the taxpayer that could be achieved from aligning regulatory agencies more closely to their primary purpose. These direct savings may well be dwarfed by the additional compliance and indirect costs borne by industry. Quantifying these costs - coupled with the opportunity costs associated with management time that could be better used to innovate products and services – would require further research.

This paper reviews the costs of regulation but not the benefits. Accordingly it may seem one-sided. We consider this issue as part of the taxpayer value analysis in section seven but we should note here that none of the offices of regulators see fit to communicate any benefits for taxpayers, still less quantify them. It is just presumed that this regulation is a good thing when it may well be, net, a bad thing. It seems remarkable that these offices of state are under no pressure to justify themselves. Perhaps the sound of tumbrels rattling in their direction will at least stimulate serious study of the benefits from the offices of the regulators.

**Section One: The original purpose of regulation.**

The first nationalised monopoly industry to be privatised by the Thatcher government was telecommunications. Since a fully functioning competitive market could not be introduced immediately in either voice or data communications, it was decided to establish an economic regulator, known as OFTEL. This agency, which opened its doors for business on 1 August 1984, created the model for all subsequent regulatory bodies. Over the next decade, as a range of statutory state monopolies including gas, electricity supply, water and sewerage, coal and rail were transferred to the private sector, a raft of regulatory agencies were also launched to act as a

---

proxy for competition. In common with OFTEL, these agencies - OFFER, OFGAS, OFWAT and so on, were characterised by the prefix 'OF'.

Regulation - as it applies to the agencies created to monitor those sectors of the economy privatised since 1979 - was originally intended to provide consumers with the benefits expected from competition. They were, in effect, a proxy for competition, no more, no less. Ministers indicated that regulators would be expected to withdraw from intervention in the market and wind up their activities once the market became fully competitive. This approach to regulation was perhaps most clearly articulated by Nigel Lawson, who was appointed the Secretary of State for Energy in September 1981. Lawson looked on electricity as merely another commodity, which required no specialised regulatory oversight once the market was unshackled. This was a position he explained in a ground-breaking speech entitled, suitably enough, 'The Market for Energy':

"I do not see the government's task as being to try and plan the future shape of energy production and consumption. It is not even primarily to try to balance UK demand and supply for energy. Our task is rather to set the framework which will ensure that the market operates in the energy sector with a minimum of distortion and energy is produced and consumed efficiently."

This approach to regulation continued to be articulated by cabinet ministers throughout the Conservative administration. Ian Lang, then Secretary of State for Trade & Industry in John Major's government, exemplifies this view of regulation as a temporary necessity required to encourage a fully functioning competitive market.

"In respect of many of their functions they have finite lives", he explained. "I think it is sometimes assumed that the regulators are a permanent part of the infrastructure. I do not seem them in that context. I see them as policing the industries and regulating them in the interest of the consumer whilst the market develops and competition takes root. Some of the functions which they now perform will become redundant and in a relatively short period of time".

Looking further ahead, Ian Lang acknowledged, “There may be some elements which will

---

2 This led some commentators to christen the proposed regulatory agency dealing with access to tertiary education, 'Oftoff'.


4 Ian Lang was created Lord Lang of Monkton in 1997.

continue to require regulation", but he felt that it was dangerous to generalise about how this could be handled”.  

As some of these monopoly industries became more competitive, often as a result of the regulator encouraging new entry, economic regulation was indeed relaxed. Examples include direct dial international telephone calls and all retail price controls on both gas and electricity. Most remarkable of all, perhaps, was the case of water services, which was once judged a natural monopoly. In recent years, there has been a growing trend towards cross border competition between water utilities. Furthermore, there is an increasingly competitive market in the pre-treatment of sewage as well as site and account management.

Section Two: Regulators' roles

Regulators have found, or been given, new roles for themselves partly due to the enabling legislation passed by the Thatcher and Major governments, which gave immense statutory powers to the regulators. As we discuss later in the case of OFCOM, legislation first promoted as “light” rapidly acquires barnacles as it progresses through Parliament to the point where OFCOM claims it has been given 260 objectives or responsibilities.7 One of the Conservative government's most lucid critics, Dieter Helm8, points out that, "Contrary to the intentions to minimize regulation, the scope provided for intervention in both industries was consequentially very great - both in domain and form. Almost anything could be deemed a matter relevant to competition, and competition could conflict with all or any of the (regulator's) other duties".9

The incoming Labour government seized on regulation as a mechanism for pursuing the political goals they had set out in Opposition. The Labour manifesto stressed the view that economic regulation of privatised industries needed to be reformed. Regulation - as opposed to public ownership - provided them with a means of addressing their wider social and environmental objectives.10 One regulatory head observed about the initial period of the Labour administration: "Ministers no longer looked on the regulator's job as economic regulation, they viewed it as public policy job. It was no longer apolitical, it was part of government".11

6 Ibid.  
8 Dr Dieter Helm is a Fellow of New College, Oxford and co-founder of Oxford Economic Research Associates (OXERA).  
10 See, for example, The Department of Trade & Industry Green Paper, March 1998, A Fair Deal for Consumers: Modernizing the Framework for Utility Regulation, outlining the Government's proposals on reform.  
11 Clare Spottiswoode, discussion with Keith Boyfield, 31 March 2000.
The DTI 1998 Green Paper on regulation had 42 recommendations designed to address Labour's political mission, which focused on such issues as fuel poverty and renewable energy. It was suggested that one role of government would be to issue statutory guidance on how utilities could contribute to a range of social and environmental objectives. The Green Paper claimed that the existing regulatory regime was lacking in "openness and accountability in the process and institutions of regulation". In order to correct this flaw, it was proposed that "regulators should provide reasons for key decisions and should consult on, publish and follow a code of practice governing decision-making processes". Furthermore, it was suggested that individual regulators be replaced by boards - a view promoted by the European Policy Forum and the Hansard Society.12

In due course, the Government sought to tackle what they perceived as the weaknesses in the existing regulatory regime. In addition, regulators were given new statutory responsibilities, set out in legislation such as the Utilities Act 2001.

Cecilia Ugaz and Catherine Waddams Price draw attention to the essential conflict between competition and social policy.13 Competition will tend to lower prices for the main users, i.e. the higher income groups, and raise prices for those smaller users who are not economic for providers. Social policy, which the cynical might see as covert taxation, requires the opposite. The utility companies may welcome cross-subsidy and even regulation if it keeps potential competitors out of the market. It is hard to see how giving these conflicting roles benefits the taxpayer. Regulators should encourage competition, and thereby their own demise, while wealth redistribution should be a function of the tax system. “The social action plan final document of March 2000 makes it clear that the basic cause of fuel poverty is lack of money.”14

Ugaz and Waddams Price make an important point about the way regulators operate: “Evidence shows that UK regulators have affected prices as much through informal persuasion as by formal regulatory mechanisms. Foreign owners might be less responsive to such persuasion”15


The Utilities Bill Debacle

The Utilities Bill bundled reforms for the regulatory oversight of water, energy and telecoms as well as dealing with the role of the Competition Commission as an appeals body. Strong lobbying by some of the largest telecoms companies, including Vodafone, Cable & Wireless, Orange and NTL, convinced ministers that the Utilities Act should not apply to the telecoms sector; since this was now competitive, it required less regulation rather than more. Twenty five telecoms companies, in a joint letter to the DTI and Department of Culture, Media & Sport, emphasised the regulatory threat posed by the proposed legislation. They pulled no punches: "The Utilities Bill", the letter stated, "will create a climate of conservatism in the supply of new services rather than stimulate innovation. It will throw our industry into regulatory uncertainty with the guarantee of repeated further upheaval to come".16

It further became evident that it would not be practical to include water services within the Utilities Bill, partly due to a lack of enthusiasm at the Department of Environment, Transport & The Regions, the sponsoring ministry for the water industry. As a result, these passages in the Bill were also dropped.

The outcome of this political process was that the Utilities Act was confined to the energy sector. As a Parliamentary Bill, it suffered a succession of humiliations. While in committee stage, the Government was obliged to introduce an unprecedented 500 detailed amendments. In his history of the energy sector since 1979, Dieter Helm comments that the Utilities Act was one of the "worst examples of poor drafting in recent times".17 Dr Helm attributes this failure to insufficient resources, a lack of expertise and a woeful ignorance about how utilities operate in the real world. Unfortunately, the Utilities Act has made the regulatory regime less predictable and it is generally agreed to have led to a rise in the cost of capital - a reflection of investors' unease in the UK regulatory regime.

The Consumerist Agenda

The Thatcher and Major governments subscribed to the view that individual consumers were the best judge of their own welfare, a view rooted in the Austrian approach adopted by many of the academics associated with the privatisation and liberalisation programme of the 1980s and 1990s.18

---

18 Good examples of this group are the economists associated with the Institute of Economic Affairs, notably Michael Beesley, Stephen Littlechild, Colin Robinson and Dr Eileen Marshall.
Labour tended to adopt a more interventionist stance. The Utilities Act confirmed the Labour government's commitment to consumer councils, reflecting its distrust of market mechanisms. In thinking through its proposals for reform, Labour ministers and their advisers had been strongly influenced by consumer groups who lobbied for an explicit commitment to their own set of goals. The Utilities Act established a new consumer body, ENERGYWATCH, to replace the existing consumer organisations, which Stephen Byers, the DTI Secretary of State, dismissed as being far too weak. "Consumer bodies are so closely linked to the regulators' offices that they even have to issue their press notices on headed notepaper from the regulators themselves", Byers observed in the Second Reading debate.\(^{19}\) Byers clearly thought that these consumer bodies were too much in the regulators' pockets. But this was not a view shared by independent observers, or the regulators themselves.\(^{20}\)

The Utilities Act introduced a new primary duty on regulators to protect consumer interests, wherever appropriate through effective competition. This revision to the energy regulator's statutory duty, repeated in other legislation such as the Communications Act 2003, has gone a long way towards meeting the consumerist agenda. In terms of institutions, there are now a raft of statutory consumer bodies such as ENERGYWATCH, POSTWATCH and the new Consumer Panel advising OFCOM. However, there has been a marked lack of guidance given by ministers on such issues as how far prices to some consumers should be increased in order to address the question of fuel poverty. Similarly, very little concrete guidance has been issued on how far energy prices should climb in order to deal with the environmental problems that concern ministers.

What do Regulators do?

Websites explain the roles of regulatory agencies, e.g. OFWAT and ORF. Given their common original objective to provide a proxy for competition they have evolved in surprisingly diverse ways. Representation of the consumer has been, partially at least, devolved to other bodies.

**OFWAT**

OFWAT's statutory role is to protect the interests of water customers in England and Wales in an industry that has traditionally been perceived as a classic natural monopoly. In fulfilling its duties, laid down under the Water Industry Act 1991, OFWAT compares the activities of regulated companies to promote best practice and penalise inefficiency. Indeed, this is the principal reason why the regulator has resisted moves to consolidate the water services industry within the UK.

\(^{19}\) Hansard, 8 January 2000.

\(^{20}\) Keith Boyfield's personal discussions with former regulators.
For twelve years the regulatory regime in the water services sector has remained relatively stable. However, the new Water Act, which received Royal Assent in November 2003, has introduced some wide reaching changes.

Labour was committed to extending the scope of regulation in the water industry from the time it entered office in 1997. Originally, these changes were to be ushered in by the Utilities Bill, but, as previously discussed, this Bill was radically altered during its progress through Parliament. Consequently, it was not until 2003 that the Water Services Act was amended with the creation of a new Regulation Authority and a Consumer Council for Water, known as WATERVOICE. These new regulatory structures will not take effect until after April 2005 when OFWAT has completed its price review of the industry for the period 2005–2010.

WATERVOICE is organised around nine regional committees in England and one in Wales. The nine chairs of these committees comprise the WATERVOICE Council. The regional committees are supposed to deal with individual consumer complaints and problems. Where these problems cannot be resolved by WATERVOICE and its own staff, they are handled by OFWAT. These blurred roles sometimes trigger friction between the two bodies, and WATERVOICE is regularly critical of the regulator. Now that WATERVOICE has won new statutory powers, conflict between the regulator and the consumer body is likely to be exacerbated.

Under its original enabling Act, the water regulator has a statutory duty to encourage competition where appropriate. This objective has not been easy; the cost of transportation and legal arrangements have made competition awkward to foster. Nonetheless, the development of common carriage, more inset appointments in rival areas, and the trading of abstraction licences, have made the sector more contestable. These trends have been accelerated by the Competition Act 1998, which conferred additional powers on the regulator. While few residential customers have found it worthwhile to explore these options, larger customers have done so.

The Water Act 2003 is likely to further foster competition, particularly in those areas of the market where business customers demand large quantities of water. Henceforth, market entrants will be able to enter into common carriage or wholesale agreements with water companies to supply non-residential customers consuming more than 50 megalitres of water per year.

The Labour administration has intervened more than its predecessor, a trend highlighted by the former water regulator, Sir Ian Byatt: "Present ministers have moved into the micro-management of the water industry. If they continue in this direction they will push the regulatory regime towards ever more detailed involvement by ministers -acting through their interaction with the quality regulators and the economic regulator".  

This may not be in the best interest of water customers, Sir Ian warns, since it is they "who gain from greater efficiency resulting from incentives and from the ability of companies to retain the

---

21 Lecture given at the University of Central England, November 2000.
flexibility to search for innovative solutions. Customers would also lose if water companies increasingly see themselves as environmental contractors responding - in a profitable way - to regulatory demands rather than further developing themselves as customer service bodies”.

**ORR**

The Office of the Rail Regulator (ORR) was established under the Railways Act 1993, the legislation which provided for the privatisation of the railways. The rail industry has experienced more radical change than any other privatised industry following the election of Labour in 1997. While Labour did not seek to reverse the privatisation process as far as rail franchisees are concerned, it established a new franchising authority, the Strategic Railway Authority (SRA) and returned the track and signalling side of the industry to public ownership. Railtrack was renationalised in 2001, but only after considerable controversy and the threat of legal action by some of the largest fund managers in the City.

ORR's website explains that its principal function is to regulate the not-for-profit company established to succeed Railtrack. Thus, the Rail Regulator oversees Network Rail's stewardship of the national rail network infrastructure, which includes track, signalling, bridges, tunnels, stations and depots. Effectively, this means that the Rail Regulator issues and enforces licences and licence exemptions as they apply to the operation of railways assets. The regulator’s other duties include fixing the level and structure of charges payable by franchise operators wanting to use the rail network; the approval of access agreements and subsequent amendments – a role that covers the responsibility for ensuring the fair and efficient consumption of rail network capacity; and the concurrent power, shared with the OFT, for the enforcement of competition law as it applies to rail services under the Competition Act 1998.

The Rail Regulator must act in accordance with European law as it relates to a host of matters including competition, the provision of railway services, licensing, capacity allocation, charging and technical standards\(^\text{22}\).

Unlike most sectoral regulators, however, the Rail Regulator is no longer directly concerned with consumer protection, including fares. The ORR lost its responsibilities\(^\text{23}\) for consumer welfare when the Transport Act 2000 established the Rail Passenger Council (RPC) under the Strategic Rail Authority (SRA). The Authority's main role is to award passenger rail franchises and administer the subsidies of passenger and rail freight services. But the SRA also exercises certain regulatory functions, focusing mainly on consumer matters. This has led to considerable confusion.

\(^{22}\) This presumably applies, pari passu, to the other regulators.

\(^{23}\) The RPC's predecessor, the Central Rail Users' Consultative Committee, reported to the ORR.
Few people fully understand the distinctions in the responsibilities of ORR and of the SRA. It appears that the Secretary of State for Transport, Alistair Darling, is one of the many people who are perplexed about their respective roles. He felt sufficiently dissatisfied with the current structural make-up of the UK railway system that on 19th January 2004 he announced a wide-ranging review of the future structure of the rail industry.

In announcing this review the Secretary of State touched on a crucial point of controversy, namely who is responsible for approving investment in Network Rail? In contrast to the SRA, the Rail Regulator currently enjoys a significant degree of independence. This is reflected in the fact that the Treasury could not overrule the Rail Regulator’s decision\textsuperscript{24} to increase investment in the rail network. The sums involved are considerable – Tom Winsor, the Rail Regulator, has concluded that £22.7bn is required in capital investment over the five year period 2004 - 2009.

Yet in his statement to the House of Commons on 19\textsuperscript{th} January 2004, Mr Darling said: ”It must be for government to decide how much public money is spent on the railway and determine policies”.\textsuperscript{25} This claim runs counter to the view expressed by Tom Winsor, who insists that the Office of the Rail Regulator cannot be dictated to by government with regard to Network Rail's allowable expenditure.

The present confusion over roles and responsibilities may be clarified by the government rail review. However, even ministers appear to contradict one another on the review's terms of reference. While the Secretary of State is adamant that vertical integration of the industry is not on the review agenda, a junior minister, Kim Howells, has indicated that the review may indeed cover a much wider range of issues, including the possible reintegration of the rail system\textsuperscript{26}.

The rail review, due to report by July 2004, will examine the future of the Strategic Rail Authority and identify what, if any, of its functions should continue. Informed opinion suggests that the SRA's strategic role may be moved back to the Department for Transport, leaving the SRA to concentrate on its franchising duties and ensuring passenger train services deliver on their franchise obligations. As it is, under current legislation, ministers have the legal power to give the SRA directions and guidance – an interventionist role that ministers have not been reluctant to use given the substantial sums of money involved in subsidising the rail network.

The next section shows how the increasing demands for control over regulators and wider ill-defined roles have brought confusion.

\textsuperscript{24} Announced in October 2003.


\textsuperscript{26} Ibid.
Section Three: The control and accountability of regulators

The economic regulators established by successive Conservative governments from 1984 onwards were deliberately designed to be largely independent of ministers. The aim was to free privatised industries from the incessant political interference that had dogged their development since they were nationalised following World War II. Thus, while ministers could offer guidance, regulators were not supposed to be subject to ministerial direction.

Tom Winsor, the Rail Regulator, emphasised this point in 2003 when he submitted evidence to the House of Lords' Select Committee inquiry into the accountability of regulators. Winsor pointed out that, "Under section 4 (5) (a) of the Railways Act 1993, the Rail Regulator is required to have regard to any general guidance issued to him by the Secretary of State about railway services or other matters relating to railways". However, Winsor observed that, "The obligation to have regard to general guidance is not inconsistent with the Rail Regulator's independence because the Rail Regulator may conclude, in the light of his other statutory duties, that a different course or action is warranted. 'Have regard' is not the same as 'do as you are told'.

Labour's concern with regulators

Regulators' independence provoked concern among Labour politicians, who for ideological reasons favoured greater intervention within what they judged to be vital sectors of the economy. Some, such as Margaret Beckett, then Shadow spokesperson on Trade & Industry, were concerned about the power of individual regulators, who had no board to answer to, and whose philosophical approach to regulation was diametrically different to the stance adopted by Labour. Perhaps the best embodiment of a hands-off regulator was Professor Stephen Littlechild, the Director General of Electricity Supply. Here was an academic who identified himself with the Austrian School of free market economics, so mistrusted by Labour.

Labour government legislation has similarities in the treatment of the various regulators. Authority is now invested in boards, not individual regulators who are now required to give reasons for key decisions. Moreover, they are obliged to consult on their forward work programmes and give consideration - as a group - to matters of common interest. Furthermore, regulated companies have been given the opportunity to appeal to the Competition Commission where they disagree with regulatory decisions. They may also elect to initiate judicial review of a decision, if they feel they have reasonable grounds.

