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By email: EGPPconsultation@ofgem.gov.uk

Dear Heather and Megan

Re: Consultation on changes to Ofgem's Enforcement Guidelines and Sectoral Penalty Statement ("Consultation")

This letter and its attachments form our response to the Consultation. Centrica has a number of concerns about the proposals, which are set out in detail below. Overall, regrettably, the proposals will tend to reduce regulatory certainty, contrary to regulatory best practice. In particular, we urge Ofgem not to reduce the amount of guidance about the proper level for penalties.

In our view, greater justification is required for the change proposals at this time and as presented in the Consultation.

We have outlined in Annex 1 attached to this response, the answers which directly relate to the questions raised within your consultation document dated 9 June 2021.

Proposed Changes to the Penalty Statement

Clear and consistent enforcement in the energy sector is in the interest of business and consumers alike. The removal of detail about the factors Ofgem considers and the process it follows when assessing penalties and consumer redress orders in the updated Penalty Statement (Statement) is concerning. These changes reduce the accountability and transparency of Ofgem's decision making process.

It does not fit with Ofgem's stated aim to ensure procedural fairness and its duty to ensure any penalty or redress order imposed is reasonable and proportionate in all the circumstances. The removal of detailed guidance from the Statement risks creating an unpredictable enforcement regime which could undermine confidence of businesses to invest or innovate in the energy sector.

To ensure procedural fairness, penalties and consumer redress need to be fairly and consistently assessed and calculated across different investigations. The detailed factors set out in the current Statement ensures that decision makers follow a consistent approach when making decisions about penalties and consumer redress orders. This secures fairness and consistency in decisions. Similar penalties and / or consumer redress are likely to be imposed in cases of equivalent seriousness. Consequently, reducing the level of detail provided in the Statement about these factors is likely to decrease consistency and introduce unpredictability into the decision-making process. This has the potential to reduce the deterrent message sent to the market by enforcement action.

The Statement is also a guidance document for licensees, which helps them to understand their obligations under the energy market rules. Removing information about the factors that tend to increase or decrease the seriousness of a breach and the level of fines etc. significantly reduces its value as a guidance document for licensees.

By way of comparison, in the Financial Services sector, the Financial Conduct Authority (FCA) penalty statement is a part of the FCA handbook which is the key source of guidance and information for organisations regulated by the FCA. The FCA's penalty statement includes significantly more detail than the draft Ofgem penalty statement.

Duty to Calculate Gain to Regulated Person and Potential Detriment Caused by Breach

It is not clear how Ofgem can follow a proper and legitimate enforcement process aimed at assessing consumer detriment when it is not specifically calculated and is instead considered generally as part of its assessment of seriousness (Step 2 of the calculation of the financial penalty or consumer redress). Robust quantification of detriment is fundamental to a fair and legitimate process, the outcome of which has the potential to result in significant financial liability for the licence holder.

Ofgem should clearly explain how it intends to assess and weigh proportionality and practicality when considering whether or not specifically to calculate consumer detriment. Additionally, it should set out what opportunity licence holders will have to challenge Ofgem's views. Furthermore, clarity is also required on how Ofgem will determine penalty amounts where no detriment is calculated.

Settlement Windows

Ofgem's proposal to separate the processes of Settlement and Contest may not allow sufficient time for a licence holder to have a meaningful discussion around Settlement (in order to reach a fully educated and reasoned conclusion on the option to settle) which could lead to a reduction in the number of cases that are settled. The change will also remove the ability to settle once the full statement of case is provided to the party, as this is only provided under contested cases, again reducing the licence holder's ability to make a decision on Settlement. In addition, we are keen that licence holders are provided with sufficient time to have meaningful discussions both internally to their own organisation and with Ofgem, around Settlement before this opportunity is lost due to the proposals to run Settlement and Contest processes separately.

The fact that Ofgem has also removed much of its guidance relating to the penalty and / or consumer redress assessment process, makes it much more difficult for licence holders to reach a final decision as to whether Settlement is appropriate or not.

Decision-Making Process

The proposal to select a Director or Settlement Committee for decision-making is at Ofgem's own discretion, and where it deems the Enforcement Decision Panel's (the Panel) expertise may be required. There is no threshold, grounds or process documented to reflect how Ofgem may make its choice. This does not fit with Ofgem's intent of providing clarity or transparency. Example criteria for where it is appropriate for such decisions to be made by a Director alone including guidance about the complexity, seriousness or sensitivity of cases where this would be appropriate, may be helpful, as would transparency of process and grounds for decision.

