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Consultation decision: Review of REMIT Procedural Guidelines and REMIT Penalties Statement

Final decision

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Overview:

Our approach to REMIT enforcement is set out in the REMIT Procedural Guidelines and REMIT Penalties Statement. We reviewed the content of these documents, particularly following changes to the REMIT Regulations and to Ofgem's broader enforcement processes. In December 2014 we consulted on our proposed changes.

We would like to thank the respondents to the consultation for their views. We have considered all the comments made. In this document we summarise and address the key points made. We also outline the resulting changes to the REMIT Procedural Guidelines and REMIT Penalties Statement.

Context

In Great Britain, Ofgem has been given powers to investigate and enforce against breaches of the European Regulation on wholesale energy market integrity and transparency (REMIT). These powers, set out in the Electricity and Gas (Market Integrity and Transparency)(Enforcement Etc.) Regulations 2015, include imposing potentially unlimited fines on persons who breach REMIT. To set our how we will use our powers, we consulted on and then published the REMIT Procedural Guidelines and REMIT Penalties Statement in 2013. In December 2014 we consulted on revisions to these documents to reflect internal and regulatory changes, including the addition of the Electricity and Gas (Market Integrity and Transparency) (Enforcement Etc.) (Amendment) Regulations 2015.[1]

The revised REMIT Procedural Guidelines and REMIT Penalties Statement ensure that market participants and others know what to expect, and what we expect of them, when we investigate and enforce REMIT. This will help us achieve our consumer outcomes through regulation, confidence and efficiency.[2]

Associated documents

Below are links to the following documents:

- EU regulation no 1227/2011 (REMIT): http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:L:2011:326:0001:0016:en:PDF
- The Electricity and Gas (Market Integrity and Transparency) (Enforcement etc.) Regulations 2013: http://www.legislation.gov.uk/uksi/2013/1389/contents/made
- ACER Guidance on the application of REMIT (third edition): http://www.acer.europa.eu/remit/Documents/REMIT%20ACER%20Guidance%203rd%20Edition_FINAL.pdf
- Ofgem's REMIT Procedural Guidance and Penalties Statement: https://www.ofgem.gov.uk/publications-and-updates/consultation-decision-remit-penalties-statement-and-procedural-guidelines

[1] The 2015 Regulations are due to come into force on 1 July 2015.
[2] See our corporate strategy: https://www.ofgem.gov.uk/ofgem-publications/92187/corporatestrategy.pdf.

- Ofgem's Enforcement Guidelines decision document: https://www.ofgem.gov.uk/publications-and-updates/enforcement-guidelines-decision-document
- Ofgem's consultation on the REMIT Procedural Guidelines and Penalties Statement: https://www.ofgem.gov.uk/publications-and-updates/remit-procedural-guidelines-and-penalties-statement-consultation

Contents

Executive Summary

We have specific powers to enforce the prohibitions on insider trading and market manipulation, as set out in the European Regulation on wholesale energy market integrity and transparency (REMIT). We want to ensure that companies and individuals know what to expect and what we expect of them, when we investigate and enforce against REMIT breaches. We also want to incentivise market participants to meet their duties under REMIT by setting out the consequences of failing to comply with REMIT. Our REMIT Procedural Guidelines and REMIT Penalties Statements outline the strong system we have for regulating the way market participants follow the REMIT rules.

Last year we identified a need to update the REMIT Procedural Guidelines and REMIT Penalties Statements. There were four main reasons for this. First, to align our approach in REMIT cases, where possible, with the processes used in our other enforcement cases, which had been amended following our Enforcement Review. Second, to be consistent, where appropriate, with the comparative regime in financial markets for similar offences, given the interlinkages wholesale energy markets have with financial markets. Third, to extend the Statements to cover the new civil powers that will come into effect in July this year in relation to breaches of Article 8 (data reporting) and 9 (registration) of REMIT. And fourth, we wanted to incorporate what we have learnt through using our REMIT monitoring and enforcement powers. We consulted on our proposed changes last December.

Respondents to our consultation broadly agreed with our proposed changes to amend the Statements published in 2013. So we have not made any significant revisions to the core proposals. The key changes are summarised below.

a) In both the REMIT Procedural Guidelines and the REMIT Penalties Statement we have introduced a vision and strategic objectives for REMIT casework.

b) In the REMIT Procedural Guidelines we have changed:
- the processes for conducting settlement discussions,
- the decision-makers, following the introduction of the Enforcement Decision Panel, and
- how oral representations are made.

c) In the REMIT Penalties Statement our changes cover:
- when restitution orders may be appropriate
- the steps we will follow to decide the amount of a penalty, for companies and for individuals. This includes how we will take account of factors such as the potential to cause serious financial hardship, and
- the discounts to a penalty that are available for agreeing settlement and how these decrease over time.

This response document sets out and gives reasons for the smaller changes that we have decided to make. In some cases, stakeholder feedback usefully highlighted areas where we needed to be clearer. We also summarise the main points raised by respondents that have not resulted in changes, giving reasons why they did not.

We are simultaneously publishing the final revised REMIT Procedural Guidelines and REMIT Penalties Statements. These have been approved by the Authority. The revised REMIT Procedural Guidelines will take immediate effect. The REMIT Penalties Statement will apply to any finding in respect of any failure to comply with a REMIT requirement that occurred after the date of this document.