Some of these changes recognised existing developments within regulatory practice. The energy regulator, Callum McCarthy, had already established an advisory board prior to the Utilities Bill receiving Royal Assent. Similarly, the water regulator, Philip Fletcher, had established an advisory board to assist him in reaching decisions prior to the passing of the 2003 Water Act, which established the Water Services Authority.
Shortly after it entered office, the Labour government introduced the most far-reaching transformation in the regulation of financial services seen in quarter of a century. The Financial Services Authority (FSA) was announced by Gordon Brown, the Chancellor of the Exchequer, in May 1997. There had been no prior consultative process or public debate.

Partly as a result of its complexity and lack of consultation, the enabling legislation took several years to win Parliamentary approval. The FSA was first established in shadow form in 2000, but it did not assume its full powers under the Financial Services and Markets Act 2000 until 1 December 2001. This legislation replaced a regime primarily based on self-regulation.

### Regulatory Confusion

The confusion surrounding the responsibilities and accountability of regulators prompted the House of Lords’ Constitution Committee to hold an inquiry into the "accountability of regulators to citizens and parliament". This select committee, chaired by Lord Norton,\(^ {27} \) began its inquiry in February 2003 and has since interviewed a wide number of witnesses, including current as well as former regulators, who may be freer to speak their own minds. Their evidence has been illuminating.

Sir Christopher Foster, who has advised ministers on the creation of regulatory authorities, testified that he believed "the legal basis for utility regulation has not proved adequate. From one standpoint regulators' obligation to secure quasi-market conditions in their industry needs strengthening and their independence safeguarding. But the relation between their economic and social duties needs clarifying".

The confusion over regulators' new non-economic or social and environmental responsibilities is a recurring theme in the discussion of the UK regulatory regime. If one takes the example of the Utilities Act, this piece of legislation imposed a duty on the regulator - OFGEM - to have regard to ministerial guidance on social and environmental objectives relevant to their sector. While this was not a duty sought by the regulator, the Department of Trade & Industry took a long time to issue the promised ministerial guidance. Statutory guidance was finally issued in July 2002, well over two years after the initial draft was issued in February 2000. Even so, the issue of specifying the cost trade-offs involved in pursuing these objectives was avoided.

This reluctance to define and prioritise trade-offs with regard to non-economic objectives, such as social or environmental goals, remains one of the key flaws in the UK regulatory regime. This point has not escaped the Better Regulation Task Force. In its report on *Economic Regulators*, published in July 2001, the Task Force stressed the need to maintain clear accountability for the delivery of non-economic objectives. This concern grew out of the criticism levelled by a wide range of stakeholders who felt that "the distinct responsibilities of government and regulators had

\(^ {27} \) An academic political scientist sitting on the Conservative benches.
been blurred by the addition of these new social and environmental duties”. The Task Force observed that "whereas the costs of the social and environmental objectives would anyway have to be incorporated into price caps, the wider remit complicates the job of the regulators and increases bureaucracy in departments and companies as they try to meet their obligations”.

Thus the non-economic objectives introduced by the Labour administration have confused the accountability of regulators. In the pursuit of a variety of social, environmental and consumerist goals, they have been not specified how such objectives might be financed. As Dieter Helm argues, the Utilities Act "created even greater (regulatory) discretion through the vague overarching consumer protection duty”.

The next section highlights the considerable growth in regulatory budgets and manpower over the years 1997 to 2003 and how they are likely to develop.

**Section Four: Regulatory budgets and headcount 1997 - 2003**

How have the wider objectives impacted the budgets and staffing of the regulatory agencies? This section examines the regulatory offices, their budgets and payroll numbers over the period 1997 - 2003 and discusses projected budgets and headcount figures, where these can be identified. Table 1 gives details on the annual budgets of 12 regulators for the year 1996/7 and the three years 2000/1, 2001/2, 2002/3. The year 1996/7 has been chosen to illustrate the size and activities of regulators in the last year of the Conservative administration. Note that the FSA, POSTCOMM and OFCOM had not yet been established. At this time there were also two energy regulators, OFFER and OFGAS, which were subsequently merged to form OFGEM. The data for the three years 2000/1 to 2002/3 allows one to form a picture of the recent trend in the growth of regulators.

In terms of aggregate numbers, the ten regulators analysed in 1996/7 spent a total of £141m, excluding self-regulatory City bodies such as the Securities & Investment Board (SIB), and employed 2,061 people. Six years later, the 12 regulatory bodies reviewed in Table 1 spent £481m and employed 4,879, excluding consultants.

---


29 ibid.

30 Op cit, page 293
Table 1: Regulatory budgets and headcount 1997 – 2003

<table>
<thead>
<tr>
<th>Regulatory Agency</th>
<th>Expenditure Budget £M</th>
<th>Change in budget 1996/7 – 2002/3</th>
<th>Payroll numbers</th>
<th>Change in payroll 1996/7 – 2002/3</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>1996/7</td>
<td>2002/3</td>
<td>%</td>
<td>1996/7</td>
</tr>
<tr>
<td>Competition Commission</td>
<td>7.9</td>
<td>16.3</td>
<td>106</td>
<td>97</td>
</tr>
<tr>
<td>OFT</td>
<td>19.5</td>
<td>54.2</td>
<td>178</td>
<td>402</td>
</tr>
<tr>
<td>FSA</td>
<td>n.a.</td>
<td>221</td>
<td>21% over 3yrs</td>
<td>n.a.</td>
</tr>
<tr>
<td>OFTEL</td>
<td>9.5</td>
<td>19.5</td>
<td>105</td>
<td>172</td>
</tr>
<tr>
<td>Radiocommunications Agency</td>
<td>42.3</td>
<td>71.5</td>
<td>69</td>
<td>514</td>
</tr>
<tr>
<td>Radio Authority</td>
<td>3.4</td>
<td>4.8</td>
<td>41</td>
<td>33</td>
</tr>
<tr>
<td>ITC</td>
<td>16.9</td>
<td>20.1</td>
<td>19</td>
<td>186</td>
</tr>
<tr>
<td>BSC</td>
<td>1.3</td>
<td>3.9</td>
<td>200</td>
<td>24</td>
</tr>
<tr>
<td>OFGEM</td>
<td>23.1</td>
<td>38.5</td>
<td>67</td>
<td>357</td>
</tr>
<tr>
<td>OFWAT</td>
<td>9.6</td>
<td>11.5</td>
<td>20</td>
<td>190</td>
</tr>
<tr>
<td>POSTCOMM</td>
<td>n.a.</td>
<td>6.5</td>
<td>67% over 3yrs</td>
<td>n.a.</td>
</tr>
<tr>
<td>OFRAIL</td>
<td>8</td>
<td>13.3</td>
<td>66</td>
<td>86</td>
</tr>
<tr>
<td><strong>TOTAL</strong></td>
<td><strong>141.5</strong></td>
<td><strong>481.1</strong></td>
<td><strong>2061</strong></td>
<td><strong>4,879</strong></td>
</tr>
</tbody>
</table>

* The Radio Authority presents its annual figures on a calendar year end basis.
+ OFGEM's budget figures are operating expenditure figures.

The largest regulatory office is the FSA, established in 2000. Leaving aside the Broadcasting Standards Commission, the OFT has shown the fastest budgetary growth, almost trebling the
scale of its annual expenditure. In comparison, the Competition Commission has seen its budget more than double. Among the sector economic regulators, OFTEL has recorded the highest rate of growth with a budget increase of 105 percent. OFGEM and ORR have seen their budgets climb by approximately two-thirds whereas OFWAT has only recorded a 20 percent increase in annual expenditure. In the broadcasting and communications sector, the Radiocommunications Agency, formerly part of the DTI, has substantially increased its annual level of spending, equivalent to nearly 70 percent over the period. The Radio Authority's budget has grown by 40 percent over the six year period, but the ITC has stemmed its annual spending, so that overall, its budgetary growth only reaches 20 percent. The Broadcasting Standards Commission increased its annual expenditure in 2002/3, mainly as a result of its entry into the Civil Service Pension Scheme.

A management consultants report\textsuperscript{31} into the efficiency of four utility regulators, commissioned by H M Treasury in Autumn 2000, revealed that around the half the regulators' total costs related to payroll. "Increases in payroll are strongly linked to the increase in operating costs at all the regulators".\textsuperscript{32} This Treasury review also highlighted: "another key cost component is consultancy". The Atkins study added that, "These costs are relatively modest in comparison to total costs at OFWAT and OFTEL, but very significant at OFGEM and ORR".

The strongest headcount growth was recorded by the two anti-trust regulators, the Competition Commission and the OFT, which grew by 60 percent and 57 percent respectively. Three sectoral economic regulators also chalked up significant gains: OFTEL, which employed 37 percent more staff in 2002/3 compared with 1996/7; the ORR, which employed 44 percent more staff over the corresponding time period; and POSTCOMM, whose headcount climbed by 38 percent over the three year period 2000/1 - 2002/3. Some of the other regulators displayed slower rates of growth; OFWAT grew by 23 percent and the ITC grew by only 3 percent. Two regulators reduced their overall staff numbers, notably OFGEM by ten percent.

\textit{Competition Commission}

Table 1 shows that the Competition Commission's budget increased by 106 percent between 1996/7 and 2002/3. In 1996/7, the former Monopoly & Mergers Commission operated on an annual budget of £7.9m, whereas by 2002/3 its successor body, the Competition Commission had a budget of £16.3m. Payroll numbers had risen from 97 to 155 excluding Members of the Commission - an increase of 60 percent. This growth is attributable to the wider role that the Competition Commission is expected to play following two important pieces of legislation - the 1998 Competition Act and the Enterprise Act 2002. These statutes marked the biggest overhaul

\footnotesize{\textsuperscript{31} External Efficiency Review of the Utility Regulators, Final Report, W S Atkins in association with OXERA, February 2001.}

\footnotesize{\textsuperscript{32} Ibid, p.vii.}
of competition law in 25 years. The former statute reflects the importance the Chancellor of the Exchequer, Gordon Brown, places on improving competitiveness within the UK economy. The Competition Commission is seen as a key driver for enhancing competition. The latter statute marks a transfer of responsibility for merger cases to the Commission. This is seen as a trend towards trying to depoliticise merger cases, since ministers will only be able to intervene in exceptional circumstances. However, the term 'exceptional' has yet to be defined in practice.

The Competition Commission succeeded the Monopolies & Mergers Commission on 1 April 1999. It performs three main roles: (1) inquiries into proposed and completed mergers; (2) inquiries into particular markets where competition is thought to be lacking; and (3) reviews of the economic regulation, particularly price regulation, of regulated industries. The Competition Commission has no legal power to conduct inquiries on its own initiative, consequently every inquiry it conducts is in response to a reference made by another authority, usually by the OFT or a minister, and sometimes by a sector regulator, such as OFGEM.

Under the Enterprise Act 2002, the Competition Commission may also receive market references from the OFT or sector regulators, such as OFGEM, if they have reasonable grounds for suspecting that any feature, or combination of features, of a UK market restricts or distorts competition with regard to the supply or acquisition of a good or service. These powers are held concurrently by the Commission along with the OFT and sectoral regulators.

Office of Fair Trading

The Office of Fair Trading (OFT) annual budget has risen from £19.5m in 1996/7 to £54.2m in 2002/3, an increase of 178 percent. Staff numbers have climbed from 402 in 1996/7 to 631 in the year 2002/3, a rise of 57 percent. However, most of this gain took place after 2000/1, as the OFT recruited staff to implement the regulator's new responsibilities under the 1998 Competition Act. The OFT also hired staff to handle the duties it would assume under the Enterprise Act 2002. The OFT now has a responsibility to investigate suspected cartels; it also has a duty to undertake the initial investigate research on mergers where there is a problem regarding the substantial lessening of competition test introduced by the Enterprise Act 2002. Observe that payroll numbers have soared over the last two years from 443 in 2000/1 to 631 in 2002/3. One of the worrying trends apparent in recent years has been the very high staff turnover rate at the OFT. As a result, the competence and experience of staff have been criticised.

33 The Competition Commission is asked to investigate six types of reference with regard to regulated industries. These are licence modification references and references concerning non-licence activities in the gas and electricity sectors; price determination references; references under the Financial Services & Markets Act 2000; references under the Broadcasting Act 1990; airport references and water merger references. Since 1985, the MMC and subsequently the Competition Commission have reported on 43 references involving regulated industries.
The OFT claims that its fundamental role is to 'make markets work well for consumers'. In seeking to achieve this goal the competition watchdog states that it undertakes three related roles: (1) it studies markets proactively to establish whether they are functioning in the interests of consumers; (2) it claims to uproot and deter all forms of anti-competitive behaviour, including the cartels and the abuse of market power; and (3) it aims to communicate its role and decisions, including enforcement actions, to relevant stakeholders and the general public.

The Treasury has set a service delivery agreement (SDA) for the OFT whereby it must pursue ten principal objectives. Several targets are linked to each of these objectives and the OFT's performance will be measured by its record in meeting these targets. While it appears to have performed reasonably well in the year 2002/3, media reports later in 2003 suggest that both the Treasury and the Competition Commission are becoming increasingly frustrated with the OFT's inability to achieve its set objectives. \(^{34}\) Andrew Cave claims: "The problem with the OFT is that in recent years it has tended to produce more confusion than solution. Inquiries that begin with a burst of macho strength seem to get bogged down in bureaucracy". \(^{35}\) Some of the OFT's investigations have been substantially delayed. For example, an investigation into the interchange fees charged by banks on credit cards took three and a half years to reach a conclusion. The OFT has also spent what some would see as protracted period of time reviewing the various bids for the Safeway supermarket chain.

The Enterprise Act not only bestows major new powers to the OFT, it also requires it to pursue a huge agenda. For example, the Act requires the OFT to review so called super complaints made by a range of designated consumer bodies and to announce within 90 days if they will be taken forward. Unless fairly tight criteria are adopted as to what anti-competitive practices constitute, this could lead to a soaring workload for the OFT.

Already, the new legislative powers awarded to the OFT appear to have encouraged the competition watchdog to over-extend itself. Since the Act came into force, the OFT has received 4,753 complaints about alleged uncompetitive practices, including no less than 223 allegations of cartels, notably the alleged fee fixing between independent schools. The OFT is overloaded with work and appears to be struggling to address its wide-ranging legislative responsibilities.

Financial Services Authority

The establishment of the Financial Services Authority (FSA) heralded a step change in the size and scope of regulation as it affects the financial services sector. As a one-stop shop for the regulation of financial services, it acquired about a thousand staff who had previously worked for

\(^{34}\) For example, “Government says expanded OFT isn't pulling its weight,” by David Smith, Economics Editor, Sunday Times, 14 December 2003.

\(^{35}\) ‘The long arm of the OFT is a law unto itself’, Andrew Cave, Daily Telegraph, 22 November 2003.
the Supervision and Surveillance Division of the Bank of England. Officials at the DTI's Insurance Directorate were also transferred to the new watchdog. In all, the regulatory and registration functions of nine bodies were combined within this new super-regulator. Nevertheless, the FSA almost immediately began to attract critical media comment because market participants felt that its staff lacked experience of the sector. Sir Howard Davies, the FSA's first chairman, was obliged to concede, in the Authority's first annual report: "Although we are almost fully staffed, experience levels in front line areas remain too low. An intensive programme of training and development will be necessary to correct that deficiency."

The FSA is currently responsible for overseeing at least 10,000 companies in the banking, building societies, insurance, fund management, personal investment and securities sectors. The FSA has also recently assumed responsibility for regulating around 25,000 firms involved in mortgage and insurance broking. This statutory role is claimed to stem from an EU directive on insurance mediation. In fact, and perhaps not unusually, the directive gives considerable flexibility for member states to determine the appropriate “competent authorities” who should supervise the sector.36 Previously, The General Insurance Standards Council, only created in 1999, was the competent authority on a self-regulatory basis.

In 1996/7, the Personal Investment Authority (PIA) employed 400 people, at a cost of £14.7m, a headcount that had almost doubled from the 233 staff employed in 1995/6. The Securities & Investment Board, also consolidated into the FSA, employed 195 people in 1996/7 and its total budget was £21.9m.

In contrast, as Table 1 reveals, the FSA's budget and staffing levels were in an entirely different league. In 2000/1, the FSA's annual budget amounted to £182m and the number of permanent staff totalled 2,039. Even so, the super-regulator was officially under-strength, since its targeted headcount was 2,250. There appear to have been considerable difficulties in recruiting and retaining staff at the FSA. In 1999/2000, staff turnover was 20 percent although this rate slowed to seven percent by 2001/2.

In the year 2002/3, as Table 1 shows, the FSA annual budget totalled £221m compared with £182m in 2000/1. The number of staff employed rose from 2,039 in 2001/2,313 over the corresponding period. In the year 2003/4, the FSA originally expected to spend £215.4m, slightly down on the previous year, and staff numbers - despite a larger statutory workload – were forecast to be 2,200. However, when the FSA announced its future business plan in January 2004, the total budget was revised upwards by 13 percent to £240 m, partly on account of its additional responsibilities relating to insurance and mortgage brokers37, and partly as a result of the increasing need to take enforcement action. Indeed, expenditure on enforcement action,

37 Their inclusion is estimated to lead to additional costs amounting to £29.7m.
largely driven by investigations into the alleged mis-selling of split caps, is planned to rise by 17 percent in the year 2004/5.

It may be argued that it is unfair to exclude the FSA’s predecessor supervisors from the growth calculation but they were voluntary, apart from the Securities & Investment Board. This paper reports [the increase in] statutory regulatory offices.

Prior to the establishment of the FSA, the onus of regulation as it related to financial services was on self-regulation. As John Kay observes, “Self-regulation has one advantage over statutory regulation. Self-regulation entities – companies, groups of professions – have the information to do it, and a government agency does not”. 38

The previous system worked up to a point, but criticism was levelled at the amount of duplication and confusion associated with nine different self-regulatory bodies. The 1986 Financial Services Act created the Securities & Investment Board (SIB), a statutory regulator, which in turn supervised a clutch of self-regulatory organisations (SROs), such as the Life Assurance and Unit Trusts Regulatory Association (LAUTRO), and Recognised Professional Bodies (RPBs), such as the Institute of Chartered Accountants. These bodies undertook the day-to-day regulation of their sectors.

Sir Adam Ridley, a director of Hambros Bank, commented, “The regulations are so complicated that the whole thing threatens to be a bit of a shambles. It is as if the Highway Code, instead of stating general principles, said what has to be done at every junction and intersection in the country for each of seven classes of vehicle”. 39

John Nott, a former Trade Secretary and a past Chairman of Lazards Bank summed up the conflict between Westminster and the City: “In spite of Westminster’s envy of the City, it was the only truly dynamic part of the economy. And the City establishment, which was changing into a meritocracy, had contempt for the politicians, while they in turn regarded the City as an unregulated jungle unanswerable to them and independent of them. This led to the Financial Services Act, a damaging and ill-thought out measure to protect investors, strangling every firm with needless bureaucracy when the same objective could have been achieved by a compulsory insurance levy”. 40

Over time the misconceived regulatory network of SROs merged into three bodies. This move was triggered by an effort to simplify regulation and improve the manner in which customer

40 Here Today, Gone Tomorrow by John Nott, Politico’s, 2002, p.332. Nott adds: “It would never have got through me at Trade”.

22
complaints were handled. Nonetheless, criticism of the regulatory regime began to grow\(^{41}\) and there was a widespread view that the system was unnecessarily confusing.

There was also a growing belief\(^{42}\) that following the Big Bang of the mid 1980s, the old City network, where participants had often known one another well since schooldays, was beginning to break down. The old self-regulatory regime built on personal reputation and ‘my word is my bond’ was disappearing. Such concerns were reinforced by the collapse of Barings Bank in the early 1990s, and the Maxwell scandal that involved some of the City’s main players, such as Goldman Sachs.