Alternative Action

It is not clear why Ofgem is intent on pursuing Settlement over Alternative Action. In Ofgem's own words, many successful outcomes have been achieved through Alternative Action and informal compliance. It is our view that informal action (Alternative Action) would be the quickest route to resolution. The Consultation states that "*alternative action outcomes do not include a formal finding of a breach by the Authority*". Ofgem also states '*If we consider that a case is not suitable to be resolved without the use of our statutory enforcement powers, the case may still be settled by Alternative Action.*' It would appear then, that

Alternative Action does present an option for Ofgem to use informal action whilst acting as a deterrent and acting upon its enforcement powers.

Any evidence Ofgem has to suggest that continuing to use Alternative Action will weaken deterrent messages would be welcomed in order to further understand its proposals.

Whilst there is a lack of clarity on the specific procedure to be applied in the course of Alternative Action (which should be corrected), our understanding is that licence holders who participate in the process today, do publicly admit a breach.

Therefore, a more transparent framework within which Ofgem will decide upon which process to apply i.e. Alternative Action, Settlement or Contest would help to provide transparency, consistency and fairness across all licence holders.

Self-Reporting

It appears that the introduction of self-reporting into SLCs has also removed any benefit that this may bring to the penalty or consumer redress order which is determined as part of the outcome of a case. It is, of course, also proposed that the consequence of not self-reporting will now include a harsher penalty or consumer redress order; but there is no guarantee that this will outweigh the reduced positive incentive. This could serve to deter licence holders from self-reporting, given there is no longer a benefit to doing so, and concern over lack of transparency and fairness surrounding the outcome. In turn this could lead to unintended consequences across the sector, including the inability of licence holders to learn from each other in a timely manner.

I trust the content in this response will be given due consideration in your consultation process. Should you wish to discuss any of the content with us in more detail, please don't hesitate to contact me in the first instance.

Yours sincerely

A handwritten signature in black ink, appearing to read 'A. Nolan'.

Amanda Nolan
Regulatory Manager, Consumer Affairs & Policy
Centrica

Annex 1

Question 1 – What is your view on the proposal to remove the middle and late settlement windows, and associated settlement discounts?

We agree with the proposal to remove the middle and late settlement windows and associated settlement discounts. In the event of any breach, it is in the interest of licence holders to address any consumer detriment, reimburse any detriment caused and improve relevant policies, processes and procedures at the earliest opportunity. As such, it should be sufficient for there to be a single settlement window.

However, separating the processes of Settlement and Contest may not allow sufficient time for a licence holder to have a meaningful discussion around Settlement (in order to reach a fully educated and reasoned conclusion on the option to settle) which could lead to a reduction in the number of cases that are settled. The change will also remove the ability to settle once the full statement of case is provided to the party, as this is only provided under contested cases.

The fact that Ofgem has also removed much of its guidance relating to the penalty and / or consumer redress assessment process, makes it much more difficult for licence holders to reach a final decision as to whether Settlement is appropriate or not.

Question 2 – What are your views on the option of allowing the Director responsible for Enforcement to be a decision maker in settlement cases?

Ofgem states that the Panel was established in 2014 to take decisions in contested and settlement enforcement cases and to provide separation between the case team and the decision maker. There is a risk that moving back to an individual decision-maker may remove some objectivity that a Settlement Committee may bring.

The proposed changes mean that Ofgem will exercise its discretion in choosing either a Director or Settlement Committee for decision-making. The consultation states that the option for a Settlement Committee remains for cases where it is considered the Panel's specialist expertise may bring benefit to the case, however there are no thresholds, grounds or processes documented to reflect how Ofgem may make its choice. This does not fit with Ofgem's intent of providing clarity or transparency. Ofgem should ensure it provides transparency and clarity by outlining example criteria for scope, complexity, seriousness or sensitivity, as well as setting out a clear process and grounds for decision.

It is also in the interests of transparency, to provide licence holders with some criteria of not only who the decision-maker will be in cases of settlement, but also when settlement may be a more suitable route as opposed to Alternative Action. That way, licence holders can take some assurance that an objective and considered approach is taken in all scenarios.