1. Introduction

1.1. In December 2014 we consulted on proposed revisions to our REMIT Procedural Guidelines and REMIT Penalties Statement. The consultation closed in February 2015. We received responses from the following companies:

- National Grid
- SSE
- EDF Energy
- E.On
- Npower
- ScottishPower

1.2. We have considered the consultation responses. In this response document, we set out our position on the key points raised by respondents. All references to paragraphs in the REMIT Procedural Guidelines and the REMIT Penalties Statement are related to the final documents.

1.3. Our final revised REMIT Procedural Guidelines and the revised REMIT Penalties Statement have been published at the same time as this consultation response. As required by the Electricity and Gas (Market Integrity and Transparency)(Enforcement Etc.) Regulations 2013, they take account of responses and also reflect minor amendments for clarification or stylistic reasons.

1.4. The REMIT Procedural Guidelines take immediate effect. The REMIT Penalties Statement will apply to any finding in respect of a failure to comply with a REMIT requirement that occurred on or after this publication date.

2. Vision and Strategic Objectives

Chapter Summary

All respondents agreed with our proposal to incorporate our enforcement Vision and Strategic Objectives into both the REMIT Procedural Guidelines and the REMIT Penalties Statement. We have therefore incorporated them. Respondents had some additional proposals and we explain why we have not made further changes.

Vision for REMIT Enforcement

2.1. We consulted on incorporating our enforcement Vision and Strategic Objectives into the REMIT Procedural Guidelines and Penalties Statement. This Vision, which in the REMIT context applies to individuals as well as companies, is as follows:

To achieve a culture where businesses put energy consumers first and act in line with their obligations.

- Views of respondents

2.2. All of the respondents supported our proposal to incorporate our Enforcement Vision. One respondent commented on the phrase "putting consumers' first." It said that this should be read in the context of the wholesale energy market, where market participants act in their own best interests (in accordance with the legal and regulatory framework) and the resultant competition ensures the best outcomes for consumers.

- Ofgem's response

2.3. *We exist to make a positive difference for energy consumers. One of the main ways we do this is by using regulation and enforcement to make sure that competition in energy markets is effective and works in consumers' interests.*[3] *The*

[3] See our Corporate Strategy: https://www.ofgem.gov.uk/ofgem-publications/92187/corporatestrategy.pdf

goal of REMIT is to increase the integrity and transparency of wholesale energy markets, to foster open and fair competition for the benefit of final consumers of energy. This is the context in which putting consumers first is a key element of our enforcement Vision for REMIT, as well as for our other enforcement activities.

Strategic Objectives for REMIT Enforcement

2.4. We consulted on using the same Strategic Objectives for REMIT as for our other enforcement activities. The Strategic Objectives serve as broadly defined goals that help to convert our Enforcement Vision into more specific plans. They are to: deliver credible deterrence across the range of our functions; ensure visible and meaningful consequences for businesses who fail consumers and who do not comply; and achieve the greatest positive impact by targeting enforcement resources and powers.

- Views of respondents

2.5. All of the respondents supported our proposal to incorporate our enforcement Strategic Objectives. Two respondents suggested changes to the Strategic Objectives to ensure they apply to REMIT appropriately. One noted that Article 18 of REMIT requires National Regulatory Authorities (NRAs) to apply penalties for breaches of REMIT in a proportionate way, and said that this should be made explicit in the Strategic Objectives. Another respondent recommended including an objective to ensure that REMIT is enforced consistently across Europe.

2.6. We were also asked to make clearer the interaction between the Strategic Objectives and the Regulatory Objectives set out in paragraph 2.4 of the REMIT Procedural Guidelines. (These include matters such as maintaining confidence in the integrity of wholesale energy markets and ensuring no profits can be drawn from failures to comply with REMIT requirements.) The respondent was unclear which had primacy.

- Ofgem's response

2.7. *We agree that it is important that Ofgem acts proportionately in actions relating to the enforcement of REMIT. Article 18 of REMIT says that the penalties provided for under the rules implementing REMIT in each Member State must be "effective, dissuasive and proportionate". We have designed our REMIT Procedural Guidelines and REMIT Penalties Statement to meet the requirements of REMIT. They*

explain that, in addition to the Strategic Objectives, the Authority will have regard to other Regulatory Objectives. These include the principles of best regulatory practice, including the need to be proportionate and to ensure that any sanctions we impose are effective, dissuasive and proportionate.[4] *As the need to be proportionate is set out here, we do not consider it appropriate to duplicate it in our Strategic Objectives.*

2.8. *We considered the view raised that it is appropriate to include a strategic objective relating to the consistent enforcement of REMIT across Europe. REMIT provides a consistent EU-wide regulatory framework that, amongst other things, defines and prohibits market abuse in wholesale energy markets across Europe. We recognise and support the need for NRAs across Europe to apply that framework in a consistent way. We will continue to engage with the Agency for the Co-operation of Energy Regulators (ACER) and with other European NRAs to achieve this, and to detect and investigate cross-border market abuse.*

2.9. *But, while we recognise the importance of consistency and actively work to help achieve this, Ofgem is not and cannot be responsible for ensuring that REMIT is enforced consistently across Europe. This is for two reasons. First, under Article 16 of REMIT, ACER has a duty to aim to ensure that NRAs carry out their tasks under REMIT in a co-ordinated and consistent way. Second, each NRA will apply its REMIT powers in accordance with its own national legal and regulatory framework. We will therefore not be including the proposed objective to ensure that REMIT is enforced consistently across Europe.*

2.10. *In response to the question about the interaction between the Strategic Objectives and the Regulatory Objectives, we noted above that the Strategic Objectives help to convert our Enforcement Vision into more specific plans across Ofgem's enforcement activities. The Regulatory Objectives for REMIT provide greater elaboration of these plans for REMIT enforcement. In this way, the Strategic Objectives can be thought of as a subset of the Regulatory Objectives. We have made some minor textual changes to emphasise the primacy of the Regulatory Objectives.*

[4] See paragraph 2.5 in the REMIT Procedural Guidelines and paragraph 2.8 in the REMIT Penalties Statement.