While identifying the advantages associated with self-regulation John Kay also points out a potential disadvantage, namely that, “Self-regulating entities do not have much incentive to take regulation seriously, and government does”.\(^{43}\) Politicians, responding to complaints from their constituents, take this view seriously. One such politician was John Nott, who observed at the time of the 1986 Financial Services Act that: “In my view the City was unwise to promote the concept of self-regulation. The Bank of England was even more unwise to promote it. When the next bear market comes there are going to be firms going bust. Politically, no one is going to distinguish between bankruptcy and fraud. The blame is going to descend upon the City self-regulators and certainly upon the Bank for failing to police the system… In the end we will have the legal authority which will be acting in the capacity of a court”.\(^{44}\)

Nott’s prediction proved correct. But has the new statutory regime, established under the FSA, proved an improvement on the old self-regulatory model, albeit imperfectly implemented? According to detailed market research\(^{45}\), undertaken by BRMB Social Research for the Financial Services Practitioner Panel, more than three out of four respondents judged that the current system placed too great a burden on the industry. More than half of those asked felt that the present regulatory system gave too much weight to consumer interests as against those of practitioners. A significant proportion of practitioners involved in the retail side of financial services felt that consumer protection had gone too far. People should be required to take more responsibility for their own decisions and actions.

---

\(^{41}\) See, for example, *The Regulation of Financial Services in the UK*, Treasury & Civil Service Select Committee, 1995 and also *The Changing Direction of UK Regulation*, Clifford Chance, 1997.

\(^{42}\) See, for example, chapter five in *The Death of Gentlemanly Capitalism*, by Philip Augar, Penguin Books, 2000.


\(^{44}\) ‘City Revolution’, *Financial Times*, 27 October 1986.

\(^{45}\) *2002 Survey of the FSA’s regulatory performance*, prepared by BRMB Social Research for the Financial Services Practitioner Panel, November 2002. The survey was based on an unusually large group of respondents. 3,890 senior executives in regulated financial services firms completed the postal questionnaire.
In the FSA’s Business Plan 2004/5, the Chairman’s Foreword begins: “The FSA’s legitimacy rests on two pillars: the first, the statute which establishes our duties and powers; the second, the effectiveness with which we discharge those responsibilities.” What follows is interesting, professional and well produced, with a large number of good intentions bordering on motherhood. For example, the first “outcome” that the FSA aims to achieve for consumers is that they themselves, firms and the FSA understand consumer needs. The second is that we consumers become financially aware and can take responsibility for our financial affairs. It seems that for hundreds of years we consumers have been unable to take responsibility for our financial affairs. The interventions of the FSA may, in fact, have made it less easy to understand our financial affairs but whether these FSA outcomes are sensible or ludicrous is beside the point. The FSA Business Plan lists a number of projects but not all its responsibilities under statute, still less how its effectiveness can be judged. Appendix Three shows some rather mysterious milestone dates, but the Plan is remarkably short of quantitative goals or dates by which they will be achieved. In other words, the FSA Business Plan does not say what it is supposed to achieve nor how we will know if it has. Is that not what plans are for?

The most damaging criticism of the FSA regime centres around compliance costs - two thirds of small firms and half the rest think the cost of compliance is excessive. BRMB found that 35 percent of small firms and 15 percent of larger firms judge compliance is in excess of ten percent of total cost. According to BRMB’s extensive research, many in the City feel that the FSA should look at the behaviour of companies as a whole in terms of whether they are complying with the underlying principles of regulation, rather than simply box ticking and focusing on relatively minor details.

In summing up respondents’ overall view of the FSA’s performance as a regulator, the survey noted that the regulator is “given credit for being as open and responsive as possible in the way it is operating. It is also seen as a strong regulator”. Yet, in comparison with an earlier survey undertaken by BRNB in 1999: “Wider gaps are also opening up between what practitioners identify as important, and how they perceive the FSA’s performance, in particular on providing reliable guidance when needed, having efficient administrative procedures, and interpreting rules in a flexible common-sense way – all areas in which hopes of the FSA were high in 1999. The FSA’s application of the rules is seen as being rigid rather than flexible.”

One leading financial services figure was quoted in the FT as saying, "What the City wanted from a single regulator was coherence and simplicity. What they have got and what they wanted are quite a long way apart."

---

48 Ibid.
Despite erecting an unprecedented superstructure of regulation, employing thousands of highly paid staff, financial scandals continue. It is startling to note that much of the criticism relating to the FSA focuses on an inability to crack down on market abuse. Most recently, these complaints have referred to the mis-selling of precipice bonds and the solvency problems at Equitable Life.
OFTEL

Table 1 also presents the growth in the budgets of the five regulatory bodies that have been merged into the new communications and broadcasting watchdog, OFCOM.

OFTEL doubled its annual expenditure over the six year period 1996/6 - 2002/3, although telecommunications has become a far more competitive sector in the seven years since 1997. In 1996/7, OFTEL's total expenditure amounted to £9.5m, funded mostly from regulated companies. Staff numbers increased from 172 in 1996/7 to 236 in 2002/3, a gain of 37 percent.

Radiocommunications Agency

The Radiocommunications Agency was the largest of the five regulatory offices to be merged into OFCOM. Formerly a division of the DTI, the Radiocommunications Agency was established as a separate executive agency in 1990, when it employed around 450 staff. Since then it has grown substantially. By 1996/7 the Radiocommunications Agency was spending £42.3m and employed 514 people. By 2002/3, the annual budget had reached £66.9m and the agency employed 580 staff. This represents an increase of 69 percent in the Agency's annual expenditure over the six year period 1996/7 to 2002/3, and a more modest rise of 13 percent in the number of staff employed. It is worth stressing that more than 200 people are employed as investigative field officers, scouring the country in specially equipped vans in a bid to deter improper use of the radio spectrum (notably by pirate radio stations).

The Radio Authority

The Radio Authority was a relatively small regulatory body. Nonetheless, the annual budget has increased from £3.4m to £4.8m over the period 1997 to 2002 - a rise of 41per cent. For the year to 31 December 2003, total expenditure was expected to amount to £5.2m. The number of full-time staff at the Radio Authority increased from 33 in 1997 to 47 in 2002 - a gain of 42 percent.

ITC

By regulatory agency standards, the Independent Television Commission (ITC) has been one of the most generous payers, perhaps because it operates in the glamorous world of television. This may explain why the Commission appears to have had no problems recruiting staff. In 2002/3, Dame Patricia Hodgson, the ITC chief executive, received an annual salary of around £300,000 plus a variety of perks including private health care, free tv and satellite services, and a chauffeur-driven limousine. In contrast, Rolande Anderson, the chief executive of the Radiocommunications Agency, received a total of less than £90,000 a year in the financial year to March 2003. Apart from a Civil Service Pension, she received no additional emoluments.
Dame Patricia Hodgson sought to shave staff numbers and keep a tight rein on the budget. Her view was to recruit the best, but keep numbers to the minimum. ITC's annual expenditure grew from £16.9m in 1996/7 to £20.1m in 2002/3, an increase of 19 percent. Staff numbers remained stable between 1996/7 and 2000/1. However, staff numbers had crept back to 180 by 2002/3. This translates into a three percent increase over the period 1996/7 to 2002/3.

_BSC_

The Broadcasting Standards Commission (BSC) was the smallest of the regulatory bodies to be merged into OFCOM. None of its roles were economic; its function was to maintain broadcasting standards. The BSC's budget in 1996/7 was £1.3m, increased to £2m by 2000/1. Payroll numbers fell from 24 in 1996/7 to 21 in the year 2001/2. In 2002/3 the published accounts reveal that the BSC's annual budget almost doubled to £3.9m. Most of this increase was claimed to be attributable to the BSC's entry into the Civil Service Pension Scheme.

_OFGEM_

OFGEM, the energy regulator, was formed from two previously separate regulatory agencies, OFFER and OFGAS. In 1996/7 their combined budget totalled £23.1m and these two agencies employed a total of 357 staff. OFGEM's budget climbed to £36.4m in 2000/1 and it employed a total of 434 full-time staff. These figures exclude the extraordinary costs associated with developing the new national electricity trading arrangements (NETA). Including the costs associated with NETA, OFGEM's budget in the year 2000/1 reached £64.5m of which £21.4m was spent on consultants.

OFGEM's annual expenditure is projected to reduce. The budget in 2002/3 was £38.5m but in 2003/4 it is expected to fall to £36m and £34m by 2004/5. Full time permanent staff numbers are expected to decline from 320 in 2002/3 to 300 in 2003/4 and 295 by 2004/5.

OFGEM has found it difficult to recruit and retain staff of the right calibre. When OFFER's office was moved from Birmingham to London (a move perhaps connected with Stephen Littlechild, a resident of the Midlands, stepping down as electricity regulator), OFGEM noted that it had needed to recruit extensively in order to save money on relatively expensive consultancy time.\(^{50}\)

---

\(^{50}\) See _The Politics of Regulation_ by Keith Boyfield, The European Policy Forum, September 2000, pp. 56 - 57.
In February 2004 the new Chief Executive, Alistair Buchanan,\textsuperscript{51} announced a radical overhaul of OFGEM's structure and activities. As part of this reorganisation, OFGEM stated that, "We will be undertaking a major audit of our costs with a view to living under an RPI-X price control regime for five years from April 2005. This is the same discipline that we impose on monopoly pipes and wires companies. It will serve to focus our attention on improving constantly the way we work, and maintaining year on year downward pressure on costs\textsuperscript{52}.

\textit{OFWAT}

OFWAT, based in Birmingham, has managed to maintain a fairly tight rein on expenditure, although both budgets and payroll numbers have increased following the retirement of Sir Ian Byatt. Over the period 1996/7 to 2002/3, annual expenditure rose from £9.6m to £11.5m - an increase of 20 percent. Payroll numbers meanwhile have increased from 190 to 233 over the same period. The agency's staff numbers will increase to a projected 246 by 2004/5.

\textit{POSTCOMM}

The Postal Services Commission (POSTCOMM) was established by the Postal Services Act 2000 with a board of seven commissioners. The current chairman is Graham Corbett, previously Deputy Chairman of the Competition Commission. The appointment of his successor, Nigel Stapleton, a businessman whose earlier career had been in advertising and with Unilever, was announced in November 2003.

The Act laid down four main statutory duties for the postal regulator. POSTCOMM’s principal statutory duty is to ensure the continuation of a universal postal service – the arrangement whereby letters are delivered anywhere in the UK at a uniform and ‘affordable’ price. In this context, the regulator sets the Royal Mail’s tariffs\textsuperscript{53}.

The regulator also has a duty to further the interests of users and disadvantaged customers, ‘wherever appropriate by promoting competition between postal operators’. Thirdly, POSTCOMM is meant to promote the efficiency and economy of postal operators – essentially a role relating to the dominant monopolist, the Royal Mail. Finally, POSTCOMM is obliged to

\begin{footnotesize}
\begin{itemize}
\item \textsuperscript{51} A former analyst with ABN-Amro, who joined OFGEM as Chief Executive in October 2003.
\item \textsuperscript{52} ‘OFGEM practices what it preaches', OFGEM press release, 5 February 2004
\item \textsuperscript{53} POSTCOMM has set price caps for the Royal Mail’s tariffs. From April 2001, POSTCOMM imposed a price freeze on most Royal Mail products for two years. For the period April 2003 to April 2006 the Royal Mail has been permitted to raise prices, but POSTCOMM point out that by 2006, prices in real terms will be 5 per cent lower than in 2001.
\end{itemize}
\end{footnotesize}
have regard to the need to ensure that licensed suppliers of mail services are able to finance their business.

In reality, POSTCOMM was set up to open up the postal market to competition and improve the poor service provided by the Royal Mail. As Graham Corbett, POSTCOMM’s chairman observed to the Lords Constitution Committee in June 2003: “One of the reasons for wanting to set us up in the first place was that the government simply had no appetite for having to take the rather disagreeable decisions that were necessary to move the Royal Mail forward to where it had been moved to now, in so far as we can do things which government was not readily able to do”. 54

POSTCOMM claims that it is working towards a vision of a "range of reliable, innovative and efficient postal services, including a universal postal service, valued by customers and delivered through a competitive postal market". POSTCOMM has introduced competition into the marketplace and licensed a number of rivals to compete with the Royal Mail.

Interestingly, in 2001, POSTCOMM chose to commission the management consultants, W S Atkins, to assess its comparative efficiency as a regulator. Atkins was selected because it had undertaken a similar efficiency audit on four utility regulators for HM Treasury (see above). The management consultants reported in their report summary that, "POSTCOMM is one of the few regulators we know which has committed itself to an efficiency plan. The UK utility regulators, for example, have been criticised for ever-expanding budgets ('putting down roots') as well as the widening and deepening of their regulatory activities ('regulatory creep'). POSTCOMM is aiming to avoid these problems, and its approach is commendable"55.

The Atkins report added: "We are particularly impressed by POSTCOMM's three policy/regulatory teams, most of whom have been recruited on secondment from other parts of government. They appear to be very capable and committed to their tasks, yet by the standards of other regulators they are relatively inexpensive. Moreover, there is an excellent team atmosphere in the office".

"Also on the positive side, POSTCOMM is keeping its overheads relatively low. Additionally, it has a good system for quality-checking deliverables. Overall, we think that POSTCOMM is running a pretty tight ship and it should improve further as new systems bed down56".

Despite these words of praise, the postal regulator exceeded its annual budget in 2001/2, as approved by Parliament. POSTCOMM's annual report & accounts attribute this failure to the fact that "we did not bid for sufficient cash and resources to meet our expenditure". The postal


55 Quoted in POSTCOMM annual report and accounts 2002, p.23.

56 Ibid.
regulator spent £6.4m, whereas its approved budget was £6m for the year. Over the three year period 2000/1 - 2002/3 POSTCOMM has increased its budget by two thirds and recruited 38 percent more staff. While many of these staff are seconded from Whitehall departments, the latest report & accounts notes that the forecast headcount for 2003/4 will be higher as the regulator has made provision for 'double banking' of staff who are due to complete their loan period and return to their parent (Whitehall) departments”.

Table 2 below sets out the outturn record in terms of costs and the forecast for 2003/4. Note that estimated expenditure in 2003/4 is £7.5m, compared with £3.9m in 2001/1 - an increase of 92 percent over four years.

Table 2: Outturn and estimated expenditure, POSTCOMM

<table>
<thead>
<tr>
<th></th>
<th>2001-02 actual outturn £'000</th>
<th>2002-03 Forecast outturn £'000</th>
<th>2003-04 Forecast outturn £'000</th>
</tr>
</thead>
<tbody>
<tr>
<td>Staff costs</td>
<td>1881</td>
<td>2233</td>
<td>2778</td>
</tr>
<tr>
<td>Other running costs</td>
<td>1162</td>
<td>1216</td>
<td>1305</td>
</tr>
<tr>
<td>Outside consultants, lawyers, etc.</td>
<td>2268</td>
<td>2083</td>
<td>2390</td>
</tr>
<tr>
<td>Sub-total</td>
<td>5311</td>
<td>5532</td>
<td>6473</td>
</tr>
<tr>
<td>Depreciation</td>
<td>331</td>
<td>350</td>
<td>435</td>
</tr>
<tr>
<td>Cost of capital</td>
<td>29</td>
<td>36</td>
<td>35</td>
</tr>
<tr>
<td>Capital expenditure</td>
<td>752</td>
<td>91</td>
<td>540</td>
</tr>
<tr>
<td><strong>TOTAL</strong></td>
<td><strong>6423</strong></td>
<td><strong>6009</strong></td>
<td><strong>7483</strong></td>
</tr>
</tbody>
</table>

In recent years the Royal Mail’s performance has seriously deteriorated. The level of under-performance remains disturbingly high in certain parts of the UK. Labour relations, evidenced by the spate of unofficial strikes in autumn 2003, are appalling. The Post Office’s financial performance is not much better. In the year to March 2003, the state-owned corporation lost £611m on a turnover of £8.3bn. The inability of the Post Office to achieve reasonable service and financial performance standards 57 raises the issue of whether the much-cherished universal service obligation can be maintained.

57 POSTCOMM requires the Royal Mail to compensate bulk mailers if these targets are missed and compensate individual customers if other mail is delivered late. In 2003 POSTCOMM fined the Post Office £7.5m because it was unable to meet the 2002/3 target set for postage paid business post (POSTCOMM set a target for of 92.5 per cent delivered next day, but the Royal Mail only delivered 84 per cent next day).
Significantly, POSTCOMM has already started to question what constitutes the universal service obligation. In November 2003, POSTCOMM suggested changes to UK’s universal postal service, aimed at clarifying precisely which services make up the universal service in the UK and how they should be provided by Royal Mail.

The Royal Mail currently enjoys a 99.7 percent share of the market in mail services. But the Post Office’s management team realise that it will have to trim costs and improve efficiency if it is to have any hope of competing with new entrants (In July 2002, the Royal Mail announced a three year programme involving 30,000 job cuts across all tiers of staff - by December 2003 it had reduced its 200,000 workforce by 14,500\(^{58}\)). In this respect, POSTCOMM has acted as a catalyst for greater competition, implementing a phased approach to opening up the market.

In January 2003, the regulator opened 40 percent of the Royal Mail’s market – expressed in volume terms - to competition. Phase Two of this Programme will see a further 30 per cent of the postal market opened up to competition in April 2005. In the third and final phase, POSTCOMM plans to open up the final 30 percent of the market to full competition as from April 2007. It should also be noted that EU rules now dictate that postal services across Europe should be made more contestable – all post weighing over 100 gm must be opened up to competition.

To date, POSTCOMM has awarded a number of licences to rival groups, including TPG, the Dutch postal service, Deutsche Post and Express Dairies, who recognise that postal delivery could be an attractive source of additional revenue.

POSTCOMM is licensing an activity termed ‘consolidation’, which allows a licensed operator to pick up and sort mail from customers, and then transfer it to a point in the Royal Mail delivery chain. Under this scheme, it is then the Royal Mail’s responsibility to deliver the mail to the final destination. The Post Office has a statutory obligation to allow rivals to use its delivery network. In return, the Royal Mail receives a fee for the use of its system.

Royal Mail has dragged its heels over agreeing such a fee; indeed, it appeared as though POSTCOMM would need to intervene in order to set appropriate access charges. However, in December 2003, faced with such regulatory intervention, the Royal Mail finally signed a delivery agreement with UK Mail, a subsidiary of Business Post, for ‘last mile’ delivery\(^{59}\). This voluntary resolution was welcomed by Graham Corbett, POSTCOMM’s chairman, who commented that it is “good news to see the industry moving decisively towards taking responsibility for its own commercial arrangements”\(^{60}\).

\(^{58}\) Daily Telegraph, 13 December 2003.

\(^{59}\) ‘Last mile’ delivery shares certain natural monopoly characteristic with BT’s ‘local loop’.

\(^{60}\) POSTCOMM press release, 17 December 2003.
POSTCOMM has fulfilled a useful role as a catalyst for greater competition. Over the next few years, postal services are likely to be transformed as more licensed operators compete with the Royal Mail, which is destined to lose most of its monopoly privileges. Crucially, this should reduce the need for regulation, as consumers will be able to choose between a wider range of suppliers.

POSTWATCH

The Consumer Council for Postal Services (POSTWATCH) was established on 1 January 2001, replacing the Post Office Users National Council (POUNC). A review of its subsequent growth and activities is instructive.

The POSTWATCH headquarters is located in London, and the organisation has nine regional offices throughout the UK. The Council consists of a Chairman, four Council Members and nine Regional Council Chairmen. Besides two part-timers, total full-time staff at POSTWATCH headquarters amount to 80 people, including 12 'network advisers' (officials who are assessing the future of post offices threatened with closure). There are a further 32 full-time staff based in the regions, and 12 staff employed full-time at the POSTWATCH Customer Call Centre located in Belfast. The nine regional Chairs receive a fee as well as four co-opted National Council members.