Question 3 – In your view, are there any other steps you think we could take to speed up the settlement process, without undermining the evidence-based nature of our decision making?

We urge Ofgem to provide greater clarity on the benefits of early, open and transparent engagement. The industry fully supports increased openness and transparency between the regulator and licence holders, so that the focus can be on resolving issues promptly and in the best interests of consumers, and so that learnings can be widely and quickly shared with other suppliers who can replicate any necessary actions in response. However, such engagement and beneficial outcomes will only become established if suppliers are incentivised to carry out such behaviour.

It appears that the introduction of self-reporting into SLCs has also removed any benefit that this may bring to the penalty or consumer redress order which is determined as part of the outcome of a case. It is, of course, also proposed that the consequence of not self-reporting will now include a harsher penalty or

consumer redress order; but there is no guarantee that this will outweigh the reduced positive incentive. This could serve to deter licence holders from self-reporting, given there is no longer a benefit to doing so, and concern over lack of transparency and fairness surrounding the outcome. In turn this could lead to unintended consequences across the sector, including the inability of licence holders to learn from each other in a timely manner.

Ofgem will ultimately need to consider which enforcement model it wishes to adopt, but if the objective is to promote the best outcome for consumers, we believe that this would be far better served through encouraging suppliers to share such issues immediately. We believe this would be best achieved by providing the clearest of guidance that in the case of any unintentional non-compliances that had been identified by the supplier, Ofgem's enforcement policy would be focussed on ensuring that the issue was promptly fixed and the issue openly shared. Ofgem's current Enforcement Guidelines (Guidelines) provide very clear definitions of its approach, process, criteria and structure to justify its decisions. The proposed Guidelines written at a principles-based level introduce the risk of undermining the evidence basis of the approach taken and outcomes considered, which may conversely lengthen any Settlement or Contest process.

It is not clear why Ofgem is intent on pursuing Settlement over Alternative Action. In Ofgem's own words, many successful outcomes have been achieved through Alternative Action and informal compliance. It is our view that informal action (Alternative Action) would be the quickest route to resolution. The Consultation states that *"alternative action outcomes do not include a formal finding of a breach by the Authority"*. Ofgem also states *'If we consider that a case is not suitable to be resolved without the use of our statutory enforcement powers, the case may still be settled by Alternative Action.'* It would appear then, that Alternative Action does present an option for Ofgem to use informal action whilst acting as a deterrent and acting upon its enforcement powers.

Any evidence Ofgem has to suggest that continuing to use Alternative Action will weaken deterrent messages would be welcomed in order to further understand its proposals.

Whilst there is a lack of clarity on the specific procedure to be applied in the course of Alternative Action (which should be corrected), our understanding is that licence holders who participate in the process today, do publicly admit a breach.

Therefore, a more transparent framework within which Ofgem will decide upon which process to apply i.e. Alternative Action, Settlement or Contest would help to provide transparency, consistency and fairness across all licence holders.

All licence holders need to have confidence that there is a level playing field when it comes to the rules within which they are required to operate. And have confidence that once rules are set, they will be followed by all on the same basis, and the consequences for not doing are the same for all.

Question 4 – Do you have any comments on the updated guidance on Provisional and Final Orders in section 7 of the guidelines?

One of the reasons provided for the consultation's proposed changes was for the Guidelines and Statement to provide more clarity and transparency. However, Ofgem's statement at paragraph 1.12 that it *'may depart from the general approach to enforcement set out in these guidelines'* contradicts the intent of the changes.

This change will have the effect of removing clarity and specificity, which will damage transparency and undermine certainty in the process. It introduces significant uncertainty into the process, creates unnecessary regulatory risk which is not in the interests of consumers and will impact the processes outlined at section 7 of the guidelines.

Paragraph 7.4 of the proposed Guidelines, Making a Final Order, states the consultation must be live for not less than 21 days but may be subject to change in the future 29 (1) c of the Gas Act and 26 (1) c of the Electricity Act. It would be helpful for Ofgem to outline the circumstances or criteria that may lead to these timescales changing in the future or changing at some point.

Ofgem notes at paragraph 7.19 that the Statutory deadlines that apply to making a final order or confirming a provisional order, are an example of a circumstance where it may depart from the general approach to enforcement. However, it goes on to state that if it considers it appropriate to do so it may depart from the guidelines in relation to any related breach even where the order does not relate directly to that breach. This creates a risk for license holders that where an investigation into several potential breaches is opened, that the right to follow the outlined procedure is lost due to Ofgem's decision to investigate the issues together.

