

Ofgem
10 South Colonnade
Canary Wharf
London
E14 4PU

30th July 2021

Dear Heather and Megan,

Consultation on changes to Ofgem's Enforcement Guidelines and Sectoral Penalty Statement

This response is provided on behalf of National Grid Electricity Transmission plc (NGET) in our role as electricity Transmission Owner (TO) in England and Wales and National Grid Gas plc (NGG) in our role as gas Transmission Owner (TO).

As licenced businesses, we welcome the opportunity to respond to the Enforcement Guidelines Consultation published on 9th June 2021. We have structured our response around the questions included in the Enforcement Guidelines Consultation document.

In summary, we welcome and agree with Ofgem's vision of enforcement in that it achieves a culture whereby businesses put energy consumers first and act in line with their obligations. The enforcement process and guidelines play an important role in protecting consumers and driving the right behaviours from licensees. We recognise that the energy market and enforcement landscape have evolved significantly since the guidelines were last revised in 2017 and Penalty Statement was introduced in 2014, not least because there has been increased scrutiny from energy consumers and an increase in the number of enforcement cases being dealt with by Ofgem and licensees on an annual basis.

We acknowledge the changes and enhancements that Ofgem are proposing to make to the guidelines to ensure flexibility in approach, but we consider that a one size fits all approach is not appropriate, because cases can vary significantly in terms of their root cause, complexity, and impact. The approach needs to balance fairness, thoroughness, and flexibility, and always be proportionate to the specifics of each case. The approach taken by Ofgem should be cognisant of the additional measures and controls included in the regulatory frameworks (particularly the RIIO 2 licences granted to each National Grid Group business and the multitude of Price Control Deliverables PCD obligations they now include), and balance these with the reality that the ambitious delivery programme between now and 2026, and beyond, means that even a prudent and efficient licensee may encounter challenging and complex factors which could impact compliance, particularly given that major projects are delivered by third parties.

On this point, we consider that implementing enforcement with little or no regard to the circumstances of a technical licence breach, for example where a licensee uses its best or reasonable endeavours to meet its obligations, but for whatever reason does not do so, will stifle innovation in delivery solutions and therefore ultimately negatively impact end consumers. The guidelines and Penalty Statement should be clearer on the treatment of companies, especially where circumstances are outside the licensee's direct control, which could then find themselves in a non-compliant situation.

We can see that Ofgem are endeavouring to deal with the increased volume in compliance cases in the most efficient and effective way, but this way of working needs to recognise what the root causes of this increased volume might be, aside from an increase in the number of licensees. Each licensee should understand the importance of compliance, but high volumes of compliance cases may indicate more systemic issues within the energy industry which are impacting on compliance and which warrant further investigation. The focus should not necessarily be on settling a case early, but instead reaching the right outcomes, for energy consumers, Ofgem and the licensee, to avoid perverse or quick decisions being made.

Therefore, the Settlements process should include steps to triage cases in the first instance to establish the most appropriate course of action. Alternative measures are still appropriate in instances of technical breach with low complexity and impact. However, more complex issues should be afforded the investigation time that is warranted in the circumstances. Defaulting to a position that encourages early settlement, including the proposal to remove 2 settlement windows, risks insufficient investigation of the issues, and will not avoid enforcement cases from occurring or recurring. This is because each of the settlement windows combined allows for a comprehensive analysis of all of the issues associated to the case presented in the initial findings, so the time period suggested in moving to just one window will not necessarily allow this and so in complex cases it may be difficult to decide whether it is appropriate to settle or not. Hence, we do not believe that removal of the middle and late settlement window improves resource efficiency, it simply focuses resource on the early window.

We suggest that the role of the Enforcement Decision panel in contested cases continues and we acknowledge why Ofgem are proposing to assign a single director as the decision maker in settlement cases in that they are suitably senior, but it is vital that this process allows for the director to have sufficient technical and industry knowledge, and be impartial, so as to avoid unconscious bias and conflicts of interest. We do not agree that all cases should be decided by only 1 director, but if they are, then these should be limited to the right cases (deemed as less serious, using appropriate criteria to define this), but there must still remain the opportunity for the decision of this 1 director to be scrutinised and reviewed independently, perhaps through additional and independent assurance reviews, including audits.

We note in paragraph 1.8 that Ofgem have conducted a review of the guidelines and Sectoral Penalty Statement, taking account of the evolving market and recent enforcement experiences. Since this review has led to the proposed changes and the updates to the documentation from this, we suggest that this evidence be published alongside this Consultation and made transparent, so that we can further understand the rationale for the proposed changes.

We agree with the housekeeping changes to the Enforcement Guidelines and Sectoral Penalty Statement and we have set out below some further thoughts in relation to each Consultation question.

Confidentiality

I confirm that this response can be published on Ofgem's website.

Yours sincerely,

[By email] Chris Bennett, Director, UK Regulation, National Grid

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

We do not agree that the middle and late settlement windows, including settlement discounts, should be removed.