Payroll numbers have soared since POSTWATCH was first established. In 2001/2 there were 37 full time employees and four National Council Members received emoluments. In addition, POSTWATCH employed nine part-time staff. Two years later, this figure had risen to 59 full-time employees with 14 part-time staff (these figures exclude the four National Council Members who also receive a fee). In aggregate, POSTWATCH currently employs 124 full-time and 15 part-time members and staff. This figure is treble the size of the 2001/2 payroll; what is more, it is treble the size of POSTCOMM'S total headcount.

Annual expenditure in 2002 and 2003 was approximately £8m. However, the level of annual spending is projected to reach almost £10m in the year to March 2004. POSTWATCH appears frustrated and ignored and complains that it is unable to refer POSTCOMM’s decisions to the Competition Commission. This reflects a common grievance among the consumer panels set up by the Government since 1997. They wish to play a more important role in decision making and settling the licensing conditions of regulated companies. However, this is meant to be the regulator’s role. The fact that consumer panels’ are bidding to do the same job betrays the confusion over the distinct roles of regulator and consumer spokesmen – the regulator was originally conceived of as a proxy for the consumer. Establishing consumer panels tends to

---

61 Figure supplied by POSTWATCH Press Office, January 2004.
trigger friction between the regulator and the consumer body over who is representing the consumer.

Relations between POSTCOMM and POSTWATCH appear to have deteriorated. In evidence to the Lords select committee inquiry, POSTWATCH accused POSTCOMM of failure on several fronts, including poor decision taking, inadequate and unsound consultation, a reluctance to publish information and providing an ‘inside track’ in negotiations with the Royal Mail. POSTWATCH also argued that the regulator was not accountable to postal users.

POSTWATCH does not appear to be performing well. In its submission to the Lords Constitution Committee inquiry, it made a series of factual errors.

**ORR**

The Office of the Rail Regulator (ORR – Ofrail was deemed an unsuitable name) has seen annual expenditure increase from £8m in 1996/7 to £13.3m in 2002/3. In percentage terms, this is a two-thirds gain. ORR's budget for 2003/4 is £15.3m. Staff numbers have increased from 86 in 1996/7 to 124 in 2002/3, a rise of 44 percent. The Strategic Rail Authority's accounts are a labyrinthine bureaucratic maze. Strictly defined, the budget in 2002/3 totalled £34.9m and the total number of staff employed amounted to 382. Staff numbers are projected to increase to 499 in 2003/4.

The ORR’s budget is divided between four functions: infrastructure and regulation; rail market access and performance; corporate affairs (albeit a broad definition) and the regulator’s office. It is interesting to note that while the regulator’s office only employs seven people, it accounts for a fifth of the ORR’s budget.

Rail regulation has probably proved the greatest disappointment of all the regulatory models established following the wave of privatisation measures implemented over the last two decades. The regulatory structure is part of the problem. Accordingly, the Secretary of State for Transport decided in early 2004 to initiate a wide-ranging review of the rail industry.

Four problems stand out. Firstly, the roles of the ORR and Strategic Rail Authority (SRA) are confused – a state of affairs that has led to repeated confrontation between the two bodies. Furthermore, ministers have found it difficult not to interfere, particularly as the cost to the taxpayers has soared. Thirdly, a series of major accidents, involving many fatalities, has generated a risk-averse culture within the rail sector. And finally, there has been a shocking inability to estimate accurately the true cost of modernisation schemes, notably the West Coast

---

62 POSTWATCH submission to the House of Lords’ Constitution Committee inquiry into regulation, paras 7, 17 and 18, April 2003.
63 See, for example, ‘No niceties as Winsor presses SRA’, Daily Telegraph, 28 October 2003.
upgrade between London and Glasgow. This last factor effectively bankrupted Railtrack and led to the effective renationalisation of the rail infrastructure network.

The statistics show that privatisation proved a noticeable success in the first five years.\textsuperscript{64} Passenger numbers rose by 20 percent between 1992/3 and 1999/2000, punctuality improved, as did the catering, and the rolling stock was modernised. More than anything, the new rail franchisees demonstrated a customer sensitivity never seen under British Rail.\textsuperscript{65}

However, the rail industry began to slide into decline in the late 1990s following serious accidents, including the major disasters at Paddington and then Hatfield in 2000. The Transport Act 2000 created a new franchising authority, the SRA, responsible for allocating taxpayers’ subsidies to the rail network. The SRA’s precise role and relationship with the ORR was never satisfactorily defined and regulatory intervention by both these bodies began to show a marked increase.

A risk-averse culture was fostered by the Health & Safety Executive, which began to view the railways as a major hazard industry, in the phrase of the Executive’s former head of rail safety, Alan Osborne.\textsuperscript{66} Expenditure on track and signalling soared to £6bn a year whereas train performance, reflected in punctuality, declined sharply.

As a concept, risk management appears to have fallen by the wayside. Hundreds of millions of pounds have been spent on seeking to avoid further accidents, even though rail is a far safer mode of transport than road. The National Audit Office observed: “Fear of prosecution if an accident occurs can also encourage railways executives and engineers to adopt a risk-averse stance, and these factors can lead to the cost of safety-related improvements being very high when compared to the risk of an accident”.\textsuperscript{67}

Unless major changes are implemented in the way in which the UK rail industry is organised and regulated, the level and cost of regulatory intervention is likely to steadily increase. The key


\textsuperscript{65} For example, platform staff in smart new uniforms helped passengers on to trains on the West Coast route, something never seen in the British Rail era.

\textsuperscript{66} Alan Osborne resigned in exasperation as head of rail safety at HSE in October 2003, less than a year after he was first appointed (source: ‘Why Network Rail is going nowhere fast’, \textit{Daily Telegraph}, 29 November 2003).

\textsuperscript{67} \textit{Network Rail – Making a Start}, December 2003, National Audit Office.
problem with the industry is that it faces incessant government intervention, either directly by ministers or through the regulatory superstructure that has developed over the last decade. Ministers continue to determine the key elements of rail policy. At present, the Secretary of State for Transport is provided with the necessary legal authority under Section 4 (5 a) of the Railways Act 1993. The rail regulator and the Strategic Rail Authority implement the details framed by government.

For its part, the ORR essentially fulfils three roles: it regulates the state-owned monopoly provider of rail services Railtrack; it further regulates the use of rail capacity and it is responsible for encouraging effective and efficient working relationships between players in the rail industry (alas, not a role that it appears to have performed with any notable success); and thirdly, it is charged with promoting competition and preventing anti-competitive agreements and practices in the rail industry – a derogated role it receives under an amendment to the 1998 Competition Act (Otherwise this role would be performed by the OFT).

These roles need to be fundamentally rethought. The separation of track and signalling from the rest of the rail industry has patently not worked. Disaggregation has merely led to each side of the industry blaming the other for shortfalls in service. The infrastructure provider has slid into bankruptcy and it is currently absorbing vast amounts of taxpayer subsidy, a trend only marginally held in check by the rail regulator.

**Costs per head**

The common theme that emerges from this analysis of regulatory agencies is one of remarkable growth. Overall, the numbers of people employed by the dozen regulatory agencies has grown by 157 percent (albeit the FSA did not exist in 1996/7 and POSTCOMM had also yet to be established). The cost of running these regulators, meanwhile, has increased by 261 percent. This is partly due to the rapid increase in costs per head, including salaries and benefits.

---

68 Sir Simon Jenkins, a former BR non-executive director, has consistently argued that the 1993 Railways Act placed far greater power in the hands of ministers than ever existed under nationalisation. In *The Times*, issue of 21 January 2004, he wrote that, "Whitehall involvement in the railway is greater than ever since wartime. Forty people in Whitehall oversaw rail policy in 1990. There are more than 900 today, including the SRA's 600 staff, plus a mystifying £50 m worth of 'consultants', equivalent to a further 1,000".

See also *Accountable to none: the Tory nationalization of Britain* by Simon Jenkins, Hamish Hamilton, 1995.

69 See *Access Charges Review: Final Conclusions*, 12 December 2003, where the ORR has decided to ‘limit’ Network Rail’s funding requirements to £22.2bn over the five years beginning April 2004.
Table 3: Regulator costs, payroll numbers and average cost per head

<table>
<thead>
<tr>
<th>Regulatory Agency</th>
<th>Expenditure/Budget £m</th>
<th>Payroll numbers</th>
<th>Cost £K per head</th>
<th>1996/7</th>
<th>2002/3</th>
<th>1996/7</th>
<th>2002/3</th>
<th>1996/7</th>
<th>2002/3</th>
</tr>
</thead>
<tbody>
<tr>
<td>Competition Commission</td>
<td>7.9</td>
<td>16.3</td>
<td>97</td>
<td>155</td>
<td>105.2</td>
<td>81.4</td>
<td>105.2</td>
<td></td>
<td></td>
</tr>
<tr>
<td>OFT</td>
<td>19.5</td>
<td>54.2</td>
<td>402</td>
<td>631</td>
<td>85.9</td>
<td>48.5</td>
<td>85.9</td>
<td></td>
<td></td>
</tr>
<tr>
<td>FSA</td>
<td>221</td>
<td>2313</td>
<td>186</td>
<td>180</td>
<td>95.5</td>
<td>90.9</td>
<td>111.7</td>
<td></td>
<td></td>
</tr>
<tr>
<td>ITC (yr end 31 Dec)</td>
<td>16.9</td>
<td>20.1</td>
<td>186</td>
<td>180</td>
<td>95.5</td>
<td>90.9</td>
<td>111.7</td>
<td></td>
<td></td>
</tr>
<tr>
<td>OFTEL</td>
<td>9.5</td>
<td>19.5</td>
<td>172</td>
<td>236</td>
<td>82.6</td>
<td>55.2</td>
<td>82.6</td>
<td></td>
<td></td>
</tr>
<tr>
<td>BSC</td>
<td>1.3</td>
<td>3.9</td>
<td>24</td>
<td>20</td>
<td>195.0</td>
<td>54.2</td>
<td>195.0</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Radio Authority</td>
<td>3.4</td>
<td>4.8</td>
<td>33</td>
<td>47</td>
<td>103.0</td>
<td>102.1</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Radiocommunications Agency</td>
<td>42.3</td>
<td>66.9</td>
<td>514</td>
<td>580</td>
<td>115.3</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>OFGEM (previously OFFER &amp; OFGAS)</td>
<td>23.1</td>
<td>38.5</td>
<td>357</td>
<td>320</td>
<td>120.3</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>OFWAT</td>
<td>9.6</td>
<td>11.5</td>
<td>190</td>
<td>233</td>
<td>49.4</td>
<td>50.5</td>
<td>49.4</td>
<td></td>
<td></td>
</tr>
<tr>
<td>POSTCOMM</td>
<td>6.5</td>
<td>71.2</td>
<td>86</td>
<td>124</td>
<td>91.3</td>
<td>93.0</td>
<td>107.3</td>
<td></td>
<td></td>
</tr>
<tr>
<td>ORR</td>
<td>8</td>
<td>13.3</td>
<td>86</td>
<td>124</td>
<td>93.0</td>
<td>91.3</td>
<td>107.3</td>
<td></td>
<td></td>
</tr>
<tr>
<td>STRATEGIC RAIL AUTHORITY</td>
<td>34.9</td>
<td>382</td>
<td>382</td>
<td>382</td>
<td>91.3</td>
<td>91.3</td>
<td>91.3</td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>TOTAL</strong></td>
<td><strong>141.5</strong></td>
<td><strong>511.4</strong></td>
<td><strong>2061.0</strong></td>
<td><strong>5292.2</strong></td>
<td><strong>68.7</strong></td>
<td><strong>91.3</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Note: Missing data for Postcomm and SRA have been in filled using the 2002/3 average cost per head.

In its report for HM Treasury, W S Atkins concluded that OFGEM, OFTEL, OFWAT and the ORR were "professionally run organisations" where there were "many examples of good practice". However, the Atkins study highlighted three main areas of concern - the lack of information made available to measure their efficiency; the relatively high cost of support services, such as finance, human resources and IT; and the perception that "the regulators need to have a bigger cadre of senior professionals but with fewer staff supporting them".

Regulators claim to have made a determined effort to try and make the cost of regulation more transparent to stakeholders. This has been encouraged by the Better Regulation Task Force, which published a highly critical report in July 2001. The Task Force recommended that regulators should publish annual business plans setting out how they plan to prioritise their different economic and non-economic objectives. The Task Force further recommended that

---

70 Economic Regulators, July 2001, see discussion in chapter 2.
economic regulators should be obliged to publish cost-benefit assessments for proposals with any significant impact on business activity.

In its report on *Independent Regulators* the Better Regulation Task Force pointed out that "a number of economic regulators have said publicly that they will publish impact assessments of major policy proposals. This is a welcome step forward from the reaction we received in 2001".\(^{71}\)

Although central government now complies with the requirement for Regulatory Impact Assessments (RIAs), the extent of this compliance is still somewhat confused and they are not well completed.\(^{72}\) The Better Regulation Task Force observed that "we still have some concerns about the overall quality of RIAs".\(^{73}\) The extent to which regulators should use RIAs is unclear, not least because it is far from obvious where the offices of the regulators should be concerned with promoting new regulations at all. It is for government to push new regulations through parliament and for the regulators to enforce whatever becomes the law. Accordingly, RIAs should be produced by the relevant departments of government, not by the regulators.

On the second area of concern identified by the Atkins report, it certainly seems to have been the case that regulator were spending considerable sums on support services (equivalent to 22 per cent of the four utility regulators' total expenditure in the year 1999/2000 - nearly double the figure of a comparator group of executive agencies and other regulators selected by the Treasury consultants). This led Atkins to comment that, "On the fact of it, this analysis suggests that too much money is going into non-regulatory activities and some economies might be achievable in overheads".

The third and final concern expressed by the Atkins inquiry appeared to strike a chord with many stakeholders, including regulated companies. Regulators such as OFTEL were experiencing very high rates of staff turnover because they were poor payers, particularly when seeking to recruit in central London. OFGEM has also had to pay substantial amounts in consultancy fees because it was unable to attract suitably qualified staff at the rates it was permitted to pay by the Treasury.

Since the Atkins report was published H M Treasury has allowed regulators greater discretion when it comes to recruiting and retaining staff. A lesson appears to have been learnt from the experience of the ITC, where overall staff numbers were culled by the CEO, Dame Patricia Hodgson. At the same time, Dame Patricia and her board have not been reluctant to offer competitive salaries and perks to attract the right calibre of staff.

\(^{71}\) *Independent Regulators*, BRTF, 2003, p.31.


This approach appears to have been adopted at OFCOM, where more than 70 staff will be earning more than £100,000 a year. The new chief executive, Stephen Carter, makes no apologies for the fact that OFCOM will cost considerably more than the five regulatory agencies it replaces: "Good regulation is not synonymous with cheap regulation. We will not be cheaper to run and at no time would we want to find ourselves in a position where we were under-financed".74

This section has reviewed the regulators reported budgets and headcount up to 2003. The existing picture is completed, before we review alternatives, with a final section on the newest regulator, which opened for business on 29 December 2003, OFCOM.

**Section Five: OFCOM**

OFCOM is the new super regulatory agency established to oversee the broadcasting and communications sectors. In a press conference held on 16 December 2003, OFCOM's chairman, Lord Currie, and its chief executive, Stephen Carter, set out their plans for the agency. This was an important event since it was the first opportunity to learn about the regulator's budget and staffing.

There were many welcome aspects to this briefing. Stephen Carter began by stating that his aim in running OFCOM was "not the growth of regulation". He stressed that OFCOM would "regulate with a clearly articulated and publicly reviewed Annual Plan, with stated policy objectives".

In merging five separate regulatory agencies, OFCOM had taken the opportunity to streamline the combined headcount by 297 people, mainly processing and administration jobs. This is equivalent to a cut of 34 percent in payroll numbers. Table 4 details the efficiencies that OFCOM claims to have achieved in operational areas apart from its policy work.

---

74 Speech to the Incorporated Society of British Advertisers on 1st July 2003.
Table 4: OFCOM headcount compared with the five previous regulators

<table>
<thead>
<tr>
<th></th>
<th>Previous Regulator Total Operational Headcount</th>
<th>OFCOM Total Operational Headcount</th>
<th>% Reduction</th>
</tr>
</thead>
<tbody>
<tr>
<td>Human Resources</td>
<td>46</td>
<td>22</td>
<td>-52%</td>
</tr>
<tr>
<td>Communications</td>
<td>45</td>
<td>14</td>
<td>-68%</td>
</tr>
<tr>
<td>Operations</td>
<td>457</td>
<td>330</td>
<td>-28%</td>
</tr>
<tr>
<td>Commercial</td>
<td>131</td>
<td>90</td>
<td>-31%</td>
</tr>
<tr>
<td>General Administration</td>
<td>204</td>
<td>130</td>
<td>-36%</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>883</strong></td>
<td><strong>586</strong></td>
<td><strong>-34%</strong></td>
</tr>
</tbody>
</table>

Source: OFCOM

However, OFCOM is in the midst of recruiting skilled professionals with expertise in competition law, economics, R&D and project management in order to meet – as Stephen Carter explains - its statutory role as a "robust regulator". In accordance with the remit set by Parliament, the new regulatory body intends to conduct a considerable number of evidence-based inquiries. It has already launched three such reviews: a public service broadcasting review; a spectrum framework review and a telecoms strategic review.

One of the original justifications for establishing the new communications regulators was to save costs. As noted above, this aim will not be met. Such is the scale of the additional duties bestowed on OFCOM by Parliament - a further 135 duties on top of the 128 duties laid down for the five regulatory bodies it replaces - that OFCOM estimates that its total running costs in 2004/5 will be £164m. This includes a £20m charge on the loan repayment it has negotiated with the Treasury for the exceptional charge associated with set-up, transition and inherited liabilities. It also includes a VAT charge of £8m that it cannot reclaim from Customs & Excise as a statutory organisation. This total of £164m also incorporates a budgeted £8m in additional running costs associated with OFCOM's extra duties as laid down by the Communications Act.

This £164M compares with £115M for the five previous regulators in 2002/3 and £73M in 1996/7.

OFCOM's array of statutory duties reflect the importance the Labour government attaches to a whole host of non-economic objectives. The detailed 263 duties are listed as in the Appendix but are summarised on their website as:

“Under the Communications Act 2003:

3(1) It shall be the principal duty of Ofcom, in carrying out their functions;

(a) to further the interests of citizens in relation to communications matters; and

(b) to further the interests of consumers in relevant markets, where appropriate by promoting competition”

39
OFCOM’s specific duties fall into six areas:

1. Ensuring the optimal use of the electro-magnetic spectrum
2. Ensuring that a wide range of electronic communications services - including high speed data services - is available throughout the UK
3. Ensuring a wide range of TV and radio services of high quality and wide appeal
4. Maintaining plurality in the provision of broadcasting
5. Applying adequate protection for audiences against offensive or harmful material
6. Applying adequate protection for audiences against unfairness or the infringement of privacy”.

In practice, the Communications Act looks as though it will be one of the most interventionist and burdensome pieces of legislation passed by Parliament in the last quarter of a century. Originally promoted as a light touch piece of legislation, the Act has not lived up to its billing. The blame for this lies with Parliament and politicians. As Stephen Carter has pointed out: "many still subscribe to the original billing for the Act that it would be a light touch piece of legislation. It may indeed have started out that way in the politicians’ minds and OFCOM as a body will indeed aspire to be a light touch regulator; but it is certainly not a light touch piece of legislation. Instead, as it went through Parliament, an almost unspoken bargain emerged. To paraphrase it: ‘ownership and control will be liberalised; but as a counter-weighting safeguard we, Parliament, will actually increase the detail and demands of regulation’”.