Question 5 – Is there any other information on Provisional or Final Orders you would find helpful to be in the Guidelines?

There is no further information on Provisional or Final Orders beyond that already provided. It would be helpful to see a comprehensive set of Guidelines, particularly in light of the increased use of Orders in recent years.

Question 6 – Do you have any comments on any areas of the revised guidelines?

We would suggest any references to Citizens Advice Consumer Service should now also reference Advice Direct Scotland for Scottish consumers, given the devolvement of consumer protection for energy to the Scottish Government.

It would be helpful to understand who Ofgem references by the term 'other energy businesses' as this is not made clear in the content and may be open to interpretation.

At the webinar Ofgem held on 21 July, it was noted by an attendee that complex areas of energy policy may contribute to unintended consequences such as non-compliance. Although this was pushed back to industry to address any such concerns with Ofgem's policy teams, it would also be helpful and more intuitive for Ofgem to use its own lessons learned from enforcement and compliance action to highlight areas of policy concern which may contribute to such unintended consequences. For example, a recent Compliance Case closed by Ofgem involved 18 suppliers who had breached rules relating to Price Protection (SLCs 23.6, 24.9, 24.11). We have already raised our concerns with our Ofgem Account Manager on the obvious complex nature of such licence conditions.

Section 4

It appears that the introduction of self-reporting into SLCs has also removed any benefit that this may bring to the penalty or consumer redress order which is determined as part of the outcome of a case. It is, of course, also proposed that the consequence of not self-reporting will now include a harsher penalty or consumer redress order; but there is no guarantee that this will outweigh the reduced positive incentive. This could serve to deter licence holders from self-reporting, given there is no longer a benefit to doing so, and concern over lack of transparency and fairness surrounding the outcome. In turn this could lead to unintended consequences across the sector, including the inability of licence holders to learn from each other in a timely manner.

Section 5

We urge Ofgem to consider, as outlined earlier in this response, the continued use of Alternative Action, along with publications, as a speedy resolution to putting things right for consumers.

It would also be helpful to have a framework which outlines the circumstances in which Ofgem might consider Alternative Action is the most appropriate approach to take with a licence holder.

Similarly, as outlined in Section 4 above, we believe Ofgem should, from a procedural fairness perspective, retain the statement that *'any financial penalty must be reasonable in all the circumstances of the case.'*

Section 6

Where Ofgem's Panel is satisfied that a licence holder has or is likely to be in contravention of an obligation, a notice will be published on Ofgem's website, setting out the decision that a breach has occurred (or is ongoing) and that (the Panel) proposes a financial penalty and / or consumer redress order. Ofgem then states that it may publish the Panel's decision that a contravention has occurred (or is ongoing) and that it does not intend to propose a financial penalty and / or consumer redress order.

It would be helpful to understand if a) the latter (no financial penalty and / or consumer redress order) has ever happened in the past; and b) what criteria Ofgem may apply to arrive at such a decision in the future.

Question 7 – What are your views on the changes to the Sectoral Penalty Statement?

Assessment of Seriousness

Ofgem has removed a significant amount of detail from the guidance about the factors it will consider and the process it will follow when assessing the appropriate penalty for a breach (of SLCs). This is a key change and gives more discretion to Ofgem about the factors it takes into account when determining what level of fine to impose. It also gives licence holders less clarity and removes their ability to engage with Ofgem about the proper level for any penalty.

To ensure procedural fairness, penalties need to be fairly and consistently applied across different investigations. The detailed criteria in the current version of the Statement ensures that decision makers apply consistent criteria and approaches when assessing financial penalties and / or consumer redress orders. This ensures fairness and reduces unwanted variability in decisions. As a result, similar levels of fines are more likely to be imposed in cases of equivalent seriousness. Reducing this level of detail is likely to increase unwanted variability in decisions.

The Statement is also a guidance document for licence holders, which helps them to understand their obligations under energy market rules. Removing details of the factors that tend to increase / decrease the seriousness of a breach / the level of fines etc. significantly reduces its value as a guidance document for licence holders.