3. REMIT Procedural Guidelines

Chapter Summary

All respondents agreed with our proposals to introduce set settlement windows with discounts that decrease the closer the matter gets to conclusion. We answer some additional questions that were raised about the details of this. We are also confirming our proposed change to the stage at which the subject of an investigation may request an oral hearing. Finally, we note our responses to some general comments on our procedures.

Settlement Processes

3.1. One outcome of the Enforcement Review was the creation of a process for settlement discussions that incorporated three discount windows with clearly defined opening and closing points (Early, Middle and Late Settlement Windows), with discounts that decrease the closer the case comes to conclusion. We proposed broadly following the same approach in REMIT cases.

- Views of respondents

3.2. One respondent considered that there should be an option of settlement without having to admit to a breach of a REMIT requirement. It said that a market participant might make a commercial decision to settle without accepting it had done wrong. The same respondent said that where settlement was achieved, the person concerned should be 'invited' rather than 'expected' to sign a settlement agreement.

3.3. Several respondents asked for guidance on the circumstances in which we might decline to enter into settlement discussions. One respondent also sought clarification around the circumstances in which a Senior Partner may take a decision to agree settlement rather than a Settlement Committee. The Procedural guidelines specify two circumstances where this can take place. The first is where the value of the resultant penalty is under £100,000 and the second is where the issues raised are unlikely to attract significant industry or media interest or are otherwise uncontentious. The respondent was concerned that there not be sufficient clarity over the value of the penalty at the point at which the Senior Partner is given responsibility for taking a settlement decision to determine whether the £100k threshold is met. The respondent was also concerned that whether an issue is contentious was by nature subjective.

3.4. One respondent considered that the length of the Early Settlement Window was too short, at 28 days, to reach an agreement on the nature and scope of any failures to comply with REMIT requirements. They asked us to change this to "a reasonable period". The same respondent also considered the length of the Middle Settlement Window, at 14 days, to be too short. They were also concerned that the settlement discounts proposed were too low to incentivise early settlement.

- Ofgem's response

3.5. *We have decided not to amend the REMIT Procedural Guidelines to include the option of settlement without admission of failing to comply with a REMIT requirement. This retains consistency with our processes in non-REMIT cases. Settlement in the regulatory context is not the same as settlement in a commercial dispute. Under the discount scheme we are adopting, persons who admit failing to comply with a REMIT requirement are treated more leniently. The biggest discounts are for those cases in which agreement can be reached swiftly thereby producing the greatest saving to the public purse.*

3.6. *In response to the proposal that a person should be 'invited' rather than 'expected' to sign a settlement agreement, we refer to paragraph 10.5 in the Procedures. This highlights that Settlement is a voluntary process. There is no obligation on persons to enter into settlement discussions or to settle. Any decision to settle should be based on a full awareness of the requirements of settlement and the consequences of settling, including that a finding of breach will occur. For this reason, we are retaining the wording that makes clear what our expectations in this process will be.*

3.7. *We do not intend to issue further guidance on the circumstances in which we might decline to enter into settlement discussions at this time. We may consider this again once we have concluded more investigations under our REMIT powers. Until then, the decision whether to initiate settlement discussions will be considered on the circumstances of the investigation. While taking this decision we will be bound by the requirements on us to act reasonably and proportionately.*

3.8. *On the concerns about whether the penalty value will be known at the time the decision is delegated to a Senior Partner, we can clarify that, if settlement discussions begin before a Warning Notice is issued (ie, in the Early, or potentially the Middle, Settlement Window), we will work out an appropriate penalty value. This will be necessary to aid our decision whether to enter into settlement discussions. In relation to the second circumstance, in which a Senior Partner may take a decision to agree settlement, we do not share the concern that it may be too subjective. We note that we will be considering the decision about whether we believe the situation to be non-controversial while bound by the requirements on us to act reasonably and proportionately.*

3.9. *In respect of the comments raised regarding the length of the Early Settlement Windows, we have not changed the timescales set out for the settlement process, or the discounts on offer. This new settlement process is designed to deliver procedural efficiencies and savings of time and resource. The biggest discount on a penalty is available for those cases where matters can be resolved within a set period of 28 days, which we consider reasonable. (This timetable has proved sufficient in all non-REMIT enforcement cases to date.) The next biggest discount is reserved for those cases resolved during the next set period, which we also consider to be reasonable.*

3.10. *We would like to clarify that the Middle Settlement Window is not 14 days by default. This Window opens when the Early Settlement Window closes. It closes when the period for making representations on a Warning Notice expires. So if the Early Settlement Window opens relatively early in an investigation, and then closes 28 days later, there could be a significant period of time until a Warning Notice is issued.*

3.11. *We consider that the proposed changes will improve the settlement process, giving persons greater certainty and transparency of the process, and help us to achieve our aims in terms of efficiency and impact.*

Oral representations

3.12. Persons facing enforcement action for failing to comply with a REMIT requirement have the right to a hearing in front of the Panel of EDP members in their case. Under the GB Enforcement Regulations, they have this right upon receipt of a Warning Notice. We had also introduced the opportunity for oral representations to be made at an earlier stage, when a Statement of Case (now an Issues Letter) is issued. We proposed making this early opportunity discretionary: the EDP Panel may, at their discretion, agree to a request for an early hearing.