Section Six: Two Alternative Regulatory Approaches

The previous five sections of this paper have shown how the offices of the regulators have grown since they first came into being nearly two decades ago. Of course, commercial activities need to be regulated, but that is a separate issue. The question here is the extent to which some sectors need regulators in addition to the norm. Regulation of all forms of business has been growing apace and also applies to the sectors reviewed in this paper. The main, and perhaps the only, fundamental distinction between general business and these sectors is their degree of monopoly due to the nature of their business or the costs or scarcity of supply. In other words, they are in markets where competition cannot be relied upon to give the consumer good value for money. Thus the original idea was that the sectoral regulators would bring competition and then fade

---

75 http://www.ofcom.org.uk/about_ofcom/how_we_work/statutory_duties
76 ‘The Communications Act: Myths and Realities’, speech by Stephen Carter to media and legal practitioners, 9 October 2003, available on OFCOM’s website, www.ofcom.org.uk
77 For a discussion of what constitutes a natural monopoly, see Privatisation, Restructuring, and Regulation of Network Utilities, by David Newbery, MIT Press, 1999, especially chapter 2.
away. Competition has increased in some areas but as far as bureaucratic withdrawal is concerned, the record has been patchy (examples are discussed below).

This will not have surprised those who study organizations. The prime objectives of any biological organism, including bodies corporate, are to maintain life, but directly and through reproduction, and to grow. Companies were original conceived to provide short-term capital for finite ventures but they rapidly became self-perpetuating. As Charles Handy and others have pointed out, companies do not exist in order to make money but make money in order to continue to exist. Acquiring other companies may not be good for shareholder wealth (it usually is not) but meets the company’s desire for growth and protects it, usually, against being absorbed by others. So we would expect the regulators, and their supporters, to seek new reasons for their existence and for their growth and to resist any idea that they should fade away. In the economics literature, the Public Choice School has taught us that regulators are very reluctant to disappear. Indeed, in California the telecoms regulator after liberalisation was bigger than ever.78

Some might argue that the original idea of transition to competition was wrong. Perhaps market competition in these sectors regulation would not provide the best value for consumers? (consumers and taxpayers being usually one and the same). It is possible that the existing arrangements are evolving, however clumsily, in the right direction, but two other alternatives should be explored: reverting to the original transitional economic regulators and eliminating them entirely apart from a strengthened overall competition regulator based on a merger of the Competition Commission and OFT. Doubtless some will be horrified by either suggestion but after two decades where regulators have only partially achieved their original objectives and are floundering in a welter of new ones, it is at least time to compare alternatives.

In assessing the future need for regulation, we first consider the two main arguments for the offices of regulators as they now exist: natural monopolies and democratic accountability. The first reflects their original economic role and the second underlies their transformation under the current administration, namely that, in addition to economic considerations, regulators, and thence those industries, should be responsible for social and other non-economic objectives laid down by government.

**The economic rationale for regulators**

Sectoral regulators are required where there is a dominant trader or natural monopoly. In this respect, the exclusion of the BBC from OFCOM is a departure from logic, a point reinforced by the recent Hutton Report. For the gas and electricity supply industries and the local loop in the telecommunications sector, it is economically wasteful to reproduce their networks with secondary systems with streets being dug up to lay distribution pipes and cabling for all suppliers.

78 Keith Boyfield discussion with Irwin Stelzer, March 2000.
Technological advances can, however, transform the economics of these industries to the extent what were deemed to be natural monopolies are opened up to competitive entry. In telecommunications, for example, cellular telephony and wire internet services offer competitive alternatives to fixed link networks. Similarly, OFWAT has consistently encouraged new opportunities for competitive services in the water services sector (principally competition at the margin of water utilities' monopoly territories).

OFTEL has carried out a market segment review to establish whether a telecoms market is sufficiently competitive for the regulator to withdraw completely from price capping and other forms of regulatory intervention. Accordingly the regulator no longer intervenes in the international direct dialling telephony market. More recently, OFTEL invited consumers to choose which telephone directory services they wished to use following the abolition of BT's 192 monopoly. OFTEL's work programme included exit strategies for the regulator as well as target dates for a review of the need for continued regulation. What is more, OFCOM, which has taken over responsibility for telecoms regulation, has a statutory responsibility to review whether regulation is still required in specific markets.\(^{79}\)

Other regulatory agencies, such as OFGEM, have adopted a similar approach to OFTEL when it comes to reviewing the need for continued regulatory intervention. Thus, in the electricity sector, OFGEM concluded in April 2002 that it was no longer necessary to continue the residual controls on the prices charged by suppliers to their customers. By April 2003, OFGEM had withdrawn from some 70 percent of the activities subject to regulation at the time of privatisation.

However, it remains the case that it is the regulator who judges when it is appropriate to withdraw from regulating a specific market. In this sense, they are both judge, defence and prosecution over the need for their continued role. Where the regulator no longer intervenes directly with regard to prices, they still claim to have an essential role. For example, OFGEM state that where competition has been established, "OFGEM has a role to monitor its progress and, if necessary, enforce licence obligations, competition and consumer law, so that all customers continue to benefit".\(^{80}\)

**The non-economic role for regulators**

The independence regulators enjoyed from government, an integral part of their justification under the previous Conservative administration, formed the focus for attack by Labour. The

\(^{79}\) This was a point acknowledged by Lord Currie at the OFCOM press conference held on 16 December 2003.

\(^{80}\) OFGEM memorandum submitted to the House of Lords Constitution Committee Inquiry, May 2003.
history of nationalised industries led some to believe that the less politicians meddled in these sectors, the better the deal consumers would receive. Privatisation has had its faults but the overall performance of denationalised sectors of the UK economy has been impressive.\(^{81}\)

Yet the independence regulators enjoyed under the original privatisation statutes was frustrating for a new administration. It was claimed that the regulators were not democratically accountable. Bringing “democratic accountability” meant, in effect, a degree of re-nationalisation without the political difficulties of that concept.

Clare Spottiswoode, the former head of OFGAS, has consistently opposed moves to politicise regulation. In the early years of privatisation, she notes: "The regulators were economic, and were not expected to be involved in other areas unless this could be done without affecting significantly the main role of creating an efficient industry". In contrast, she points out, "This is much less clear cut these days, regulators do appear to be expected to be an arm of Government policy, which inevitably brings them into the political arena. The Government publishes 'guidance' to regulators as to how to deliver some of the Government's policy aims".\(^ {82}\)

Clare Spottiswoode suggests that regulators should be solely responsible for economic regulation. Environmental and social policies should be the responsibility of elected Government ministers. In reaching their decisions, ministers should explain their reasoning and not hide behind supposedly independent regulators.

The issue of democratic accountability is, deliberately or not, misleading. A government is, to a large extent, entitled to decide what functions it performs in the name of the people itself, the functions it devolves to independent bodies such as the courts and regulators, and what is left with the private sector. What it should not pretend is that regulators are independent if they are not, nor should it give regulators functions they cannot fulfil. For example, requiring regulators to deal with social issues without a framework to decide them or the means to pay for them will cause, and indeed has caused, them to increase in girth while reducing in potency. The eunuchs in 18\(^{th}\) century Turkish courts provide an interesting analogy. They kept order but did little to improve innovation and choice.

We now consider two alternatives: (1) returning regulators to their original role and, (2) replacing them all by a single Fair Trading Authority. The section then concludes with the implications for individual regulators.

\(^{81}\) See, for example, *Privatisation: A Prize Worth Pursuing?* By Keith Boyfield, European Policy Forum, May 1997.

\(^{82}\) House of Lords Constitution Committee, Inquiry into regulators, Memorandum of evidence submitted by Clare Spottiswoode, para 20.
(1) The economic regulators alternative

The alternative of returning regulators to perform purely economic roles, essentially to proxy the effects of competition, has been discussed above. The regulators would still be additional to the general EU and UK competition requirements, but the links to the Competition Commission and OFT should be clearer. In effect, the regulators should be subsidiary to the Competition Commission, to whom there should be the right of appeal. The Competition Commission should have as much independence from government as the law courts.

The office by office implications are covered below, but in general the non-economic roles given to regulators would be either (i) returned to Whitehall departments, or (ii) devolved to the companies in those sectors, or (iii) delegated to non-executive consumer advisory groups, which exercise power firstly through dialogue with company boards and secondly through publicity.

Whitehall departments have, since the 1980s, been encouraged to devolve activities to “Next Steps Agencies” but there is an important distinction between these agencies as extensions of government and the offices of regulators which are supposed to be independent and acting in the interests of consumers.

One area of current confusion is the provision of utilities, for example, posts and phones in outlying country areas and islands, where prices to consumers are considerably below costs. The government needs mail contact with these citizens (Inland Revenue, DWP) and more efficient solutions (for example, PO boxes, and increasingly e-mail through the e-government initiative) may reduce the gap. Where the deficit remains, it is unclear who should pick up the bill. This has no simple solution but probably the least bad is for these matters to be negotiated between suppliers and local government. Some solutions, for example, mailboxes as in the USA, are less expensive than others and should be tailored to local needs. Local governments in these areas already received higher per capita grants from EU and UK governments and these grants might need adjustment. The point is that companies would be able to operate commercially and competitively, leaving social aspects in social hands.

What would be the impact on the headcount and budgets of regulatory offices? Dame Patricia Hodgson, the former head of the ITC, observes that headcounts and budgets are arbitrary. She suggests that they should simply adapt to the budgets they are set.

“The trouble with regulators is they're programmed to regulate. You can't really ask them to put in a good day's work at the office NOT regulating. So, as well as getting the policies and governing statutes, you need to avoid regulatory creep. The most effective way is to limit the number of regulators! 2,800 at the Financial Securities Authority. Compare these numbers with under 200 at the Competition Commission - a regulator judged by the Global Competition Review as second in the world behind the US structure of the Justice Department and Federal Trade Commission. The Competition Commission is geared to deal with every sector in
our economy, but to concentrate on specific questions: mergers, dominance, price caps. Our super-regulators could well improve their effectiveness by identifying the make or break decisions for their sectors and refraining from other activity”.

“We need much more systematic design work to see whether regulators can operate tight, strategically focused intervention. Let's speculate whether the FSA with 280 staff wouldn’t be pretty much as effective as an FSA with 2,800 staff? If spending constraints meant we had to reduce the FSA to 280 people tomorrow, it wouldn’t be beyond policy design to recast compliance regulation into strategic deterrents.”

In essence, alternative 1 envisages a return to the original transitional economic role for all sector regulators. They should plan for their demise with target dates for each stage. Sunset clauses should be inserted into their constitutions so that they automatically close, or at least their raison d’être is reconsidered, at that time.

There is a role for consumer groups but Labour revisions, such as POSTWATCH, have created antagonism where synergy should prevail. Both alternatives retain non-executive groups representing consumer interests but they should work directly with the suppliers as distinct from competing with regulators. Any intelligent board of management knows perfectly well that cash comes from customers and their needs should prevail. Customer advisory groups are normal practice in the private sector and they can be seen as part of the market research function.

Can this issue then simply be left to the suppliers to decide? Unfortunately not. Companies should provide key marketing metrics, such as market share and customer satisfaction, in their annual reports. The Accounting Standards Board supported by an array of top UK companies recommended, in 1993, that they did but those same companies then failed to follow their own advice. The Accounting Standards Board issued revised guidelines in January 2003 making this advice more specific. However, there is little evidence large firms will comply until they have to. One exception has been the utilities, perhaps because they are regulated.

The reluctance to publish this data has scant justification. The directors should already see these metrics and publication costs nothing. Competitive sensitivity of historic data is only rarely a justification for secrecy. The topic deserves mention here because this information is important for consumer advisory groups wishing to make a constructive contribution. Where privatised companies retain a large market share, over 40 percent for example, it would be reasonable to maintain this requirement for transparency.


84 See Market metrics: What should we tell the shareholders? Tim Ambler, Patrick Barwise and Chris Higson, Centre for Business Performance, Institute of Chartered Accountants in England and Wales, October 2001.
(2) The single Fair Trading Authority alternative

The second approach to regulation is to take the view that, after as many 20 years of privatisation, once state owned companies should be treated no differently to others. They would be subject to the Competition Commission and OFT like any other business. Furthermore, as we discuss below, the lines between these last two are so blurred that they would be better merged as, say, the “Fair Trading Authority” (FTA). As recommended in *The Politics of Regulation*\(^\text{85}\), such a body could focus on developing a consistent approach to competition policy. Responsibility for “good behaviour” would fall on the companies themselves with possibly higher penalties for transgression. So the specialist regulators would be wound up although the FTA might well need some sector specialists to deal with the peculiarities of difficult sectors.

Non-economic roles would be dealt with as in the above alternative. Crucially, this more radical alternative asks why the split between the privatised part of the economy and the rest needs to be perpetuated?

Such a model has been proposed by Dr Cento Veljanovski: “The best way forward is a complete rationalisation with one set of laws governing all industry and sectors administered by a single agency with a proper appellate structure”, he suggests\(^\text{86}\). The question of “appellate structure” is very important. In principle we have three levels:

- Agencies acting within and reporting to government departments.
- Regulators intended to be independent of government (ORR)
- The courts and quasi-courts, such as the Competition Commission. Then the courts have appeal provisions with that system.

In the EU, perhaps too many anti-competition rulings by Brussels are knocked back in the courts because the same department acts as both prosecution and judge whereas in the UK the OFT raises issues for the Competition Commission to determine. There is little doubt that prosecution and judgment should be separate but it is open to question whether this means that the UK needs both the OFT and the Competition Commission when it also has the courts. Alternatively, the role of the Competition Commission as court should be clarified. In that case, it could also be streamlined as the provision of evidence should be a matter for the disputing parties. We return to this crucial issue later.

The new competition authority would apply one set of general competition rules, augmented for network industries, such as telecoms, gas, electricity and post, by price and access regulation.

---


administered by the same body. Many of the problems associated with natural monopolies are similar, so it makes sense to merge the separate industry regulators. Better to have just one body administering competition law than a whole cluster of separate regulatory agencies, each with delegated powers under the 1998 Competition Act.

A precedent for such a radical reform is provided by the work and recommendations of the Australian Federal Government Inquiry on National Competition Policy, chaired by Professor Fred Hilmer (The Hilmer Report). From the outset, the Hilmer Report rejected the UK model of industry regulation observing:

“The Committee started from the proposition that competition policy across all Australian industries should desirably be administered by a single body. In particular, the Committee considers that there are sufficient common features between access issues in the key network industries to administer them through a common body. As well as the administrative savings involved, there are undoubted advantages in ensuring regulators take an economy-wide perspective and have sufficient distance from particular industries to form an objective view on often difficult issues” 87.

As Veljanovski acknowledges, the danger of integration is that it could concentrate power in the hand of just one body rather a raft of regulatory agencies. However, Veljanovski argues that “if at the same time administrative power is diffused and properly checked and made independent of government, then this concern can be addressed”.

This view, influenced by the Austrian tradition 88, is similar to the proposals of Professor Philip Booth. 89 Booth argues that “statutory regulation should not stifle innovations in market practice that can achieve the objectives of statutory regulation more effectively; and that one should look beyond a simple producer/consumer relationship to sophisticated institutions of an extended market order that can achieve many of the objectives that a statutory regulator seeks to achieve”.

Booth concludes that while there may be a special role for statutory regulators in banking markets, in order to address problems associated with potential systemic risk, with regard to short term financial products – motor insurance, household insurance, unit trusts – “it would seem that the most regulators would need to do is to enforce publication of a solvency position on a recognised basis”. Apart from this requirement, it is argued that “the consumer needs to be assured that the contract signed is the contract delivered”. In this context, Booth stresses that

87 The Hilmer Report, p.327.
88 The Austrian School is associated with Ludwig von Mises and Friedrich von Hayek.
“There is no need for special financial regulators to deal with this, even if the issues are slightly more complex than for non-financial products”.

With regard to insurance and pension products, information about the solvency position of suppliers is again key. Such a role could be performed by an intermediary; indeed, insurance brokers already undertake such assessments. Booth comments that, “regulation may need to go further but it is important that any regulation does not impede the development of market-based mechanisms of handling risk and handling long-term relationships between the insurer and the consumer”. The underlying theme of the Austrian approach is that despite its imperfections, the market discovery process is likely to generate more consumer benefits than a market inflexibly regulated by statutory bodies.

Since asymmetric information between suppliers and consumers is a commonplace in modern market economies, reputation, or branding, has become even more important. Indeed, reputation is the principal means through which a market economy deals with consumer ignorance. Self-regulatory bodies, if they are to work successfully, must be prepared to name and shame individual firms. In this way, concern for reputation obliges both individuals and firms to take their own compliance procedures seriously.

Consider, for example, the laundry detergents market. It has relatively few suppliers and a case could be made for a Detergents Standards Authority (DSA) to regulate it. Such a body could intervene in many ways, for example, insisting that lower priced and less advertised products were offered for sale, or by stipulating that all advertising carried lists of ingredients. In the 1960s, this policy approach was adopted by Harold Wilson’s Labour government. Yet the result was that the lower priced, less advertised products were shunned by consumers. Since regulations are useful barriers to entry, such superficially well-intentioned policies risk less innovation, less consumer satisfaction, and less competition. Furthermore, prices would need to rise to meet the costs of the DSA.

Is this a ridiculous line of argument? Not if one examines the FSA, a body that exhibits many of these tendencies because it understands neither marketing nor, as it acknowledges in its Business Plan 2004/5, the consumer. The laundry detergent market works to the benefit of both consumers and suppliers through the mechanism of brands. Brands (or reputations) protect the consumer as well as helping the supplier maintain continuity.

Owners of strong brands have a powerful incentive not to cheat because the cost to the brand’s reputation is likely to be larger than the short-term gain. Bad practice has been a problem in the financial sector as it evolved from a primitive personality market based on friendships (“my word is my bond”) but the problem can be seen as a lack of strong brands. Regulation is not the

90 Ibid.
solution and may, as those of a mischievous disposition focus on ways to evade it, even contribute to bad practice. Furthermore, the problem is compounded by a regulatory authority that, through its ignorance of market mechanisms, prevents the development of strong brands through insistence on rules that are therefore not ultimately in the consumer’s interest.

Implications for particular regulators

We now look more specifically at nine regulatory bodies:
♦ Competition Commission and Office of Fair Trading (OFT)
♦ The Financial Services Authority (FSA)
♦ OFCOM
♦ OFGEM
♦ POSTCOMM
♦ OFWAT
♦ The Office of the Rail Regulator (ORR) and Strategic Rail Authority (SRA)

Competition Commission and Office of Fair Trading (OFT)

To tackle these increasingly apparent problems, it could be seen as sensible to merge the OFT with the Competition Commission, and thus give the UK a single competition authority, albeit with access still available to the courts. This could cut wasteful duplication. As the law currently stands, for example, the OFT is responsible for initial inquiries into mergers that are felt to be anti-competitive. It then hands over to the Competition Commission, where it feels there is a case to answer, and it is left to the Commission to make determinations over remedies (with appeal rights to the Competition Appeal Tribunal\(^2\)). Integrating these processes within one body could simplify matters and the right of appeal through a Tribunal or the courts could be retained.