We note in paragraph 2.2 that since the guidelines were introduced in 2014, and last revised in 2017, no party has settled in the middle or late windows. However, the fact that no party has used the middle and late windows does not mean that their existence did not influence behaviours in the settlement process. Each of the settlement windows is helpful where Ofgem decide to commence formal proceedings without the risk of that work being made redundant by a party deciding to settle. Each time settlement discussions start it pushes out the formal proceedings work which does make the enforcement timeline extremely long potentially. However, those windows do still have some benefit in the circumstances where parties may continue considering their case and even if the work is redundant, it would still be saving consumer time and money if Ofgem were to settle the case and not have to complete its formal proceedings work.

Removing the middle and late windows will not necessarily reduce the time and resource in settling cases, so this is not a rational argument to suggest removing them. Rather, by removing the windows at best it will front load the time and resources invested in a case and at worst it will be at the expense of reaching a fair and considered position.

There is a certain amount of subjectivity and complexity in assessing certain types of breaches as well as the impact of them, so removing settlement windows would not necessarily be in the best interests of consumers. The focus should not be on settling a case early but getting the correct outcome.

The settlement windows work where the relevant organisation and Ofgem evaluate the merits of the case in terms of whether the licensee has met its obligations or not, so the windows are helpful to consider all the evidence. Each of the settlement windows helps clarify and determine a party's position in a gradual, fair, and effective way. Therefore, the process should be thorough and flexible, and include several check points where both Ofgem and the licensee can review their positions before moving on to the next steps.

The consultation also describes in paragraph 2.3 that the settlement window will close on expiry of a reasonable period (usually 28 days) which will be notified to the business when the settlement mandate, draft penalty notice and/or redress order and press notice are provided to the company. It is a moot point whether 28 days given for the settlement window is too short because surely in complex cases, more time would be required to agree a suitable position, and also because where organisations such as Ofgem and ours have complex governance structures, the default 28 days should not be applied without proper consideration.

The consultation also describes that the settlement window may be reopened at the Authority's discretion in exceptional circumstances. However, if the settlement window is reopened there is no guarantee that a settlement discount will remain available. It is unclear what "exceptional" means in this regard. In any event, 28 days seems too rigid in these circumstances. We recommend that whatever period is agreed upon, it reflects the complexity and consequences of the case.

If 28 days continues to be the preferred time window, then it is essential that, particularly in complex cases, Ofgem proactively engages with the relevant licensee to discuss the case and explain its thinking as early as possible prior to any formal clock ticking.

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

We do not agree that 1 Director alone should be given the responsibility for decision making to settle all cases, so the option to use a settlement committee should remain.

We agree that in limited circumstances a decision made by the Director of Enforcement would be acceptable, for example, where there has been a technical breach of an obligation, with no significant harm to end consumers and no financial penalties incurred.

However, for more complex cases, we would expect Ofgem to give proper consideration as to whether a settlement committee could add additional expertise and perspective prior to any decision being made and so we would prefer the option of a settlement committee to remain for these types of cases.

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?

Yes. However, to answer this question, it is not entirely clear on whether the intention is to shorten investigations, which would therefore put investigations at risk, or alternatively, shorten the settlements process itself which are two different things. We would welcome Ofgem clarifying and expanding on this point within the Consultation Decision document. For the enforcement process to work effectively and fairly, both Ofgem and the licensees need to provide sufficient resources to cases, which may mean that the work needs to be done more quickly or more intensively to arrive at decisions more quickly and which therefore impacts on other work.

We would strongly support formal deadlines on Ofgem to complete various stages of investigations. At present, Ofgem can send multiple RFIs to the licensee prior to a case even being opened and then, upon case opening, spend months if not years, further investigating and then settling or contesting the case. We consider that the steps involved in concluding a case and determining and informing the licensee that a case has been closed could be improved, and so setting a reasonable period in which cases need to move to the next stage would be helpful.

It does not feel right or appropriate that some of these cases take years to resolve, which naturally has a reputational impact on the licensee and may cut across multiple price control periods, with all the complexity that brings too. We offer this suggestion as a method to resolve these cases quicker for the benefit of Ofgem, the licensee and end consumers.

It may also be appropriate to allow for without prejudice meetings to discuss the Statement of Initial Findings at draft stage and to understand Ofgem's position, which may help speed up the settlement process because the licensee could present counter views or additional evidence to support the case, which may assist both the licensee and Ofgem in reaching a fair and balanced decision more quickly.

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

We do not have any further comments on the updated guidance on Provisional and Final Orders.

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

We consider that the Provisional and Final Orders are fit for purpose, with no changes required.

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

We agree with the proposed housekeeping changes for the revised guidelines and have no further comments in this regard.

In relation to industry codes, we would welcome these being acknowledged somewhere because they are established under each respective licence and have their own liability regime between parties. It is not clear how the calculated detriment takes account of these provisions, for instance the Connection and use of System Code (CUSC) includes arrangements for liability between parties. Without recognising and dovetailing these Codes within the guidelines, licensees could be in a position whereby the enforcement case is compounded and so be at risk of disproportionate settlements, because the licensee, in this event would need to resolve the case with Ofgem and the industry stakeholder(s) affected by the relevant industry code too. Alongside this where an automatic funding adjustment mechanism exists in the licenses, this should also clearly be factored into the enforcement arrangements as this is a de facto form of penalty.

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

The Sectoral Penalty Statement is fit for purpose and so we have no further comments on this.