- Views of respondents

3.13. None of the respondents objected to this change. One respondent raised two related points. First, it asked for further guidance on how hearings would work in practice. Secondly, it thought it unreasonable to prevent parties introducing new material at a hearing. The respondent said the hearing should be the opportunity for any and all defences to be aired.

- Ofgem's response

3.14. *We have decided to introduce this change in light of respondents' views.*

3.15. *On the related points raised by respondents, the manner in which hearings operate in practice is a matter for the EDP, working within the framework of the REMIT Procedural Guidelines and the Enforcement Guidelines. The EDP will decide and communicate to parties how and when hearings will take place in individual investigations and may consider issuing more general guidance on how hearings work, in the future.*

3.16. *The hearing is an opportunity for parties to put their case to the decision-makers directly. But, prior to this, the parties subject to enforcement action will have received and had opportunity to make representations on an Issues Letter, and a Warning Notice. The process is not intended to encourage parties to hold back evidence or information until a hearing, but to allow a full exploration of the issues in a timely manner. If parties have evidence that they did not fail to comply with a REMIT requirement we would expect them to raise that at the earliest opportunity. So it should only be in exceptional circumstances that new relevant evidence comes to light after the opportunity to make written representations on a Warning Notice but before a hearing takes place. The Procedural Guidelines give the EDP, in exceptional circumstances, the discretion to allow such new material to be heard. This approach is consistent with how hearings operate in our sectoral cases. We therefore have not changed this position in the Procedural Guidelines.*

Other Comments

3.17. This section highlights other comments made in relation to the proposed Procedures. Where relevant to a specific section in the REMIT Procedural Guidelines, the comments have been grouped under the same headings as the part in the REMIT Procedural Guidelines to which they relate.

Criteria for opening an investigation under REMIT

3.18. The REMIT Procedural Guidelines (paragraph 4.9) gives a list of factors that we may take into account when deciding whether to open a REMIT investigation. It summarises how these operate in an earlier paragraph (paragraph 4.6).

- Views of respondents

3.19. One respondent said that the description of a "priority matter" to investigate given in paragraph 4.6 was inconsistent with the list given in paragraph 4.9. Another respondent asked for consistency and clarity in our use of language as to whether an incident was a "REMIT breach" or a "failure to comply with a REMIT requirement".

- Ofgem's response

3.20. *The intention of the brief descriptive examples in paragraph 4.6 was to give an indication of how we assess priorities, with the list of prioritisation criteria given in 4.9 being those which we will use to determine whether a matter is a priority to be investigated. However, to prevent any confusion about this, we have deleted the descriptive examples from paragraph 4.6.*

3.21. *Regulation 4 of the REMIT Enforcement Regulations[5] defines a "REMIT requirement" as a requirement imposed by certain of the Articles in REMIT itself. These include Articles 3(1) and (5) (prohibition of insider trading), Articles 4(1), (2) and (3) (obligation to publish inside information, Article 5 (prohibition of market manipulation), Article 8(1) and (5) (data collection), Article 9(1), (4) and (5) (registration of market participants) and Article 15 (obligations of persons professionally arranging transactions.). Under regulation 26, we may impose a penalty on a person who has failed to comply with a REMIT requirement.*

3.22. *Given the cross-reference to REMIT, a failure to comply with a REMIT requirement would be, in layman's terms, a breach of REMIT. We therefore use these terms interchangeably in these documents.*

The Investigation process

3.23. In finalising the revised REMIT Procedural Guidelines document, we made some minor edits to make the language and structure of the Guidelines easier to read and follow. As part of this review, we noted that the Enforcement Guidelines set out that the name of the Senior Responsible Officer (SRO) would be given in the letter notifying a person they are being investigated under our sectoral powers. And that the SRO should be contacted if a company wishes to raise any procedural issues during the course of the investigation.

3.24. We are aligning procedures with respect to communications to and from the SRO in REMIT cases with those in our sectoral guidelines. So we have added the above points to paragraph 5.2 of the REMIT Procedural Guidelines.

[5] As amended by The Electricity and Gas (Market Integrity and Transparency) (Enforcement etc.) (Amendment) Regulations 2015 which is due to come into force on 1 July 2015 and covers Articles 8 and 9 of REMIT.

Issues letter

3.25. In line with the proposals in our consultation, we have changed the name of the Statement of Case to an Issues Letter, following no stakeholder objection. This avoids confusion with the Statement of Case issued in our other enforcement work, which follows different processes from the ones required in our REMIT Regulations. We will prepare an Issues Letter when we consider that there has been a failure to comply with a REMIT requirement. This will set out the relevant facts, explain our initial findings and the case against the person, and seek the person's views.

The decision-making process for contested cases

3.26. Under the REMIT Enforcement Regulations, we may impose a penalty on any person – legal or natural – who we find to have breached REMIT.

- Views of respondents.

3.27. A respondent asked whether there was a need, in instances where a penalty may be imposed on an individual as opposed to a company, for the Panel in that case to include a person with judicial experience. This would be to ensure that a person with experience of assessing appropriate penalties for individuals was on the Panel.