Such a proposal is likely to raise objections that under current EU intentions, it would be difficult to merge the OFT with the Competition Commission. This reflects the trend in recent merger judgements by the European Court of Justice, where the Court takes the view that separating the initiating role on merger cases from the judging role (currently performed by the Competition Commission) is essential. However, there is another way of looking at this issue. One could establish a merged OFT/Competition Commission expressly to undertake the investigative work on the review of mergers that are felt to risk a substantial lessening of competition. The final decision on whether to allow the merger to go ahead could then be performed by the courts, thereby maintaining the separation between the review of a merger case and the judging function.

\(^2\) See 'Merger watchdog that meet needs bringing to heel', Keith Boyfield, Financial Times, 5 February 2004.
The Federal Trade Commission (FTC) in the US provides a model. It is highly regarded\textsuperscript{93} for its policy work and its staff prepared in-depth reports and testimony for Congress and a wide range of Federal government agencies. The FTC is responsible for a range of federal anti-trust and consumer protection law, having been originally established by the Federal Trade Commission Act and the Clayton Act, both passed by Congress in 1914. The FTC’s anti-trust division, the Bureau of Competition, is charged with tackling anti-competitive business practices. Where it has grounds for believing that there have been violations of competition law, it recommends the FTC to take the case to court. It also uses its statutory powers to address unfair methods of competition and mergers that may result in a significant lessening of competition.

Further research is needed to compare the UK and US processes and the costs, e.g. human resources, involved in dealing with complaints and suspected anti-competitive practices. It will be argued, for example, that the FTC is not a model for the CC at all since the duties of the FTC are much more limited. But then perhaps the duties of the CC should be much more limited. The Americans seem happy enough with their solution in a much larger and more complex market. Again the benefits of the two-tier system (OFT then CC) apply to other regulators and, as noted above, the EU seems headed in that direction.

If the objective is to achieve stronger regulation, then the more tiers the better. Why stop at two? If the objective however is to have strong GDP growth and maximum taxpayer value, then regulation should be minimised consistent with the national interest, even if it does occasionally meet embarrassment in the courts.

The distinguishing aspect of the US system is its reliance on the judicial system to resolve suspected anti-competitive practices. This would appear to provide a more effective form of consumer redress than the UK system. The potential threat of class actions complete with triple damages provides a powerful disincentive for companies to engage in anti-competitive practices. At the same time, the competition authorities must be able to prove their contention that companies and organisations are acting in an illegal manner. Furthermore, it can be argued that legal redress through the courts provides greater certainty since there is less likelihood of political interference in the regulatory process. This is illustrated by the fact that the Labour government declined to reappoint Sir John Bridgeman as Director General at the OFT - a move seen by some commentators\textsuperscript{94} as politically motivated.

Irwin Stelzer, the leading US economic commentator\textsuperscript{95}, has drawn attention to the advantages of a greater involvement by the courts. He notes that there are "no ups and downs due to changes in

\textsuperscript{93} A peer review of UK competition policy commissioned in December 2000 showed that the UK regime is less highly regarded than the US regime (source: DTI annual report, 2002).

\textsuperscript{94} See 'Bridgeman quits as fair trading watchdog', Financial Times, 25 February 2000.

\textsuperscript{95} Irwin Stelzer is a Fellow of the Hudson Institute in Washington DC and the founder of National Economic Research Associates (NERA).
political fashion. It’s a money driven system and I’ve always had great faith in the profit motive. The lawyers who do it are entrepreneurs - they take risks.”

In terms of budget and numbers, more emphasis on the courts as a means of resolving competition issues would enable a streamlining of the current disaggregated anti-trust agencies established in the UK. The Competition Commission currently operates on a budget of over £16m and the OFT presently spends approximately £54m a year, amounting to a total expenditure of £70m. Six years previously, the MMC operated on a budget of less than £8m, while the OFT operated on an annual budget of less than £20m. Allowing for inflation, a merged Fair Trading Authority should be able to carry out its responsibilities on a budget of £40m a year. A staff complement of 500 (compared with the CC and OFT’s combined total of approximately 850) should be sufficient to pursue a more focused agenda, aimed at combating anti-competitive practices.

This could be challenged on a number of bases: the US courts-based approach is not as “good” (but see above for what that may mean) as the EU administrative approach, the 1997 budget was inadequate for successful operation, and the direct benefits of the separate CC and OFT underestimate the full benefits since their decisions are used far more broadly than just for the cases that come before them. In the absence of any published benefits, we cannot be sure but the very absence of publishing such benefits, or any apparent wish to do so, indicates a complacency with the status quo. If the government proposed a merger and a major budgetary reduction, it might at least produce some justification for the budgets they have.

Unless the Enterprise Act 2002 is significantly amended any merged anti-trust agency would face repeated calls to intervene in the UK economy. These calls would be triggered by the statutory obligations it is required to perform in the form of markets and policy initiatives, consumer regulation enforcement and competition enforcement. In particular, the requirement under the Enterprise Act to review super-complaints from designated consumer organisations is likely to prove a remorseless driver for regulatory intervention. A Fair Trading Authority (FTA) should be under no obligation to explore complaints in any depth. Complainants who seem likely to absorb more resource than seems justified to the FTA could be invited to pursue legal remedy in the courts.

---

96 Discussion with Keith Boyfield, 12 April 2000.

97 The DTI has issued a consultation proposal on whether the judicial process could be streamlined to make it easier to bring private legal actions. It is suggested that this could be done by expanding the role of the Competition Commission Appeals Tribunal to allow it to hear claims for damages in competition case brought by harmed third parties.
The Financial Services Authority (FSA)

What can be done to tackle the burden of excessive regulation in the financial services sector? There is a clear choice between accepting statutory regulation, in the form of one single super-regulator, but seeking to make it more efficient, or choosing an alternative approach, influenced by the Austrian tradition in economics, where the onus is on markets to police themselves. A related problem is the growing tendency of investors to look to the authorities, including government, to reimburse them for their own poor investments. Eliminating caveat emptor will prove expensive no matter what form the reimbursement takes.

Of course, the European Commission as well as the UK government is a driver of new initiatives, although it suits Whitehall to cast the EU as the bogey man even where the ideas originate in Whitehall. In pursuing the goal of establishing a single financial services market within the EU by 2005, the Commission's Financial Services Action Plan involves a package of 40 separate measures aimed at bringing this about. The EU is also amending European law governing banking, insurance and pensions. This initiative has adopted the so called 'Lamfalussy approach', aimed at amending in line with a range of 'high level principles'. This work is being steered by the Committee of European Securities Regulators, chaired by the distinguished Dutch lawyer, Arthur Docters van Leeuwen.

Four EU directives have been agreed - the Insurance Mediation Directive, the Financial Groups Directive, the Market Abuse Directive and the UCITS Directive. Further directives being debated include the Prospectus Directive, the ISD and the Transparency Directive. Furthermore, the European Commission plans to issue directives on insurance, reinsurance, corporate governance and clearing and settlement procedures.

The key word above is “directive”. These are not detailed regulations; a directive states the intention and leaves it to member states to decide how that should be achieved. The suspicion that the UK “gold plates” EU legislation and thus places uncompetitive burdens relative to other states is unproven but may well be true. Certainly the Insurance Mediation directive, as noted above, did not actually require a statutory regulator but only a “competent authority”. Member states differ markedly in their approach to financial regulation, with some countries relying heavily on statutory regulation (e.g. Germany), while other countries place much greater emphasis on self-regulation (e.g. Greece).

Views of the FSA are both positive and negative. A 2003 survey by the Corporation of London found 174 major international firms who said the FSA was a big advantage for London, whereas only 31 dissented. But there is also persistent criticism as it is perceived heavy handed and

---


bureaucratic culture. This is partly attributable to the FSA’s keenness on consultation – a trend that has swamped City firms with paperwork.

An opportunity to downsize the FSA presents itself with the appointment of Callum McCarthy as the new chairman. As pointed out in section four, McCarthy succeeded in cutting back OFGEM’s budget and staff numbers as competition established itself in the gas and electricity markets. Reports suggest that McCarthy will seek to promote competition, trim waste, and curbs the FSA’s tendency to be too inward looking\(^{100}\). Furthermore, he has made it clear that he is critical of the length of time the FSA has taken in investigating alleged cases of financial misconduct by both firms and individuals. He is keen to speed up procedures.

The FSA’s new chairman is also a champion of promoting financial literacy and consumer information. In this regard, he is following in the tradition of his predecessor, Sir Howard Davies, who is convinced that the FSA must do far more to educate consumers about financial products and services.

Financial literacy in the UK is undoubtedly poor. Callum McCarthy is apparently fond of quoting the statistic that 25 per cent of the UK population do not understand percentages. It therefore comes as no surprise that a recent survey\(^{101}\) found that 85 per cent of 15-19 year olds want some education about personal finance matters. Clearly, many schools have fallen down in educating pupils about the basics of bank accounts, mortgages and insurance products. But this is essentially indicative of a long-standing problem with the school curriculum – maths lessons would be far more relevant and interesting if they were related to personal financed products rather than obscure commodities such as wheat (many urban school children would not recognise this basic foodstuff).

Education about financial services is not an obvious role for the regulator but one for schools and colleges (a similar misconception applies with OFCOM’s proposed role, see later discussion in this section). For the FSA to pursue a major programme of citizen education about financial services - a step it wishes to take – would be prohibitively expensive and bring it into competition with the entire educational system.

The FSA appears to be too large and expensive. According to the FSA’s own comparisons\(^{102}\), their annual budget of £249m contrasts with a budget of £77.1m for its counterparts in France and £35m in Germany. Whereas the FSA employed 2,313 staff in April 2002/3, the French regulatory bodies employed 888 and the Germans 901. This reflects the fact that in France and Germany, the regulatory authorities are performing a more focused, higher level role where priorities are firmly set. In relation to thriving financial centres in the Far East, such as Hong

\(^{100}\) ‘A regulator who won’t let himself be tied up in red tape’, *Sunday Telegraph*, 30 November 2003.  
\(^{102}\) See Appendix 8, FSA Annual Report 2002/3.
Kong and Singapore, the FSA is also more expensive. The Monetary Authority of Singapore, for example, had a budget of £14.6m and employed 158 staff.

The FSA’s current budget of £215m and its headcount could be at least halved with greater focus and less detail. The FSA’s statutory duty under the Financial Services & Markets Act (FSMA) to educate citizens about financial services should be abolished. The vast proportion of the FSA’s costs relate to staff salaries. In halving its workforce, priorities will need to be re-ordered. This is something the FSA has tended to avoid in the past. Indeed, the City regulator has grown like topsy because it has been unable to prioritise its objectives. The four statutory objectives set out in the FSMA are so broad it is difficult to conceive how they can be fulfilled on a feasible basis. They should be seen as a framework, not a duty.

Placing a cap of say, 1,000, on the maximum number of staff would be the best way of curbing the FSA’s tendency towards pursuing a more ambitious workload (viz, the FSA’s aim to improve financial literacy). This figure is, of course, arbitrary but, as Patricia Hodgson noted above, there is no scientific way to establish the optimal sizes of any of these offices with any precision. Regulators in general, and the FSA in particular, do not have detailed goals or plans for achieving them. There is no Taylorist, stopwatch basis for identifying how many staff would then be required, even if they did. Work, in essence, expands to engage the number of people available and their chief executives, rightly enthusiastic for their roles, will tend to demand more resources for praiseworthy, if vague, objectives. We therefore based this headcount on being slightly in excess of the equivalents in France and Germany.

On the basis that the FSA was limited to a maximum staff headcount of 1,000, then its annual budget should total approximately £100m.

**OFCOM**

While it has been given a wide range of statutory duties, need OFCOM be the size that it has turned out to be? The supposedly “light” regulatory requirement has produced no less than 263 tasks for OFCOM (see Appendix). No doubt each was added to placate some critic of the original Bill but in the event a radical review would now seem appropriate. No organisation should have 263 mandatory objectives.

OFCOM has seven criteria for judging its long-term success in meeting its statutory brief. Of these, only three could be described as strictly economic: namely, lower barriers to entry for innovators, diversity of market supply and regulatory certainty for investors. But a properly working market should encourage lower entry barriers and create a diversity of market supply of its own accord. Establishing regulatory certainty is only required where one has a regulated market. But in the case of broadcasting and communications, the radical (Austrian) alternative would seem perfectly adequate.
The other four success criteria are non-economic. The first relates to broadcast content and formats - an objective that could be left to the market now that viewers can choose between hundreds of different channels (the licence fee currently paid to the BBC could also be reallocated to support programming which is deemed a merit good, such as LWT’s South Bank Show).

Secondly, OFCOM is supposed to encourage media literacy and access. Surely this is a role better performed by educational institutions? Besides, media suppliers will be keen to attract customers for their own products and services, just as in any other market. Concerns about access to broad band and other services should be dealt with by government departments or local authorities, for example, through the provision of up to date computer equipment at schools, colleges and public libraries.

Thirdly, OFCOM states that it wishes to encourage a flourishing TMT sector, but this is a role for the market, not for quasi-public sector theorists. The record of government involvement in sectors of the UK economy is hardly encouraging - one simply needs to recall the chequered history of British Leyland, the National Enterprise Board and government support of the British cinema industry.

The final criterion identified by OFCOM - "greater value and choice for the citizen-consumer" - could also be left to the market and competition law as it applies to every sector of the UK economy.

Lord Currie, the chairman of OFCOM, asserted at the press conference on 16 December that "cheap regulation can be very expensive". Yet it is also possible that expensive regulation can be wasteful. Whilst we recognise that the 263 statutory duties have only just been enacted, the cold light of day would indicate that a fundamental rationalisation should take place sooner rather than later. As in the case of the FSA, the enthusiasm for legislation seems to have converted simplicity into such a maze that we should now ask if it is really worthwhile at all.

The less radical alternative takes a more generous view of the economic need for regulation on this sector. A Leaner and Meaner OFCOM proposed a streamlined OFCOM, excluding the Radiocommunications Agency but within the Communications Act.\textsuperscript{103} This would require a total staff of 390, as set out in Table 5.

\textsuperscript{103} A Leaner and Meaner OFCOM, Keith Boyfield, European Media Forum (EMF), July 2002.
Table 5: Recommended Staffing at OFCOM (Alternative 1)

<table>
<thead>
<tr>
<th>OFCOM board</th>
<th>Chair + up to six members</th>
</tr>
</thead>
<tbody>
<tr>
<td>CEO’s office including strategy &amp; policy unit.</td>
<td>Approximately 50</td>
</tr>
<tr>
<td></td>
<td>(6 in CEO’s office; 10 in policy unit; 15 in common services; 15 in media office)</td>
</tr>
<tr>
<td>Division 1: Network services, Tariffs &amp; Competition Issues</td>
<td>Approximately 200</td>
</tr>
<tr>
<td></td>
<td>(100 dealing with regulatory policy and 100 with compliance issues)</td>
</tr>
<tr>
<td>Division 2: Broadcast Audience Interests</td>
<td>Approximately 140</td>
</tr>
<tr>
<td></td>
<td>(70 handling specialist content policy and tiers 2&amp;3 TV regulation; 30 dealing with programme and privacy complaints; 10 working on media literacy initiatives; and further 30 in the Radio Group)</td>
</tr>
<tr>
<td>TOTAL</td>
<td>= 390</td>
</tr>
</tbody>
</table>

Besides the chief executive's office, which would include a strategy and policy unit, the EMF study envisaged OFCOM operating as two divisions, the first dealing with network services, tariffs and competition issues; and the second responsible for broadcast audience interests. In terms of overall numbers, the CEO’s office, including the policy & strategy unit, as well as the media office, secretariat and common services, should be able to fulfil its responsibilities with a total headcount of between 45 and 50.

As argued in the EMF study, the network services division would require a total staff count of approximately 200 people. This would be roughly divided between one hundred staff dealing with regulatory policy, such as competition policy, telecom spectrum policy and access issues, with a further one hundred officials taking care of compliance matters such as telephone numbering and complaint monitoring. This estimate appears reasonable given the fact that OFTEL employed a total of 208 officials in the year 2000/1. Over time, as the regulator withdraws from detailed intervention, these numbers should reduce.

The division dealing with broadcast audience interests would be responsible for content regulation. In this respect, it would have responsibility for the development of public service broadcasting standards. This will include oversight of tiers 1,2 and 3 policy, as outlined in the Communications Act. The division would also be responsible for TV licensing and enforcement sanctions. Licensing is closely related to programme content, since one of the regulator's main tolls is its power to assign and revoke a broadcasting licence.

---

104 It is worth noting that in 2002, the Prime Minister's reorganised the 10 Downing Street Policy Directorate. The Group comprises only 14 individuals although their remit is to cover the whole of the Government’s domestic policy agenda.

56
The proposals set out in the EMF study are substantially lower than the 880 staff headcount announced by OFCOM’s management on 16 December 2003. The new communications regulator has a far more ambitious goal, which is characterised by a mission to intervene.

**OFGEM**

OFGEM points out that by April 2003, it had discontinued regulating directly in approximately 70 per cent of the activities subject to regulation at the time of privatisation. This is a welcome trend that should be encouraged. There are undoubtedly many more aspects of gas and electricity supply that could be opened up to competition, thereby removing the need to regulate.

The former electricity regulator, Professor Stephen Littlechild\(^\text{105}\), has argued that utility retail issues should be handed over to an economy-wide anti-trust body, presently the OFT. As he told the specialist journal, *Utility Week*, “I think that with the growth of competition, we have to move away from the idea that you have to regulate in detail and monitor everything day by day”\(^\text{106}\).

Thus it is reasonable to ask whether these functions require a separate regulator. As John Smith QC points out, "So long as the Government retains control over entry to utility markets through the grant of licences, the Government must retain the means of ensuring the accountability of the licensee to deliver what the State is expecting".

However, this role need not be performed by a separate regulator. Callum McCarthy, when Director General of OFGEM said: “I would love to go down in history as the last energy regulator but I believe the gas and electricity markets will continue to need some regulation, either by OFGEM or by the OFT. The need to balance real time demand and supply will require some form of oversight. This will inevitably involve complex rules – and someone who understands how the rules work”\(^\text{107}\).

McCarthy recognised that this function could be assumed by an anti-trust body, such as the OFT, although he rightly pointed out that there would need to be a division within such a body dealing with energy issues. But there might well be many advantages in integrating the work done by sectoral regulators, concerned with natural monopolies. As one former Treasury mandarin\(^\text{108}\) has emphasised to one of the joint authors, expansion of sectoral regulators is often unjustified since

---

\(^\text{105}\) Subsequently appointed to OFGEM’s advisory panel of industry experts.


\(^\text{108}\) Sir Steve Robson, the former Second Permanent Secretary at HM Treasury. Discussion with Keith Boyfield.
most of the methodological work on regulatory issues, such as the cost of capital, has already been done. There were few new surprises.

If one established a new Fair Trading Authority this could act as a valuable resource for acquired knowledge on best regulatory practice. Furthermore, as regulatory skills are scarce (as OFCOM is learning), why have such talent permanently focused on just a few sectors of the economy?

The radical option would be to scrap the Utilities Act and transfer OFGEM's remaining responsibilities to a newly integrated competition authority, as described above. The OFT already investigates a wide range of industries ranging from clearing banks, retailers and providers of private education. Why should energy be any different?

Again, as John Smith QC notes, EU law prohibits an abuse of dominant position, and such an abuse may consist of unfairly high prices. This could serve as an alternative approach to licence enforcement or amendment, although as lawyers point out, there are currently no guaranteed rights of appeal through this process.

**OFTWAT**

The water industry is probably the prime example of a natural monopoly. The recent Water Act has also established an independently funded consumer body, WATERVOICE, which appears to have a deteriorating relationship with OFWAT.

Both OFWAT’s budget and staff numbers have shown a marked increase in the last few years. Furthermore, WATERVOICE now represents a substantial new burden on the industry – and its customers. Approximately 25 percent of OFWAT’s expenditure is accounted for by the consumer body\(^\text{109}\), and this will jump now that it has been established as a separate statutory body.