Ofgem is proposing a significant change to its approach to sanctions for regulated parties, namely only calculating the detriment to consumers as a result of the relevant breach(es) where it is proportionate, reasonable and practicable to do so. This is, as with many of Ofgem's proposed changes, justified on the basis that it is complex and time-consuming to do so.

It is not clear how Ofgem can follow a proper and legitimate enforcement process aimed at assessing consumer detriment when it is not specifically calculated, and is instead considered generally as part of its assessment of seriousness (Step 2 of the calculation of the financial penalty or consumer redress). This is fundamental to a fair and legitimate process, that ultimately will result in a potentially significant payment obligation being placed on a licence holder. Clear guidance on the factors being taken into account in reaching a decision on penalty is the foundation for a clear and reasoned decision that can be understood. Before such a change can be implemented, Ofgem should clearly explain how it intends to assess and weigh proportionality and practicality when considering whether or not to actually calculate consumer

detriment, and what opportunity licence holders will have to challenge Ofgem's views. There is also a lack of clarity on how Ofgem will determine penalty amounts where no detriment is calculated.

There is a material concern here that the design of this approach will limit licence holders' ability to make representations on Ofgem's calculations of the financial penalty, which does not lend itself to a fair, proportionate and accurate outcome. In practice at present, parties are typically given the opportunity to make representations on Ofgem's assessment of consumer detriment and licence holder gain. If Ofgem decides that it is not proportionate, reasonable and practicable to calculate consumer detriment (or indeed licence holder gain), parties should be able to make representations on these factors and how they should be considered by Ofgem as part of its assessment of seriousness. Ofgem should also be required to justify its decision whether or not to calculate consumer detriment and/or licence holder gain and include its assessment of these factors as part of its assessment of seriousness. Otherwise, the process would not be sufficiently transparent.

Speed of process cannot be a justification for avoiding a proper process. We also note that Ofgem (as with other changes) does not appear to have considered whether they will result in more satisfactory outcomes for industry and, more importantly, consumers. There is a risk that dispensing with a specific calculation of licence holder gain and, in particular, consumer detriment, will result in consumer detriment being included in Ofgem's assessment of seriousness in circumstances where a precise calculation would have resulted in little or no consumer detriment actually being assessed. This is particularly the case if regulated parties are not given the opportunity to make representations on consumer detriment as part of Ofgem's assessment of seriousness.

Stress or Anxiety

We note that paragraph 8.3 from the existing Penalty Statement has been removed from the proposed Statement: *'The Authority will not normally require regulated persons to pay compensation for stress or anxiety caused to one or more consumers as a result of a contravention.'* An explanation of why this has been removed, and Ofgem's intent for the future would be helpful, as it is not at all clear whether Ofgem intends to include this, for example, in its assessment of seriousness, or has simply removed the content as it is not relevant.

If Ofgem does intend to require licence holders to pay compensation for stress or anxiety caused, it should provide clear guidance on when this would be appropriate and how it will be determined. We note that under civil law there are restrictions when an individual can obtain compensation for stress and inconvenience. Non-financial loss / loss which is not related to property damage is generally not recoverable for breaches of contract law unless a contract was specifically to provide pleasure or relaxation. There are more situations where this loss can be recoverable in tort law. However, if an individual brings a negligence claim which purely relates to financial losses they have suffered, they will generally not recover loss for "stress and anxiety".

Where a judge imposes damages for this type of loss, they aim to award fair and reasonable compensation which is consistent with what has been provided in similar cases. In particular, they follow the guidelines set out by the Judicial Studies Board in relation to appropriate compensation levels. Therefore, the current level of guidance in the Statement would not be appropriate if Ofgem intends to introduce this type of compensation.

If Ofgem has, however, simply chosen to remove the above content, then it would be helpful to clarify what safeguards are in place to ensure that such precedent is not introduced more formally in future cases.

Non-Retrospective Application of Rules

It would be appropriate for Ofgem to expressly state in the Statement that the energy rules will **not** be applied retrospectively and Ofgem will assess compliance by the rules in force on the date that the action being investigated took place.

Paragraphs 5.5. and 5.9 introduce the term '*and / or other market participants*' which is not described in either of the consultation documents. It is therefore unclear what other detriment there may be, and, in the absence of detailed and specific criteria, how any penalty and / or consumer redress order may be determined.

Paragraph 4.2 contains a typo – 'address' which we assume should be 'redress.'