- Ofgem's response

3.28. *We are satisfied that the EDP membership both can and will recognise the impact of decisions on breaches and sanctions involving individuals. We note that the composition of the EDP, as set out in the REMIT Procedural Guidelines, is consistent with the procedures for the panel composition for the FCA's Regulatory Decisions Committee[6], who perform a similar role to Ofgem's EDP. Further, we have a clear statement – in the REMIT Penalties Statement – of how sanctions will be applied in those circumstances. Given this, we do not consider it necessary to introduce a requirement for a Panel hearing a case against an individual to include a member with judicial experience.*

[6] As set out in the FCA's Decision Procedure and Penalties Manual.

4. REMIT Penalties Statement

Chapter Summary

Respondents generally agreed with the proposed policy statement. In the light of comments, we have clarified that the duration and frequency of a breach will be amongst the factors to be taken into account in deciding whether or not to impose a financial penalty. We also restate our view that parties should do all they can to identify those affected and provide restitution to them. We clarify that the Authority may in settled cases allow voluntary payments in lieu of part of a financial penalty. We also set out our position on the issue of serious financial hardship.

We consider that our Penalties Statement provides appropriate incentives for regulated parties to comply with REMIT. We also believe it strikes an appropriate balance in promoting consistency with the enforcement of regulations in financial markets and across the Authority's own portfolio of enforcement powers.

Deciding to impose a penalty and/or make restitution etc.

4.1. In our consultation we proposed a non-exhaustive range of factors that the Authority may consider when deciding whether to impose a financial penalty, make a restitution order or issue a statement of non-compliance. We also proposed a range of factors that may affect the level of any penalty imposed.

- Views of respondents.

4.2. One respondent noted that our proposals did not mention the duration of a breach. The respondent said it should be a relevant factor in setting the amount of a penalty.

- Ofgem's response

4.3. *We agree that duration should be mentioned in our guidance. However, we have decided that duration should be a factor that may affect the decision whether to impose a penalty. This approach is consistent with the FCA's.*

4.4. *Similarly, our proposals did not mention frequency as a factor in deciding whether to impose a penalty (but did mention it as a factor in setting the penalty level). We consider that, like duration, it is an appropriate factor to take into account in the decision whether to impose a penalty. We have therefore included it as a factor that affects both these decisions. This approach is consistent with the FCA's.*

Assessing seriousness/determining the penalty starting point

4.5. In our consultation we noted that the starting point for financial penalties would be a figure that reflects the seriousness of the breach, irrespective of whether the Authority has identified and calculated detriment and/or gain. We proposed to adopt a five-level scale of seriousness.

- Views of respondents

4.6. Respondents generally supported these proposals. However, one respondent requested guidance on the circumstances in which we might decide that profits rather than revenue was a more appropriate indicator of harm when assessing the seriousness of a breach by a firm. That respondent also asked us to clarify how we would derive the profits from a relevant product line or business area. Another respondent said that instead of five levels of seriousness we should have an upper limit of 20% of relevant revenue. This would, said the respondent, facilitate setting penalties at levels that reflect the subtleties of each case.

4.7. One respondent said the Authority should not consider the impact of the breach on market confidence because that was a subjective test and we should concern ourselves with tangible effects. Another argued that the factors indicating recklessness were not appropriate and did not reflect case law. This respondent said recklessness involved a greater wilful disregard of the risks of a breach.

4.8. Consistent with the FCA, we proposed that the penalty starting point in market abuse cases against individuals should be the greater of a percentage of relevant income, a multiple of the profit made (or loss avoided) or, in the most serious cases, £100,000. One respondent stated that we should not have quantified starting points for individuals in serious cases and should not say the starting point will be "the greater of" these alternatives. The same respondent said a starting point of at least £100,000 was too high because energy traders were typically paid less than financial traders. This respondent said a figure of £15,000 would be proportionate and that our proposal could affect their ability to recruit.

4.9. Separately, we were also asked whether an individual's relevant income for the purposes of calculating a penalty starting point was pre-tax or post-tax.

- Ofgem's response

4.10. *Our proposals on the circumstances in which we might decide that profits rather than revenue was a more appropriate indicator of harm when assessing the seriousness of a breach were similar to the FCA's published policy, which does not provide additional guidance of this nature. We intend to adopt a flexible approach rather than introducing fixed percentage levels in relation to profits. This will allow us*

to reflect the particular circumstances of each case in deciding on the most appropriate indicator of harm.

4.11. *On the comment regarding the levels of seriousness, we have decided to keep the five levels proposed. This is consistent with the FCA's approach and it should be well understood by wholesale market traders. The subtleties of each case can be taken into account during the later stages of setting the penalty (for example, when considering aggravating and mitigating factors).*

4.12. *We did not amend our processes in line with the proposal to have flexibility to pro rata relevant revenue when there was a single event lasting less than a year. This is an important element in determining the starting point for a penalty. We consider that a blanket pro rata system for all firms in relation to breaches of short duration would weaken the incentive for compliance and would create an undesirable point of difference with the FCA's regulatory regime. However, the Authority may take this into account as necessary when setting the final level of the penalty in any particular case.*