What can be done to counter this regulatory growth? The most effective way to arrest regulatory creep would be to integrate the regulation of the water industry within a general competition authority, as argued above. Most of the complex problems surrounding regulation of the water services sector have now been addressed. With this work concluded, there is scope for integrating OFWAT into a broader competition authority. The objectives of such a reform would be to reduce the overall cost of regulatory oversight and deploy scarce talent to wealth creative activities.

---

\(^{109}\) See Philip Fletcher’s evidence to the Lords Constitution Committee inquiry, 11 June 2003, para 566. In 2002/3, prior to the establishment of WATERVOICE as a separate statutory body, its budget totaled £2,834,000 within a total budget of £11,524,000 for OFWAT and WATERVOICE combined.
OFWAT could be scaled back to an annual budget of around £10m and a total staff of 200 without damaging any of its key regulatory roles. If it was to be integrated within a general competition authority, further savings could be made on accommodation costs as well as ancillary functions such as press & external affairs, IT and general secretarial. A water office within such a body would require around 120 – 150 staff and a budget of £7.5 m would suffice. This is a substantial saving on the estimated budget and staff complement for 2004/5.

WATERVOICE could be replaced by a single consumer advisory body as other organisations adopt to improve their understanding of their markets. The costs of the advisors are low and part of a sensible market research budget. Under the present arrangements, WATERVOICE is likely to move into greater conflict with the water regulator. Its statutory powers are relatively weak, and it will inevitably become frustrated with its inability to exert influence over the key decisions that affect the industry. The regulator’s role is to represent consumers as a proxy for competition. It must balance the industry’s financial stability and investment requirements against legitimate consumer interests. It cannot fulfil this responsibility if there is a consumer body seeking to perform the identical role. The two will simply clash. But the current water regulator, Philip Fletcher, as a career civil servant, takes a quite understandable Panglossian view of the status quo.

The former regulator, Sir Ian Byatt, takes a more detached view. During the course of the Lords Constitution Committee inquiry, when questioned about the permanence of industry specific regulators by Lord Lang of Monkton, Sir Ian observed, “Where you can have competition, I do not think you need a specialist regulator”. He added, however, that each of the basic utilities has a monopoly area and in this context he said, “I think it is sensible to have a specialist regulator, partly of course because a large amount of investment is required in that area and you need the knowledge to do it”.

Sir Ian recognised that one could follow the American (and Australian) example, and set up a general regulatory commission. He pointed out, nonetheless, that such a commission would inevitably have an office of water, and an office of telecoms and an office of energy – “so you can skin the rabbit in various ways”. But the point here is that there would be less of a tendency for regulatory creep with one single competition authority (particularly if there was a cap on total numbers and budget, thereby necessitating clear priorities to be set) than with the current range of economic regulators, and their offspring, the consumer bodies. On the other hand, we have witnessed the diseconomies of scale, so that a super-regulator is a bad idea. It would be better

110 This conclusion is the precise opposite of the view held by the current regulator, Philip Fletcher, who believes that there should be a separate consumer representative body, see his evidence to the Lords Constitution Select Committee, 11 June 2003, para 566.

111 In evidence to the Lords Constitution Committee, Mr Fletcher commented, “I think we have a very effective system (of regulation) with proper clarification of roles”, ibid, para 563.

112 Significantly, the Water Industry Commissioner for Scotland estimates that Scottish water and sewerage bills in 2001/2 were 60 per cent higher than would have been needed if the three former
either to stay with small sectoral regulators or have a small Fair Trading Authority that only operates at high level.

**POSTCOMM**

The need for a separate regulator is only justified while there is a dominant supplier of mail services. Once competition has become established, presently targeted for 2008, access agreements to the Royal Mail’s network may need to arbitrated where allegations of unfair practice arise, but this role could be fulfilled by a general competition authority and through the courts. When British Airways was by far the dominant UK air carrier, smaller companies such as Virgin were protected by such means. There should no longer be a need for a separate sector specific regulator.\(^{113}\)

This is a point recognised by POSTCOMM’s chairman, Graham Corbett. In evidence to the Lords Constitution Committee he observed, “If indeed there were no non-economic criteria, one could almost say, subject to the provisions of the Competition Act, “Why do we need a regulator? Just let the Competition Act take over”. \(^{114}\)

POSTCOMM’s non-economic duties, primarily centred on furthering the interests of disadvantaged customers such as the elderly or the disabled, could, as noted above, be negotiated by local government. The maintenance of rural post offices, for example, could be addressed through offering subsidies channelled through local authorities. The maintenance of a universal service could be safeguarded by specific subsidies to remote parts of the UK, such as the Highlands and Islands.

This still leaves the issue of POSTCOMM’s budget and staffing arrangements, while it focuses on opening up the postal market to competition. What should be done to improve its own efficiency? Under the Postal Services Act, the regulator is funded by the fees it charges to licensed operators – the licence fee increases with the volume of mail handled. Businesses users post 86 per cent of all mail in the UK.\(^{115}\)

---

\(^{113}\) Scottish water authorities had been operated as efficiently as privatised English and Welsh counterparts. Source: Memorandum of evidence by OFWAT to the House of Lords Select Constitution Committee, March 2003, para 15.


\(^{115}\) Source: POSTCOMM annual report 2002/3, p.16.
As highlighted in the previous section, POSTCOMM's budget has almost doubled in four years (an increase of 92 per cent since it was first established in 2000). It currently operates on a budget of £7m a year and employs approximately 40 staff.\footnote{Since it was established in 2000, the DTI has given the regulator the additional responsibility of advising the government on the network of public post offices, specifically the development of the rural and inner city networks.}

There may well be some scope for trimming POSTCOMM's annual budget, which exceeded the target set by Parliament in 2002/3. POSTCOMM’s accounts are likely to be qualified for a second successive time by the external auditor, the Comptroller & Auditor General. This record signals that financial control may be poor: the regulator had not anticipated a rates demand on its headquarters building and it has spent more than anticipated on external legal advice and consultants’ fees following a series of disputes with the Royal Mail.

The picture that emerges is one where POSTCOMM’s staff are not necessarily on top of their brief. While the regulator is relatively small, it has increased significantly in size since it was first established. It has also had to spend considerable sums on outside advice in its dealings with the Post Office (spending on consultancy and legal fees at over £2m a year, outstripped staff costs in 2001/2 and is likely to be almost as high in 2003/4, according to forecasts).

Based on its performance to date, it is not at all clear what POSTWATCH contributes in return for its annual budget of £10 m.\footnote{PostWatch’s Forward Work Programme states projections for its overall budget for the next three years. The figure for 2003/4 has already been exceeded. The latest estimate for the year ending March 2004 is £9,904,873.} More to the point, as the postal markets is opened up to competition, there should no longer be any need for such a body, as both business and individual consumers can choose between rival postal services.

**ORR and Strategic Rail Authority**

Network Rail, the state-owned infrastructure provider, should be broken into regional chunks that can be married with regional train franchises, such as Virgin Rail and GNER. At the boundaries this would require retuning to match territories as well as a protocol for using each others’ lines where overlap cannot be avoided. The train companies have a much greater incentive than anyone else to ensure that track and signalling is working efficiently. They also have an incentive to ensure that investment programmes are effectively implemented, given an appropriate franchise period. While regulation will need to continue, it should be much less intrusive. Furthermore, if infrastructure is integrated back into the rail franchise network, the regulator’s current role as a promoter of efficient working relationships between industry players will be far less onerous. Indeed, economists in the tradition of Professor Ronald Coase\footnote{Nobel Prize Laureate 1991, Emeritus Professor of Economics at the University of Chicago.} would
argue that, left to themselves, the rail operators could establish a perfectly satisfactory market solution to a national rail time-table (as happened in the 19th century).

Currently, the ORR’s budget in 2003/4 is expected to be 13 percent higher than 2002/3 while consultancy costs are forecast to account for around 30 percent of the overall budget. But the rail regulator should be able to function on an annual budget of £10m – slightly less than what it spent in 2001/2, and £2m more than it spent in money terms in 1996/7.

The rail industry needs to be managed by industry professionals, rather than regulators. For all intents and purposes, the managers of the rail infrastructure threw up the towel when Railtrack was re-nationalised in 2002, at the behest of Stephen Byers and the Department of Transport. Political and regulatory intervention has been seen not to work in the rail industry.

The fresh look announced by the Secretary of State for Transport in January 2004 will hopefully clarify the roles government should retain, devolve to an independent regulator (if such a role exists) and devolve to the train operating companies with their non-executive passenger advisory groups acting as part of their market research. Clearly the government should itself determine the total amount of rail subsidy and the criteria for allocation. Equally clearly, the re-nationalised infrastructure does not need a regulator since the whole point of regulators is to monitor privatised industries. Allowed to operate freely, market mechanisms would deliver a more efficient railway service that delivered greater passenger benefit. The corollary is that it must expect to receive less in taxpayer subsidy.119 Since rail subsidies can be used to police good competitive behaviour by the private companies, then, whether the infrastructure is parcelled out to the train operators or not, it would seem that no role need remain for the SRA or the ORR.

Section Seven: Potential increase in taxpayer value

This paper has reviewed the record of regulation in the UK over the last twenty years. There are many aspects of this regulatory performance to be commended. Regulators have often been at the forefront of introducing competition into a sector of the economy that was dominated by a privatised monopoly. Through their efforts, consumers in the telecoms, gas, electricity and water industries have reaped a range of benefits in terms of price, quality and choice as new players have entered the market.

However, in the last few years there has been a noticeable step change in the growth of regulation. This has been prompted by a wave of legislation since Labour assumed office in May 1997. Typically, this legislation has conferred a raft of additional non-economic objectives, often

119 Prof David Newberry at the Dept of Applied Economics, Cambridge, has undertaken considerable cost-benefit analysis which indicates that rail subsidies provide very poor value for money, even from an environmental viewpoint.
dealing with social and environmental issues, on top of the strictly economic goals set for regulators previously. Underpinning this trend has been a tendency for the government to use regulatory agencies as a non-democratic surrogate for the achievement of a list of political objectives, which often run counter to regulators’ economic goals (For example, the energy regulator is required to encourage renewable forms of energy, but these are often located in remote parts of the country, and little has been explained as to who should bear the cost of transmitting such power to urban areas).

This paper has examined the case for restricting regulation to economic issues, as a proxy for a fully competitive market. This would leave politicians to address social and environmental issues, through central or local government initiatives. Hence, rural post offices providing what are considered essential services might compete for subsidies from local authorities. And television production companies producing merit good programmes, such as arts programming developed by Melvyn Bragg’s South Bank Show unit at LWT, might compete for subsidy provided through the licence fee.

Regulation cannot be scrapped overnight, particularly in sectors of the economy, such as water and the local telephone and postal ‘loop’, where natural monopolies still exist. On the other hand, the growth exhibited by regulators - across the spectrum – over the last five years could be trimmed and the number of staff drastically reduced. These resources and talented staff could be redeployed elsewhere in the economy to much greater effect, thereby augmenting total GDP.

In the case of OFTEL, however, it could be argued that it would have been close to being phased out if it had not been captured, and therefore preserved, by OFCOM. The mobile market is competitive with four strong companies and arrangements for the surviving monopoly areas close to resolution. The taxpayer would have been better off if OFTEL had been preserved with a proximal sunset date rather than merged with OFCOM.

In the previous section, recommendations were made as to how regulators could be slimmed down in the shorter run. This would require amendments to legislation since it is argued that a number of the non-economic roles currently performed by regulators are either superfluous or better achieved through other means. Table 6 draws together the recommended figures set out in section six and summarises how much budgeted expenditure could be saved, compared with the budgeted totals for 2002/3 (In the case of OFCOM, its estimated total expenditure in its first year, 2004, has been included). This is based on the less radical alternative although the OFT and Competition Commission are still shown as being merged.

As noted elsewhere, we do not regard that as fully practical although there is room to streamline the two bodies and identify the Competition Commission more closely with the courts if it is truly, as some believe, a quasi-court whereas the OFT is, so to speak, the “Crown Prosecution Service” so to speak. The figures would not be significantly changed from those in Table 6 which therefore remain.
Table 6: Summary of potential increase in taxpayer value – Budget and Manpower

<table>
<thead>
<tr>
<th>Regulatory Agency</th>
<th>2002/3</th>
<th>Proposed Budget £M</th>
<th>2002/3</th>
<th>Proposed Headcount</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Budget £M</td>
<td>Headcount</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Competition Commission</td>
<td>16.3</td>
<td>155</td>
<td>50</td>
<td></td>
</tr>
<tr>
<td>OFT</td>
<td>54.2</td>
<td>631</td>
<td></td>
<td></td>
</tr>
<tr>
<td>FSA</td>
<td>221</td>
<td>2,313</td>
<td>1,000</td>
<td></td>
</tr>
<tr>
<td>OFCOM*</td>
<td>164</td>
<td>880</td>
<td>390</td>
<td></td>
</tr>
<tr>
<td>OFGEM</td>
<td>38.5</td>
<td>320</td>
<td>100</td>
<td></td>
</tr>
<tr>
<td>OFWAT</td>
<td>10.8</td>
<td>233</td>
<td>200</td>
<td></td>
</tr>
<tr>
<td>POSTCOMM</td>
<td>6.5</td>
<td>40</td>
<td>-40</td>
<td></td>
</tr>
<tr>
<td>ORR</td>
<td>13.3</td>
<td>124</td>
<td>100</td>
<td></td>
</tr>
<tr>
<td>TOTAL</td>
<td>524.6</td>
<td>4,696</td>
<td>-2,330</td>
<td></td>
</tr>
</tbody>
</table>

* OFCOM figures relate to estimates for the year 2004.

We now review the less and more radical alternatives before reverting to the question of taxpayer benefits from the offices of the regulators.

**Alternative 1: Sectoral Economic Regulators Continue as Separate Bodies**

The FSA has grown into an unwieldy and expensive leviathan. It is recommended that this agency’s budget should be capped at £100m a year (in 2004 money terms) with a maximum headcount of 1,000. This still far outstrips the budget of regulation in the financial services in the mid 1990s, although it does incorporate functions previously performed by the Bank of England.

This paper argues that many of the statutory roles conferred on OFCOM are unnecessary. It advocates a much slimmer agency, excluding the functions performed to date by the Radiocommunications Agency (a heavy spender and – in regulatory terms – a major employer). The previous section suggested and OFCOM budget of £50m a year and with a total staff headcount of 390. Including the Radiocommunications Agency would increase the numbers to £100M and headcount of 600.

The energy regulator, OFGEM, is beginning to scale down its budget and headcount, partly on account of the fact that it is now required to regulate much less. Yet more could be done to trim costs. OFGEM should focus on the remaining areas of natural monopoly – no more, no less.
Alternative 1 would reduce the annual budget to £10m and scale back headcount to 100. As suggested earlier, a sunset clause should be used to ensure regulators do phase out as planned or at least their position is re-considered after a finite interval.

OFCWAT is probably the most efficient economic regulator. This is not unconnected with the fact that it is based outside London. There is no particular reason why regulatory agencies should be located in London, indeed, it might well help if their staff were outside the Whitehall, Westminster and City villages\(^{120}\). OFFER, the electricity regulator, ran perfectly satisfactorily when it was based in Birmingham, as does OFCwat. What is more, it seems strange that a government so committed to regional development should concentrate such a wealth of economists, lawyers and other professionals in London, further adding to the over-heating of the region.

Under alternative 1 a modest cut-back is envisaged in OFCwat’s budget and headcount, which has recently been on the increase because of the additional statutory duties conferred by the Water Act 2003. Many of these obligations are entirely unnecessary or unwise. In particular, the HQ office and regional network of WATEROICE should be scrapped as superfluous. Competition in the water industry should be encouraged wherever possible; consumer councils should be discouraged as their function should properly be performed by the regulator.

Alternative 1 proposes that POSTCOMM and its sister consumer body POSTWATCH should be viewed as temporary organizations with a budget of £4m and headcount of 40 until a sunset date in 2008.

The first alternative proposes that the ORR’s budget should be set at of £10m – slightly less than what it spent in 2001/2, and £2m more than it spent in money terms in 1996/7. In terms of headcount, the ORR’s staff should be capped at 100, the same number that it employed in 2000/1.

Looking further ahead, the aim should be to integrate the regulation of the rail industry within a Fair Trading Authority but perhaps including a few specialist railway experts. This would present greater career choice to regulatory staff and act as an effective cap on regulators’ tendency to expand their empires. Competition issues as they relate to the rail sector could be deal with under the powers of the 1998 Competition Act and, as recommended by Irwin Stelzer, greater use of the courts could be made in order to establish regulatory certainty, less tainted by the risk of political interference.

Finally, some savings could be made by ensuring all these offices were outside the premium cost area of London and the South East and the government should re-affirm the independence of

\(^{120}\) California established its energy regulator in San Francisco specifically because the city was hundreds of miles from the state capital, Sacramento, the home of politicians, officials and lobbyists.
economic regulators by publicizing the non-economic interventions they intend to retain for Whitehall departments.

Although Table 6 shows, the potential increase in Taxpayer Value to be derived from Alternative 1 is in the order of £300m (down from the 2002/3 total of £525m to £224m – 2003/4 will of course be higher than 2002/3), and the number of regulators would be more than halved from 2003/4, i.e. from 4,696 to 2,330, these figures must be adjusted for the fact that the FSA is directly funded by the industry. Thus the saving is £179m.

However, we should also take account of the reduced compliance and indirect costs for the private sector. Adding back the FSA saving and matching the public/private costs, on the assumption that the public/private interaction probably means that £1 on cost on one side incurs £1 on the other. No doubt better estimates can be researched but for this purpose we have £300M compliance saving for the private sector with perhaps the same again for indirect costs, such as from innovation and lessened distraction.

The Chancellor’s tax cut of this £600m would be about £150m so the gain for Taxpayer Value from this alternative would be £329m

It is worth noting in this context that, according to David Willetts, the 1975 13% payroll cost of company pensions has now soared to 28.5% of which 8% is due to regulation and compliance costs.121

**Alternative 2: A Single Fair Trading Authority**

Alternative 2 would produce greater savings but not the entire amount as some specialist costs would remain within the FTA and some of the FSA and OFCOM roles would also be maintained. Even so, following the same logic as above alternative 2 would release £494m in 2002/3 figures with more in future years.

Whilst there are financial and ideological attractions in alternative 2, its immediate practicality is open to challenge. We have seen the diseconomies of scale in the regulatory offices and there is much to be said for smaller units working closely with their sectors. We suggest that alternative 2 remains a long-term goal but alternative 1 (minimizing small, specialist sectoral economic regulators) would be the better route.

In order to implement either alternative 1 or 2, a new parliamentary bill would be required in order to (dependent on which option was preferred):

- merge the Competition Commission and the OFT to form the Fair Trading Authority.

---

- clarify the involvement of the courts and the judicial/appellate system.
- remove the concurrent powers of a group of economic regulators, namely OFCOM, OFGEM, OFWAT, POSTCOMM and the ORR, in favour of the proposed new competition body, the Fair Trading Authority.
- abolish the non-economic objectives set for economic regulators, particularly those new statutory responsibilities established since May 1997.
- close down, or introduce sunset clauses for, OFGEM, OFWAT, POSTCOMM, ORR and SRA.
- transform the various consumer bodies set up since May 1997 to advisory groups for the companies, including OFCOM’s Consumer Panel, ENERGYWATCH, POSTWATCH, the various rail consumer bodies and WATERVOICE.
- require businesses with greater than 40 percent market share in the previously regulated sectors to provide marketing metrics, e.g. customer satisfaction, as recommended by the Accounting Standards Board.
- streamline the FSA as outlined above.