4.13. *The Authority does not agree that it should be concerned only with tangible effects, as suggested by the comment on considering effects on market confidence. A core aim of REMIT is to create the conditions where all market participants can have confidence that the wholesale energy markets are functioning properly. It is therefore important that, just as the Authority may seek to penalise attempted market manipulation that does not succeed in securing any gains for the perpetrator, or other breaches with potentially harmful effects, so it may also consider the impact of a breach on market confidence and take appropriate enforcement action.*

4.14. *The Authority considers that the factors cited under 'recklessness' are appropriate and does not intend to modify them. We note that it is a non-exhaustive list, and that the Authority considers it important that the senior managements of firms understand and act on their responsibilities to establish and maintain effective compliance regimes. Furthermore, a greater wilful disregard of the risks of a breach is likely to be considered to be reckless, although the Authority will of course consider all the circumstances of each case.*

4.15. *We want to ensure that strong incentives are in place for individuals to comply with REMIT. We believe that quantifying the starting point provides regulatory certainty and that a starting point of at least £100,000 for the most serious cases of market abuse provides a strong incentive to comply. We do not therefore intend to modify this figure, as proposed by one respondent. However, we note that the Authority can take personal income into account when setting the level of the penalty and may reduce the penalty if it would cause serious financial hardship.*

4.16. *Finally, in response to the question raised, we confirm that the starting point will be a pre-tax figure. An individual's relevant income will be the gross amount of*

all benefits received by the individual from the employment connected with the breach and for the period of the breach. Where an individual was in that employment for less than 12 months, the relevant income will be calculated on a pro rata basis to the equivalent of 12 months' relevant income. This is consistent with the FCA's approach and with the approach taken when a firm has been in existence for less than a year.

Reasonable belief and reasonable precautions

4.17. Our proposals for calculating penalties introduced five fixed levels that represent, on a sliding scale, the seriousness of the breach. In assessing the seriousness of a breach and the behaviours of a person, we said that the Authority will consider any representations that a person reasonably believed that its conduct did not amount to a REMIT breach, and/or that it took all reasonable precautions and exercised all due diligence to avoid such a breach.

- Views of respondents

4.18. Two respondents stated that the reasonable belief and due diligence test was tougher than the FCA's equivalent. One of these respondents also said that the Authority should not impose penalties if it accepted that the person had a reasonable defence. They agreed that the Authority should consider representations on this issue.

4.19. One respondent stated that a financial penalty should be less likely if the person followed any guidance, codes, rules or commonly accepted practices or customs. Another respondent stated that the Authority should not penalise individuals if they acted reasonably, following company procedures, but only if their conduct was reckless, deliberate, negligent, lacking integrity or seeking personal financial gain.

4.20. One respondent said the list of considerations should include guidance from other competent authorities such as ACER and the FCA. A different respondent asked us to clarify whether they have to meet each item in the lists or just one of them.

- Ofgem's response

4.21. *The 2013 Regulations require the Authority's policy on determining the amount of a penalty to have regard to whether the person believed, on reasonable grounds, that the behaviour was not a breach and whether the person took all reasonable precautions and exercised due diligence to avoid behaving in a way that breached an obligation. These regulations also require us to indicate the circumstances where the Authority expects to accept representations of this nature.*

Our Penalties Statement is consistent with these statutory requirements. We have made clear that the Authority will consider any such representations.

4.22. *We said in our proposals that our consideration of whether a person has a reasonable defence relates for example to whether the person followed guidance given by the Authority, followed internal company procedures or the conduct was engaged in for a legitimate purpose. However, it does not cover market customs and practices more generally since the Authority may wish to take a view on whether such customs and practices are appropriate.*

4.23. *In deciding whether or not there is a reasonable defence, the Authority may also take a view on the appropriateness of any company policies, procedures or advice that were available to the person. If the internal policies, procedures or advice were not appropriate, the Authority may consider it appropriate to impose sanctions on the firm instead of or as well as the individual.*

4.24. *In response to the comment raised, we have decided not to include ACER's Guidance in this list because such guidance is to the NRAs and not market participants. Where we consider it appropriate, we may publish guidance that takes into account this information, or information from other authorities, including the FCA. We have, however, taken the opportunity to clarify in the Penalties Statement that parties will have to demonstrate satisfactorily that they have considered all relevant matters; and what is relevant may differ according to the circumstances of the particular case.*

Aggravating and mitigating factors

4.25. We proposed that The Authority may increase or decrease the amount of the penal element to take into account factors that aggravate or mitigate the breach.

- Views of respondents

4.26. One respondent said there should no double counting of factors already considered in assessing the seriousness of the breach. This respondent also felt there was potential for double counting of deterrence given that it was mentioned at paragraph 6.9 and at the later stage 4 of the penalty calculation process with the deterrence uplift criteria.

4.27. Another respondent noted that 'repeated breaches' was not an aggravating factor in the FCA's guidance and should not be in the Authority's guidance. A different response stated that previous non-compliance of the same type should influence the level of the penal element but that the Authority should not increase a penal element where another body has already taken action for that same event.

4.28. Then, a respondent said the aggravating factor relating to whether a firm has previously been told about the Authority's concerns was too broad and could discourage or over-formalise dialogue between a firm and the regulator including at working level. Another respondent said that we should add a mitigating factor that the conduct conformed to industry practice and custom. Meanwhile, one respondent felt that the FCA's guidance gave less emphasis to immediate and full self-reporting than the Authority's proposed guidance.