Benefits from the offices of regulators

A monopoly is not necessarily bad for the consumer: it depends on how the monopoly behaves and what alternatives the consumer may have. Looking back it seems strange that inefficient monopolies were tolerated because they were owned by the state whereas relatively efficient companies with marginal monopolies cannot be trusted when they are private. OFTEL is a case in point. The telephone user was receiving far worse value in 1980 than in 2004 so why did we not need OFTEL in 1980 but do need a regulator today?

It was not until late in drafting this paper that the absurdity dawned that the UK has large and growing offices of regulators without anyone asking to see the benefits, net or gross, quantified or verbal. There is almost a sense that the private sector, or profit, is an Aunt Sally and that citizens through tiers of offices of regulators and consumerist groups should be encouraged to pelt it with any restrictions that come to hand. Reality is the reverse: profits and the private sector provide the taxes on which the whole regulatory structure, and public sector, depend.

This paper cannot balance this one-sided review of costs because the regulators do not provide data on the benefits. It would be healthy if they did. Lord Currie\textsuperscript{122} has suggested that technological development will be one benefit derived from regulation but, as Tellis and Goulder

\textsuperscript{122} As part of a question put to the FSA Chief Executive at the IEA/Cass Business School seminar, 3\textsuperscript{rd} March 2004.
have shown, regulation stifles both technical and market innovation. Thus, in this respect, Lord Currie’s perceived benefit from regulation is negative. It is understood that the Competition Commission has conducted some work on this area but until the data can be debated in the public arena, we can only conclude that taxpayer value will increase from less, rather than more, regulation.

The Regulatory Impact Assessments (RIAs) introduced for new regulation affecting business and other interests could provide a useful precedent. It may not be practical, as the BRTF suggested, to use RIAs for individual decisions by regulators but it should be possible to use the format for an annual appraisal of the costs and benefits of each regulatory office as part of its planning process. Declining benefits should be rewarded by declining budgets.

Consideration of benefits prompts a fundamental review of how the roles of the offices of the regulators have changed. OFTEL was created to liberate its market and then leave the stage. Today the regulators, notably the FSA, no longer have the development of competitive markets as their primary goal. They see themselves as police forces, if not gaolers, with permanent responsibilities to protect consumers and pursue the interests of government.

This is a serious shift of orientation and almost certainly negative for GDP. One might wonder if the regulators have forgotten that free market business profits provide the wealth and the taxes for the country as a whole.

Reverting to sector regulators, even with smaller budgets, would not achieve the re-orientation required to drive towards wealth creation. By contrast, a single Fair Trading Authority, as distinct from a super-regulator, could intervene only in cases of uncompetitive or unfair practices. Near-monopolies would still need to obtain approval for prices until their markets are competitive but that should be the dominant objective.

In conclusion, we ask whether the way regulators are now evolving is in the best interest of the citizens, or taxpayers. They should not be viewed in isolation but as a superstructure on top of the rapidly increasing level of regulation being applied to all business. Moreover, the costs of the regulators themselves are likely to be a small proportion of the costs to the UK economy when direct and indirect costs to business and the consumer, through reduced innovation, are taken into account. This paper has reviewed two alternatives and no doubt there are others. More important is to recognise that further expansion of the present UK regulatory system is not inevitable.

---

OFACOM’s Statutory Duties

This list is the 263 separate functions mandated by the Communications Act 2003.

<table>
<thead>
<tr>
<th>Section</th>
<th>Duty</th>
<th>Comments</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Office of Communications Act 2002</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>2</td>
<td>Initial function</td>
<td>1 (ss1) + 4(para 8, 11, 12 &amp; 16 Sch)</td>
<td>5</td>
</tr>
<tr>
<td><strong>Communications Act 2003</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>3</td>
<td>Further interests of consumers &amp; citizens</td>
<td>2 + 8 (ss 3) + 1 (ss 5) + 1 (ss 8)</td>
<td>12</td>
</tr>
<tr>
<td>4</td>
<td>Duty to meet 6 Community requirements</td>
<td></td>
<td>6</td>
</tr>
<tr>
<td>5</td>
<td>Network /spectrum directions</td>
<td>1 (ss2)</td>
<td>1</td>
</tr>
<tr>
<td>6</td>
<td>To keep regulatory burdens under review</td>
<td>1 (ss 1) + 1 (ss 2) + 1 (ss4) + 1 (ss7)</td>
<td>4</td>
</tr>
<tr>
<td>7</td>
<td>To carry out impact assessment</td>
<td>Sfs</td>
<td>1</td>
</tr>
<tr>
<td>8</td>
<td>To publish / meet promptness standards</td>
<td>1(ss1) + 1 (ss4)</td>
<td>2</td>
</tr>
<tr>
<td>10</td>
<td>To encourage availability of apparatus</td>
<td>2 (ss1) + 1 (ss2)</td>
<td>3</td>
</tr>
<tr>
<td>11</td>
<td>To promote media literacy</td>
<td>5 (ss1)</td>
<td>5</td>
</tr>
<tr>
<td>12</td>
<td>To establish / maintain Content Board</td>
<td>1 (ss1)</td>
<td>1</td>
</tr>
<tr>
<td>14</td>
<td>To ascertain public / consumer opinion about comms networks, services etc.</td>
<td>1(ss1) + 1(ss4) + 5(ss6)</td>
<td>7</td>
</tr>
<tr>
<td>15(1)</td>
<td>To publish / take account of research</td>
<td>2(ss1)</td>
<td>2</td>
</tr>
<tr>
<td>16(1)</td>
<td>To establish arrangements to consult consumers.</td>
<td>1 (ss1) + 1 (ss2) + 1 (ss7) + 1 (ss8) + 2 (ss10)</td>
<td>6</td>
</tr>
<tr>
<td>20</td>
<td>International representation</td>
<td>4 (ss1) + 1 (ss3)</td>
<td>5</td>
</tr>
<tr>
<td>21</td>
<td>Broadcasting directions</td>
<td>2 (ss2)</td>
<td>2</td>
</tr>
<tr>
<td>22</td>
<td>Provision of information to S of S</td>
<td>1(ss1)</td>
<td>1</td>
</tr>
<tr>
<td>23</td>
<td>Community information</td>
<td>1(ss2)</td>
<td>1</td>
</tr>
<tr>
<td>25</td>
<td>Training &amp; equal ops</td>
<td>1(ss1) + 1(ss2) + 2(ss3)</td>
<td>4</td>
</tr>
<tr>
<td>32</td>
<td>Duty to consult before making designations</td>
<td>1 (ss1) + 1(ss2)</td>
<td>2</td>
</tr>
<tr>
<td>36</td>
<td>Fixing of charges</td>
<td>1 (ss3)</td>
<td>1</td>
</tr>
<tr>
<td>42</td>
<td>Duty to keep register</td>
<td>1 (ss1) + 4(ss2) + 1 (ss4) + 1 (ss5)</td>
<td>7</td>
</tr>
<tr>
<td>46</td>
<td>Procedure for setting etc. conditions</td>
<td>1 (ss2)</td>
<td>1</td>
</tr>
<tr>
<td>48</td>
<td>Delivery of copies of notifications</td>
<td>4 (ss1) + 3 (ss2) + 2</td>
<td>11</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>---</td>
<td>---</td>
<td>---</td>
<td></td>
</tr>
<tr>
<td>50</td>
<td>Conditions relating to customer interests</td>
<td>1 (ss1) + 3 (ss3)</td>
<td>4</td>
</tr>
<tr>
<td>51</td>
<td>Approval of codes of practice</td>
<td>1 (ss2) + 3 (ss5)</td>
<td>4</td>
</tr>
<tr>
<td>52</td>
<td>Approval of dispute procedures</td>
<td>1 (ss1) + 7 (ss2) + 1 (ss4)</td>
<td>9</td>
</tr>
<tr>
<td>54</td>
<td>National Numbering Plan</td>
<td>1 (ss1) + 1 (ss2) + 1 (ss3)</td>
<td>3</td>
</tr>
<tr>
<td>61</td>
<td>General duty as to numbering</td>
<td>2 (ss1) + 1 (ss2)</td>
<td>3</td>
</tr>
<tr>
<td>73</td>
<td>Conditional access systems</td>
<td>1 (ss1) + 2 (ss2)</td>
<td>3</td>
</tr>
<tr>
<td>75</td>
<td>Privileged supplier conditions</td>
<td>1 (ss1) + 2 (ss7) + 1 (ss8)</td>
<td>4</td>
</tr>
<tr>
<td>77</td>
<td>Market power determinations</td>
<td>2 (ss1) + 2 (ss2) + 2 (ss3)</td>
<td>6</td>
</tr>
<tr>
<td>78</td>
<td>Proposals for identifying markets</td>
<td>2 (ss1) + 4 (ss2) + 1 (ss4) + 1 (ss5)</td>
<td>8</td>
</tr>
<tr>
<td>81</td>
<td>Transnational markets</td>
<td>2 (ss2)</td>
<td>2</td>
</tr>
<tr>
<td>82</td>
<td>Review of services markets</td>
<td>2 (ss2) + 1 (ss3) + 1 (ss4)</td>
<td>3</td>
</tr>
<tr>
<td>83</td>
<td>Review of apparatus markets</td>
<td>2 (ss2) + 1 (ss6)</td>
<td>3</td>
</tr>
<tr>
<td>106</td>
<td>Register of persons</td>
<td>1 (ss1) + 1 (ss2) + 1 (ss4) + 1 (ss6)</td>
<td>4</td>
</tr>
<tr>
<td>143</td>
<td>Statement of policy on information gathering</td>
<td>2 (ss1) + 1 (ss3) + 1 (ss4)</td>
<td>3</td>
</tr>
<tr>
<td>144</td>
<td>Provision of information</td>
<td>4 (ss1) + 1 (ss4)</td>
<td>5</td>
</tr>
<tr>
<td>151</td>
<td>UK Frequency Plan</td>
<td>1 (ss1)</td>
<td>1</td>
</tr>
<tr>
<td>152</td>
<td>Ofcom’s spectrum duties</td>
<td>3 (ss1) + 4 (ss2)</td>
<td>7</td>
</tr>
<tr>
<td>156</td>
<td>Special multiplex duty</td>
<td>1 (ss2)</td>
<td>1</td>
</tr>
<tr>
<td>158</td>
<td>Recognised spectrum access</td>
<td>1 (ss2)</td>
<td>1</td>
</tr>
<tr>
<td>184</td>
<td>Action by Ofcom on disputes</td>
<td>1 (ss2) + 1 (ss4)</td>
<td>2</td>
</tr>
<tr>
<td>186</td>
<td>Procedure for resolving disputes</td>
<td>1 (ss1) + 1 (ss5) + 1 (ss7)</td>
<td>3</td>
</tr>
<tr>
<td>196</td>
<td>Function to regulate BBC</td>
<td>1 (ss1)</td>
<td>1</td>
</tr>
<tr>
<td>201</td>
<td>Function to regulate Welsh Authority</td>
<td>1</td>
<td>1</td>
</tr>
<tr>
<td>207</td>
<td>Gaelic Media Service</td>
<td>1 (ss2) + 1 (ss3) + 2 (ss6) + 4 (ss7)</td>
<td>11</td>
</tr>
<tr>
<td>209</td>
<td>Regulation of independent TV</td>
<td>5 (ss2) + 2 (ss3)</td>
<td>7</td>
</tr>
<tr>
<td>213</td>
<td>Replace C3 / C5 licences</td>
<td>2 (ss1)</td>
<td>2</td>
</tr>
<tr>
<td>216</td>
<td>Duty to secure teletext</td>
<td>1 (ss1)</td>
<td>1</td>
</tr>
<tr>
<td>219</td>
<td>Replacement teletext licence</td>
<td>1 (ss1)</td>
<td>1</td>
</tr>
<tr>
<td>227</td>
<td>Report in advance of new licensing round</td>
<td>1 (ss1)</td>
<td>1</td>
</tr>
<tr>
<td>229</td>
<td>Replacement of C4 licence</td>
<td>1 (ss3)</td>
<td>1</td>
</tr>
<tr>
<td>243</td>
<td>Regulation of independent radio</td>
<td>6 (ss2)</td>
<td>6</td>
</tr>
<tr>
<td>251</td>
<td>Extension of licences</td>
<td>1 (ss6)</td>
<td>1</td>
</tr>
<tr>
<td>261</td>
<td>Application of regulatory regimes</td>
<td>1 (ss1) + 1 (ss2)</td>
<td>2</td>
</tr>
<tr>
<td>262</td>
<td>Ofcom reports on PS remit</td>
<td>1 (ss1)</td>
<td>1</td>
</tr>
<tr>
<td>264</td>
<td>Statements of programme policy</td>
<td>1 (ss5) + 1 (ss6)</td>
<td>2</td>
</tr>
<tr>
<td>265</td>
<td>Changes of programme policy</td>
<td>1 (ss6)</td>
<td>1</td>
</tr>
<tr>
<td>Page</td>
<td>Section Description</td>
<td>Sections</td>
<td>Notes</td>
</tr>
<tr>
<td>------</td>
<td>-------------------------------------------</td>
<td>----------</td>
<td>-------</td>
</tr>
<tr>
<td>266</td>
<td>Statements of service policy</td>
<td>1(ss6) + 1(ss7)</td>
<td>2</td>
</tr>
<tr>
<td>267</td>
<td>Changes of service policy</td>
<td>1(ss6)</td>
<td>1</td>
</tr>
<tr>
<td>275</td>
<td>Independent quotas</td>
<td>1(ss1)</td>
<td>1</td>
</tr>
<tr>
<td>276</td>
<td>Original quotas</td>
<td>2(ss1)</td>
<td>2</td>
</tr>
<tr>
<td>277</td>
<td>News &amp; current affairs</td>
<td>3(ss1) + 2(ss2) + 2(ss3)</td>
<td>7</td>
</tr>
<tr>
<td>278</td>
<td>News providers for C3</td>
<td>1</td>
<td>1</td>
</tr>
<tr>
<td>281</td>
<td>News provision on teletext</td>
<td>1</td>
<td>1</td>
</tr>
<tr>
<td>282</td>
<td>Code on programme commissioning</td>
<td>1</td>
<td>1</td>
</tr>
<tr>
<td>283</td>
<td>Regional programme-making C3 / C5</td>
<td>4(s1) + 4(s3)</td>
<td>8</td>
</tr>
<tr>
<td>284</td>
<td>Regional programming</td>
<td>5(s1)</td>
<td>5</td>
</tr>
<tr>
<td>285</td>
<td>Regional programme-making C4</td>
<td>4(s1)</td>
<td>4</td>
</tr>
<tr>
<td>286</td>
<td>Regional teletext</td>
<td>2 (ss2)</td>
<td>2</td>
</tr>
<tr>
<td>288</td>
<td>Networking arrangements</td>
<td>1(ss1)</td>
<td>1</td>
</tr>
<tr>
<td>290</td>
<td>Review of networking arrangements</td>
<td>1(ss1)</td>
<td>1</td>
</tr>
<tr>
<td>292</td>
<td>C4 programme-making</td>
<td>1(ss1)</td>
<td>1</td>
</tr>
<tr>
<td>293</td>
<td>Schools programming</td>
<td>1(ss1)</td>
<td>1</td>
</tr>
<tr>
<td>294</td>
<td>National television archive</td>
<td>2(ss2)</td>
<td>2</td>
</tr>
<tr>
<td>295</td>
<td>Teletext interference</td>
<td>1(ss1)</td>
<td>1</td>
</tr>
<tr>
<td>300</td>
<td>Deaf / visually impaired</td>
<td>1</td>
<td>1</td>
</tr>
<tr>
<td>301</td>
<td>Procedure for code</td>
<td>1(ss1)</td>
<td>1</td>
</tr>
<tr>
<td>304</td>
<td>Observance of code</td>
<td>1(ss1)</td>
<td>1</td>
</tr>
<tr>
<td>305</td>
<td>DPS independent quotas</td>
<td>1(ss1)</td>
<td>1</td>
</tr>
<tr>
<td>306</td>
<td>EPG code</td>
<td>1(ss1)</td>
<td>1</td>
</tr>
<tr>
<td>307</td>
<td>Conditions to comply with code</td>
<td>1(ss1)</td>
<td>1</td>
</tr>
<tr>
<td>310</td>
<td>Localness guidance</td>
<td>2(ss2) + 1(ss5) + 1(ss6)</td>
<td>4</td>
</tr>
<tr>
<td>312</td>
<td>Competition code</td>
<td>1(ss1)</td>
<td>1</td>
</tr>
<tr>
<td>314</td>
<td>Review of competition powers</td>
<td>1(ss1)</td>
<td>1</td>
</tr>
<tr>
<td>315</td>
<td>Ofcom standards code</td>
<td>1(1)</td>
<td>1</td>
</tr>
<tr>
<td>318</td>
<td>Supplementary advertising powers</td>
<td>1(ss1)</td>
<td>1</td>
</tr>
<tr>
<td>320</td>
<td>Setting of standards</td>
<td>1(ss1)</td>
<td>1</td>
</tr>
<tr>
<td>321</td>
<td>Observance of standards code</td>
<td>1(ss1) + 1(ss2)</td>
<td>2</td>
</tr>
<tr>
<td>322</td>
<td>Fairness code</td>
<td>1(ss1)</td>
<td>1</td>
</tr>
<tr>
<td>324</td>
<td>Duty to publicise Ofcom’s functions</td>
<td>1(ss1)</td>
<td>1</td>
</tr>
<tr>
<td>329</td>
<td>Party political broadcasts</td>
<td>1(ss1)</td>
<td>1</td>
</tr>
<tr>
<td>330</td>
<td>Retention of recordings</td>
<td>1(ss1)</td>
<td>1</td>
</tr>
<tr>
<td>331</td>
<td>International obligations</td>
<td>1(ss1)</td>
<td>1</td>
</tr>
<tr>
<td>333</td>
<td>Equal ops &amp; training</td>
<td>1(ss1)</td>
<td>1</td>
</tr>
<tr>
<td>343</td>
<td>Statement of charging principles</td>
<td>1(ss1)</td>
<td>1</td>
</tr>
<tr>
<td>348</td>
<td>Change of control of Channel 3 service</td>
<td>1(ss1)</td>
<td>1</td>
</tr>
<tr>
<td>350</td>
<td>Change of control of Channel 5 service</td>
<td>1(ss1)</td>
<td>1</td>
</tr>
<tr>
<td>352</td>
<td>Change of control of local radio licence</td>
<td>1(ss1)</td>
<td>1</td>
</tr>
<tr>
<td>355</td>
<td>Annual factual and statistical report</td>
<td>1(ss1)</td>
<td>1</td>
</tr>
<tr>
<td>374</td>
<td>Additional investigation</td>
<td>1(ss2) of s.44A</td>
<td>1</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>---</td>
<td>-----------------------------------------</td>
<td>---------------------------------</td>
<td>---</td>
</tr>
<tr>
<td>379</td>
<td>General information duties</td>
<td>1(ss3) + 1(ss4)</td>
<td>2</td>
</tr>
<tr>
<td>382</td>
<td>Other general functions</td>
<td>1</td>
<td>1</td>
</tr>
<tr>
<td>388</td>
<td>Review of media ownership</td>
<td>1(ss1)</td>
<td>1</td>
</tr>
<tr>
<td>389</td>
<td>Statement of penalties</td>
<td>1(ss1)</td>
<td>1</td>
</tr>
<tr>
<td>400</td>
<td>Regulations made by Ofcom</td>
<td>1(ss4)</td>
<td>1</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td></td>
<td></td>
<td>263</td>
</tr>
</tbody>
</table>