- Ofgem's response

4.29. *We agree that there should be no double counting of deterrence and we do not consider that the Penalties Statement will give rise to it.*

4.30. *We have considered the view of the respondent relating to repeated breaches. 'Repeated breaches' is included as an aggregating factor for non-REMIT enforcement cases. We have included this (and not aligned with the FCA on this point) because we believe it helps us achieve our Vision: it is important to allow extra deterrence when a company or individual breaches REMIT multiple times.*

4.31. *The Authority reserves the right to impose its own sanctions even if another regulatory body is likely to impose or has already imposed a financial penalty. We have amended paragraph 4.4 (which sets out when the Authority is more likely to issue a statement of non-compliance) to make this clear. The Authority may wish to do this where it appears that further action is needed to achieve any of the enforcement objectives in the Penalties Statement.*

4.32. *We do not believe that the factor relating to whether a firm has previously been given an indication of concern from Ofgem is too broad. Firms should respond promptly and effectively to any indications of concern from Ofgem about their internal procedures or conduct, whether our concern is expressed at senior or working level (and through whatever medium). The Authority may conclude that failure to do so is an aggravating factor that should increase the amount of any proposed financial penalty. The Authority will consider the particular facts of the case in coming to a view on whether a firm had been previously notified about Ofgem's concerns. As noted previously, we will be bound by the requirements on us to act reasonably and proportionately.*

4.33. *We do not believe it is appropriate to add a mitigating factor that the conduct conformed to industry practise and custom. It is possible that conduct, which may be widespread, does not comply with REMIT. Regulated persons must be satisfied that their own conduct complies with REMIT and should not seek to argue in mitigation that others are behaving in the same way.*

4.34. *The Authority attaches great value to self-reporting of breaches across its enforcement activities. Consistent with the Chairman's letter of March 2014 on future*

financial penalties under the Gas Act and the Electricity Act, and the subsequent Penalties and Redress Policy Statement of September 2014, the REMIT Penalties Statement also seeks to impress upon regulated persons the importance of prompt self-reporting after becoming aware of a REMIT breach.

4.35. *One of the FCA's principles for businesses is that "a firm must deal with its regulators in an open and cooperative way, and must disclose to the appropriate regulator appropriately anything relating to the firm of which that regulator would reasonably expect notice." This covers the need to report breaches to the FCA. We also attach great importance to this, as reflected in our Statement.*

Settlement discounts

4.36. Our proposed Penalties Statement included proposals to offer Settlement discounts on a sliding scale, depending on the settlement window in which settlement was agreed.

- Views of respondents

4.37. Most respondents accepted the proposed discounts of 30%-20%-10%. One respondent stated that the proposed discounts were too low and would not incentivise settlement.

- Ofgem's response

4.38. *We have decided to retain the settlement percentages as proposed. We consider that they are set at the right level. They are consistent with the Authority's discounts in cases under the Gas Act and Electricity Act. It is up to the persons concerned whether they wish to settle. If they don't wish to settle we will proceed to a contested case.*

Restitution

4.39. Instead of (or in addition to) imposing a financial penalty, our proposed Guidelines stated that the EDP may make a restitution order or apply to a court for one. We said in our consultation that where the Authority can identify the affected parties, it would normally expect to make a restitution order if the person in breach does not agree to provide appropriate restitution voluntarily.

- Views of respondents

4.40. Two respondents said that it would be hard to link the detriment from a breach to affected parties, especially in non-market abuse cases. They felt it was unrealistic and onerous to expect firms proactively to provide restitution.

4.41. One respondent stated that in the FCA's guidance restitution is linked to gain and does not mention detriment to others. This respondent said that restitution to be paid by individuals under REMIT should be limited to the value of the gain. Another respondent stated that the restitution amount should reflect the seriousness of the breach given the requirement under the EU REMIT Regulation for proportionate financial penalties.

4.42. One respondent felt that restitution was not appropriate for registration and data reporting breaches or in relation to any failure to retain records. The respondent said that we should note this explicitly in the Penalties Statement.

4.43. The Authority does not have the power to direct the payment of restitution to proxies/charities unless it is satisfied that the recipients of these payments are the specific customers (a) to whom the profits are attributable or (b) who have suffered the loss or adverse effect in question. However, one respondent said that our policy should be flexible enough to allow voluntary restitution in lieu of all or part of a penalty.

- Ofgem's response

4.44. *Our proposals noted that it might not always be easy to link a detriment to affected parties. We recognised that circumstances would differ from case to case. However, we remain clear that firms and individuals should do all that they can to identify those affected and provide restitution to them. We have therefore decided not to alter this text.*

4.45. *The 2013 Regulations set out the requirements for determining the amount of any restitution. Consistent with this, the Penalties Statement notes that the amount shall be that which appears to the Authority to be just, having regard to the profits that appear to have been accrued and/or to the loss or other adverse effect suffered as a result of the breach (see paragraphs 6.7, 7.7 and 8.7).*

4.46. *We do not intend to make changes to reflect the comment about restitution for registration and data reporting not being appropriate. The Regulations do not preclude the use of our restitution powers in relation to these types of breach. We see no need to do so in the Penalties Statement.*

4.47. *It is already open to us to allow a voluntary payment in lieu of part of a financial penalty in settled REMIT cases, as suggested by one respondent. But, we will only allow this if we are satisfied that it would be in the interests of consumers or market participants. This flexible approach is consistent with the REMIT legal framework and with our approach in settled cases under the Gas Act and Electricity Act.*

Serious financial hardship

4.48. The consultation discussed issues relating to whether a reduction in the proposed penalty is appropriate if the penalty would cause the subject of enforcement action serious financial hardship.

- Views of respondents

4.49. Most respondents supported our proposals about serious financial hardship. However, one respondent said the income and capital thresholds (£14,000 and £16,000 respectively) provided such limited relief for individuals that this could affect a company's ability to recruit traders.

4.50. The respondent said we should consider remuneration levels in the energy sector, not the financial sector. Another respondent said we should evaluate the thresholds on case-by-case basis having regard to personal circumstances and the effects on dependents.

- Ofgem's response

4.51. *We have decided not to change the thresholds. The intention was and remains that the thresholds provide a strong incentive for individuals to comply with REMIT. We believe that they do this.*

4.52. *We note that the Authority may, in setting the final level of a penalty, consider the individual's personal income and any representations that a penalty would cause serious hardship. In addition, the Authority may increase the thresholds in a given case (see paragraph 9.5 of the Penalties Statement).*

Other issues

4.53. Some comments made by respondents are not specific to just one part of the Penalties Statement. We outline these comments and our response to them in this section.

- Views of respondents

4.54. One respondent warned against copying FCA policies without considering particular conditions of REMIT and energy markets.

4.55. One respondent said the introductory description of the Authority's REMIT powers in the Penalties Statement should be aligned with the equivalent introductory text in the Procedures Guidelines and with Article 18 of REMIT.

4.56. One respondent said that penalties must be proportionate as well as dissuasive and effective (and that this requirement should be reflected in our regulatory objectives for REMIT).

4.57. Two respondents said we should define 'market abuse cases' and 'non-market abuse cases' and be clear which REMIT requirements fall into which category.

4.58. One respondent said that the first two deterrence uplift criteria are "extremely subjective" and gave the Authority wide discretion to increase the penalty. This respondent also said the final penalty adjustment was subjective.

4.59. One respondent stated that regulatory action should be proportionate to the level of available guidance and that we should take account of the infancy of REMIT and that initially there will be limited understanding about compliance.

- Ofgem's response

4.60. *In response to the caution against copying FCA policies, we clarify that in drafting our documents we have carefully considered the extent to which the wholesale energy market regulation should mirror the regulation of financial services. We believe that the Penalties Statement strikes an appropriate balance between consistency across the Authority's own enforcement activities and with the FCA. Clearly, Ofgem's investigating teams and the Authority will consider carefully the particular conditions of energy markets when deciding how best to use their REMIT enforcement powers in practice.*

4.61. *We agree with the comment that the introductory paragraphs in the Procedural Guidelines and Penalties Statement should align. We have therefore amended the definition of a REMIT breach in the Penalties Statement.*

4.62. *In response to the comment about needing to be proportionate, we note that the 2013 Regulations require that the amount of any penalty we impose must be appropriate in all the circumstances of the case. The Penalties Statement is fully consistent with this requirement. We also made clear in our proposals that we would*

have regard to the principles of better regulation when using our REMIT powers. This means, amongst other things, that any financial penalties should be proportionate as well as dissuasive and effective.

4.63. *We accept the benefits of clarifying, as requested, which REMIT breaches fell into which category. We confirm that breaches of Article 3 and 5 of REMIT are market abuse cases. Other breaches are non-market abuse cases. We have noted this in the Penalties Statement.*

4.64. *We have considered the views on the deterrence uplift factor and the final penalty adjustment. The Authority considers it vital to ensure that the penalties regime provides a strong deterrent effect against repeated breaches of a similar nature, whether committed by the same person or others. The Authority therefore has decided to retain an explicit statement that it may increase a penalty where the penal element would otherwise be too small to meet its objective of credible deterrence or where the Authority thinks it likely that similar breaches would be committed in the future.*

4.65. *The Authority will, as set out in the Penalties Statement, determine the person's total financial liability by adding the final penal element to any restitution payments required to be made. However, the Authority wishes to ensure that the total financial liability is always appropriate in the circumstances of the case. Therefore, the Authority reserves the right to make a final adjustment to either element of the total. This might, for example, involve reducing a financial penalty in order to avoid causing serious financial hardship to the person. We have set out our approach to this issue in paragraphs 6.38 to 6.43 for firms and section 9 for individuals. The Authority will of course consider all the circumstances of each case before deciding the total financial liability that will be imposed.*

4.66. *Finally, we note the view that REMIT is in its infancy. The EU REMIT Regulation came into force in December 2011 and the civil enforcement regime in Britain derives from regulations made in June 2013 (and augmented in April 2015). The Authority published a first set of guidance on REMIT penalties and procedures in November 2013 and published a letter about inside information disclosure in July 2014. We consider that all parties should by now have a high awareness of their obligations under REMIT. That said, the 2013 Regulations allow for a consideration of reasonable belief/due diligence, which affects the level of the penalty that the Authority can impose.*

Appendices

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Appendix 1 - Feedback Questionnaire

Ofgem considers that consultation is at the heart of good policy development. We are keen to consider any comments or complaints about the manner in which this consultation has been conducted. In any case we would be keen to get your answers to the following questions:

1. Do you have any comments about the overall process, which was adopted for this consultation?
2. Do you have any comments about the overall tone and content of the report?
3. Was the report easy to read and understand, could it have been better written?
4. To what extent did the report's conclusions provide a balanced view?
5. To what extent did the report make reasoned recommendations for improvement?
6. Please add any further comments?

Please send your comments to:

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